FINANCIAL INDUSTRY REGULATORY AUTHORITY
OFFICE OF HEARING OFFICERS

DEPARTMENT OF MARKET REGULATION, Complainant, v. PAUL CHARLES DOTSON (CRD No. 2314498), Respondent.	Disciplinary Proceeding No. 20090208031-02 Hearing Officer—LOM **HEARING PANEL DECISION** August 7, 2015

Market Regulation failed to prove by a preponderance of the evidence that Respondent, the third tippee in a chain of alleged tipper-tippees, engaged in insider trading in violation of Section 10(b) of the Securities Exchange Act, Rule 10b-5, and FINRA Rules 2020 and 2010. The First Cause of Action is dismissed.

Market Regulation failed to prove by a preponderance of the evidence that Respondent's conduct constituted a stand-alone violation of FINRA Rule 2010. The Second Cause of Action is dismissed.

Appearances

Edwin T. Aradi, Esq., Department of Enforcement, Christian J. Cannon, Esq., and James J. Nixon, Esq., Department of Market Regulation, Rockville, Maryland, representing Complainant.

John J. Kenney, Esq., John P. Curley, Esq., Jason D. Burns, Esq., Marc A. Melzer, Esq., of Hoguet Newman Regal & Kenney, LLP, New York, New York, representing Respondent.

I. INTRODUCTION

A. Charges

Respondent, Paul Charles Dotson ("Dotson" or "Respondent"), is a New York based equities trader in Canadian oil and gas stocks who is registered with FINRA[1] through his firm,

[1] FINRA is the Financial Industry Regulatory Authority, which is responsible for regulatory oversight of securities firms and associated persons who do business with the public. FINRA's Rules are available at www.finra.org/industry/finra-rules.

TD Securities (USA) LLC (together with its Canadian affiliates, "TD" or the "Firm"). FINRA's Department of Market Regulation ("Market Regulation") has charged Dotson with insider trading (First Cause of Action) in violation of Section 10(b) of the Securities Exchange Act, Rule 10b-5, and FINRA Rules 2020 and 2010. Market Regulation has also separately charged him with a stand-alone violation of FINRA's ethical conduct rule, FINRA Rule 2010 (Second Cause of Action). Market Regulation alleges that Dotson fraudulently traded on material non-public information he received as a remote tippee in an alleged tipper-tippee chain. Market Regulation seeks to bar Dotson in all capacities and argues that he is not fit to remain in the securities industry.

The charges against Dotson relate to a telephone call that he received before the markets opened on Tuesday, March 31, 2009. In that call, an oil and gas analyst with Dotson's Firm told Dotson that he had information from someone who worked at a Canadian oil and gas company, Canadian Natural Resources ("CNQ"). The information was that there was a "buzz" within CNQ that the company was looking at acquiring another Canadian oil and gas company named Nexen, Inc. ("Nexen"). The analyst also told Dotson that CNQ was halting employee trading in the company's stock around April 14 or 15, which the analyst characterized as "rare" and "odd."

According to Market Regulation, Dotson reacted by taking an unusual action. Within 35 minutes of the call he sought permission from his supervisor to take a $1.8 million long position in Nexen for a proprietary account. But Dotson's primary responsibility was to facilitate customer trading by buying and selling in anticipation of customer demand, not proprietary trading.

Market Regulation infers from what it characterizes as the unusual nature of Dotson's action that Dotson thought that he had material non-public information that gave him a trading advantage when he traded Nexen shares. Dotson ended the trading day of March 31, 2009, with slightly more than 100,000 shares of Nexen. That position was transferred from the Firm's facilitation account to the Firm's proprietary account and later sold at a profit.

B. Hearing Panel Conclusions

Although Market Regulation presents a vivid narrative, its narrative fails to consider all the facts and circumstances. The full record, as more fully discussed below, presents a different and more nuanced picture.

In brief, the Hearing Panel finds that the analyst conveyed only a vague rumor to Dotson. It was the equivalent of "water cooler talk." It did not rise to the level of material non-public information. Dotson and others realized at the time that the employee trading blackout was a standard blackout before the company issued its quarterly earnings report. Furthermore, the rumor was no secret. It was widely circulating in the market, as Dotson knew before he traded. In fact, the original source of the rumor was a gas plant operator located in a backwoods field office who alleviated his isolation by gossiping on the telephone with a childhood friend about

the industry. There is no evidence that he had access to CNQ's confidential information or acquisition plans, and the rumor he started turned out to be false.

Even if the rumor had constituted material non-public information, the Hearing Panel finds that Dotson did not have the scienter required to hold him liable for securities fraud. Scienter requires more than the mere receipt of inside information—it requires that a person know or have reason to know that the initial "tip" was an improper breach of a duty of trust and confidence. Dotson knew nothing about the initial "tip" or the tipping chain. Furthermore, his trading was not as unusual as Market Regulation paints it and is insufficient to establish scienter.

The Hearing Panel concludes that Market Regulation failed to prove by a preponderance of the evidence that Dotson engaged in unlawful insider trading. The Hearing Panel also concludes that Market Regulation failed to establish that Dotson violated FINRA's ethical conduct rule.

II. BACKGROUND

A. Investigation

TD discovered that its employees had been discussing among themselves, and with clients and others, a possible CNQ-Nexen merger based on a rumor from inside CNQ. This information came to TD's attention on April 1, 2009, the day after the trading at issue, when the compliance department of one of TD's clients contacted TD compliance personnel regarding an email the client had received on March 31, 2009, discussing the potential for a CNQ-Nexen merger.[2]

With the assistance of outside counsel at Davis, Polk & Wardwell, TD conducted an investigation. TD self-reported the matter in mid-April 2009 to FINRA and the New York Stock Exchange Regulation Group ("NYSER"), as well as other regulatory and governmental bodies. TD reported in detail to NYSER about the analyst's conversations with TD employees regarding the rumor. It also reported on conversations those TD employees had with outsiders concerning the CNQ-Nexen rumor. TD reported its conclusions regarding any trading done in CNQ or Nexen by people who had heard the rumor from a TD employee. Because some of the TD employees involved were not subject to NYSER's jurisdiction but were subject to FINRA's,

[2] CX-46, at 6-7. An exhibit is referred to here by a prefix indicating which party initially proposed it and the exhibit's unique identifying number. With respect to transcripts of audio recordings, the Parties have agreed on corrections and the corrected versions are indicated by the suffix "A." Thus, a Market Regulation exhibit is CX-2A, which is the audio and corrected transcript of the telephone call between Dotson and the analyst in which Dotson is alleged to have received material non-public information. A Dotson exhibit is RX-39, which is a transcript of a telephone call the morning of March 31, 2009, in which the participants discuss the rumor "coming out of Calgary" that CNQ might acquire Nexen.

NYSER referred the matter to FINRA's Office of Fraud Detection and Market Intelligence in September 2009.[3]

FINRA staff reviewed the NYSER file, conducted a further investigation, and took the testimony of Dotson in an on-the-record interview ("OTR"). FINRA staff also spoke informally with some of the people involved in the relevant conversations.[4]

B. Discipline Imposed By The Firm

Based on the findings in its investigation, the Firm disciplined several employees, including Dotson. In April, four employees were suspended. In June, the analyst who relayed the rumor to Dotson was terminated for cause, and the person who had told the analyst about the rumor resigned. On July 9, 2009, TD informed FINRA it had finalized its disciplinary decisions with respect to a larger group of persons and was preparing a remediation plan that it intended to forward to regulators.[5]

With respect to Dotson, the Firm determined that he had failed to follow its Code of Conduct and its policies and procedures for dealing with potential material non-public information. The Firm's Code of Conduct and its policies and procedures prohibit insider trading and give guidance on what constitutes material non-public information. To assist in avoiding improper insider trading, the policies and procedures require a TD employee who comes into possession of what might be material non-public information to contact a member of the compliance group at the Firm.[6]

The Firm concluded,

> [Y]ou [Dotson] knew that the information in question apparently came from a source within CNQ, yet you failed to consider whether that fact made it inappropriate to trade on the basis of, use or otherwise convey the information further….[Y]ou should have consulted with compliance upon receiving this information, but you failed to do so.[7]

[3] Hearing Tr. (Benko) 142-43; Hearing Tr. (Kirwan) 598-99; CX-43; CX-50. References to the hearing transcript are cited here as "Hearing Tr.," with a parenthetical for the last name of the witness whose testimony is cited and the page number of the transcript. Thus, Dotson's testimony is cited "Hearing Tr. (Dotson) 363."

[4] Hearing Tr. (Kirwan) 598-616.

[5] CX-46, at 8; Hearing Tr. (Benko) 152-53.

[6] CX-57; CX-58.

[7] CX-61.

Thus, the Firm suspended Dotson for three months and reduced his compensation by $215,000.[8]

C. Procedural History

Market Regulation filed and served its Complaint on February 25, 2014. After an extension of time, Dotson filed his Answer on May 7, 2014. Dotson filed a motion for summary disposition on September 19, 2014. Market Regulation filed its opposition on October 17, 2014. The Hearing Officer denied the summary disposition motion on December 9, 2014.

The hearing took place over the course of three days (January 26, 28-29, 2015). The Hearing Panel heard videotaped testimony, telephone testimony, and testimony from witnesses who appeared in person at the hearing.[9] The Hearing Panel also listened to audio recordings of telephone conversations that occurred at the time of the events at issue, and the audio recordings and transcripts have been entered into evidence. These include an audio recording of the conversation between the analyst and Dotson and audio recordings in which Dotson and others discussed the rumor about CNQ and Nexen throughout the same day. Additional exhibits such as emails were also admitted into evidence. The Parties filed simultaneous post-hearing briefs on March 26, 2015.[10]

III. FACTS

A. Respondent

At the time of the events at issue, Dotson was an equities trader registered through a FINRA member firm, TD. He was located in New York, but reported to the Firm's trading desk in Toronto, Canada. Dotson specialized in Canadian oil and gas companies, and spent most of his time buying and selling such securities in a facilitation account to accommodate the Firm's customers' liquidity needs.[11]

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[8] CX-61.

[9] The following people in addition to Dotson testified at the hearing: Scott MacNicol ("MacNicol") (by videotape; transcript in CX-66), Dotson's boss, who authorized the long position in Nexen; Christopher Rankin ("Rankin") (in person), a financial analyst at TD, whose specialty was mergers and acquisitions; Roger Serin ("Serin") (in person), who was an oil and gas analyst for TD at the time of the events in issue; Kitty Benko ("Benko") (by telephone), vice president of human resources at TD; and Jacqueline Kirwan ("Kirwan") (in person), regulatory analyst with FINRA's Office of Fraud Detection and Market Intelligence.

[10] The briefs were entitled as follows: Department of Market Regulation's Post-Hearing Submission ("Mkt. Reg. PH Br."); Respondent's Post-Hearing Brief ("Resp. PH Br.").

[11] Hearing Tr. (Dotson) 172, 174-75, 191-94; CX-1, at 5, 8. TD acted as a branch office of an affiliate called TD Securities Inc., a Canadian entity headquartered in Toronto. CX-66, at 4. For purposes of this decision, a reference to TD or the Firm includes both the Canadian company and the U.S. company.

Today, Dotson still specializes in Canadian oil and gas companies for the Firm. A couple of years after the events at issue, he was promoted, and he currently is co-head of TD's New York trading desk.[12]

B. Jurisdiction

Dotson was registered at the time of the alleged misconduct and at the time Market Regulation filed and served its Complaint. He is still registered today. FINRA has jurisdiction for purposes of this proceeding pursuant to Article V, Section 4 of FINRA's By-Laws.

C. Context For Dotson's Trading In Nexen

(1) The Firm's Facilitation And Proprietary Accounts

Dotson was one of the people with trading authority for an omnibus facilitation account referred to as the TC account (here called the "TC Facilitation Account"). He was responsible for the oil and gas component of the TC Facilitation Account. The TC Facilitation Account, like the Firm's other facilitation accounts, was budgeted to lose money on trading. The Firm used the facilitation accounts as a service to assist customers. If customers had interest in a stock, the Firm sold them the stock from the facilitation account. Conversely, if customers were selling a stock, the facilitation account would buy from them.[13] Generally, trades in the facilitation accounts were in-out positions that were held for a day or two.[14]

If the market was volatile and it became difficult to move in and out of a position within a day or two at a price that kept the Firm's loss in a facilitation account within its budget, then the Firm would pursue a more long-term trading strategy in the facilitation account. Thus, on occasion the Firm did both facilitation and proprietary trading in the TC Facilitation Account.[15]

In January 2009, the Firm established a separate proprietary account referred to as the TS account ("TS Prop Account"). One of Dotson's bosses, Scott MacNicol, who was then the managing director of institutional equities for TD, was put in charge of that proprietary account.[16] The Firm uses its own capital for this and its other proprietary accounts. Generally, in proprietary accounts the Firm would take positions for longer periods of time, ranging from three to four days, or three to six months, or even a couple of years.[17] Dotson had authority to trade in the TS Prop Account inventory.[18]

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[12] Hearing Tr. (Dotson) 172.

[13] Hearing Tr. (Dotson) 278.

[14] Hearing Tr. (Dotson) 191-93.

[15] Hearing Tr. (Dotson) 193-95, 197-99.

[16] CX-66, at 5-6, 9.

[17] CX-66, at 31.

[18] Hearing Tr. (Dotson) 206-08.

Although Dotson did 95% of his business as facilitation trading,[19] it was not unusual for him to trade for proprietary accounts. Dotson testified that prior to the events at issue he might trade and hold positions for a proprietary account fifteen to twenty times a year.[20] Those positions generally were made in a facilitation account and later transferred to a proprietary account.[21]

Dotson testified that he had previously traded in Nexen and transferred shares to a proprietary account. He described how he had acquired 32 million shares of Nexen from Ontario Teachers in three tranches over thirty months and then transferred some of those shares into a proprietary account.[22] Dotson also testified that he had previously traded shares for the particular proprietary account involved here, the TS Prop Account. He said that the week before the trading at issue here he had traded other Canadian oil and gas stocks for the TS Prop Account.[23]

(2) Dotson's Typical Day

Dotson testified about his typical work day. He described a noisy and chaotic environment. He multitasks constantly, listening to CNBC with a headpiece, monitoring five screens in front of him, listening to all the conversations at the desk in Toronto on a speaker, and also listening to television news on another speaker. At the same time he reads through publications, and looks at charts and earnings calendars. He reads the Wall Street Journal, New York Times, Financial Times, and three other newspapers. He monitors 300 stocks in Canada and the United States, checking for price updates. He also might be trading currency as well as stocks, because trades are settled in U.S. dollars, Canadian dollars, and British pounds.[24]

Dotson is constantly on the telephone as he multitasks. During the relevant period, he ordinarily spoke to his boss, MacNicol, between fifteen and twenty times a day.[25]

Dotson arrives at work at 7 a.m. and generally participates in a 7:10 a.m. meeting by telephone, sitting at his desk. He then participates in a 7:30 a.m. general research meeting in the

[19] Hearing Tr. (Dotson) 208.

[20] Hearing Tr. (Dotson) 392-94.

[21] Hearing Tr. (Dotson) 193-95, 205-08, 427; Hearing Tr. (Rankin) 72, 74-75; CX-66, at 29-30. Dotson testified about a Nexen-related call with his boss and others in which the group also discussed a long position in an airline simulation company that had been on the facilitation book for three months. They discussed moving that long position from the facilitation account to the proprietary book. The discussion arose because the proprietary book was still getting "up to speed." Hearing Tr. (Dotson) 542-43.

[22] Hearing Tr. (Dotson) 199-200.

[23] Hearing Tr. (Dotson) 200-03.

[24] Hearing Tr. (Dotson) 430-36.

[25] CX-66, at 5.

same way. He reads publications and multitasks during these telephone calls.[26] The period between 8 a.m. and 9:15 a.m. is the busiest period of his day.[27]

Dotson received the telephone call regarding the rumored CNQ acquisition during the busiest part of his ordinary day. And that particular day he was exceptionally busy because his assistant was out that week. As a result, Dotson was doing his assistant's work as well.[28]

(3) Canadian Oil And Gas Sector At The Time Of Dotson's Trading

a. *Turmoil In The Market*

In late 2008 and early 2009, the Canadian oil and gas sector was a small community. It was composed of approximately nine major companies.[29] The major Canadian companies that figure in the evidence in this case are CNQ, Suncor, UTS, Talisman, Petro-Canada, Canadian Oil Sands, and Husky.[30]

The sector was in turmoil because the price of oil had dropped from a high of $140 or more per barrel to a low of around $35. Rankin, a TD financial analyst specializing in mergers and acquisitions, testified that it cost around $45 a barrel to extract the oil plus $10 in royalties. Thus, oil producers were paying $55 a barrel but the commodity price was $35 a barrel.[31]

Dotson explained that the situation generated speculation about potential mergers: "[T]he minute the commodity comes under great pressure … [the market in Canadian oil and gas company stock] begins to trade as if it was an emerging market, meaning high volatility, talk of bankruptcies, talk of those types of things …. [A] lot of the conversations revolve around who can survive, who needs to do a transaction, who is capable of being an acquirer and who are the candidates for being acquired."[32]

Rankin testified that credit was tight at the same time that the oil companies were "hemorrhaging" money. This led some companies that were cash short to consider the acquisition of other companies with more liquidity to improve their balance sheets. He said that consolidation in the industry was compelled by such financial concerns rather than the purchase

[26] Hearing Tr. (Dotson) 430-36.

[27] Hearing Tr. (Dotson) 441-42.

[28] Hearing Tr. (Dotson) 437.

[29] Hearing Tr. (Rankin) 89, 94-95, 105-06; CX-66, at 11.

[30] Hearing Tr. (Rankin) 89-90, 94-95; Hearing Tr. (Dotson) 416-17, 440, 538-39; CX-66, at 11.

[31] Hearing Tr. (Rankin) 78-80; Hearing Tr. (Dotson) 416.

[32] Hearing Tr. (Dotson) 416-17.

of cheap assets.[33] According to Rankin, Suncor and CNQ were the "majors" that were running out of money.[34]

Rankin began developing an idea for a trade. Based on his financial analysis of companies in the Canadian oil and gas sector, he concluded that it made sense to buy Suncor and short CNQ. He testified in detail how CNQ had a balance sheet problem that needed to get fixed, and one way to fix it was to acquire another company. Rankin began a draft memorandum setting forth his thinking, which he circulated to TD's equity sales and trading personnel prior to the opening of the markets on Monday, March 23, 2009.[35]

b. *Suncor/Petro-Canada And Total/UTS Transactions*

On Monday, March 23, 2009, Suncor publicly announced that it was buying Petro-Canada. At the same time, Total, a French company, was in the process of pursuing a takeover offer for UTS.[36]

The Suncor and Total transactions increased speculation regarding other potential mergers.[37] Although Nexen had been the subject of rumors for a long time,[38] speculation regarding that company intensified.[39] The day the Suncor/Petro-Canada deal was announced, an article ran in Reuters discussing the possibility of CNQ and Nexen doing a deal.[40]

Rankin testified that people trading in the market were trying to figure out what other people in the market were thinking and how they were likely to trade:

> [E]verybody is looking at this market, it's going crazy, but not in a good way, it is all ugly, everything was down, and all of a sudden Suncor buys Petro-Canada and people think, okay, can there be more consolidation, and regardless of whether or not there is, it's a question of what stocks do you trade in anticipation of other people thinking about this.[41]

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[33] Hearing Tr. (Rankin) 78-81.

[34] Hearing Tr. (Rankin) 80.

[35] Hearing Tr. (Rankin) 82-86; CX-28.

[36] RX-4; RX-9; RX-12; RX-23; Hearing Tr. (Dotson) 221.

[37] Hearing Tr. (Dotson) 216, 423-26; Hearing Tr. (Rankin) 80-81; CX-66, at 10-11; RX-23.

[38] CX-66, at 11-12.

[39] Hearing Tr. (Dotson) 209-10, 220-22, 444-45; RX-15.

[40] Hearing Tr. (Dotson) 217-19; RX-12.

[41] Hearing Tr. (Rankin) 91.

[41] Hearing Tr. (Rankin) 91.

On Tuesday, March 24, 2009, news was circulating in the market about an investment bank's marketing trip to Nexen the preceding week. TD employees and others learned that Nexen had told the investment bank that it had received unsolicited calls from five multi-national oil companies expressing interest in Nexen. The investment bank note on the visit with Nexen said that "we believe that there is a good possibility that [Nexen] could be the next one to go."[42]

Neither the Suncor acquisition of Petro-Canada nor Total's bid for UTS was then certain to close. The Suncor deal could have fallen through because of regulatory complications,[43] and the takeover bid by Total also might have failed. Its bid for UTS was due to expire Monday, March 30, 2009. Although Total might extend or increase its bid for UTS, it also might walk away. Some people thought that the failure of one of these transactions to close would increase interest in Nexen as the next takeover target.[44]

Total extended its offer for UTS,[45] and the Suncor/Petro-Canada transaction proceeded.[46]

c. *Dotson's Trading In Nexen And CNQ Before The Events At Issue*

Dotson traded Nexen almost daily, along with other Canadian oil and gas stocks. TD was known to rank number one in trading volume of Nexen shares.[47]

In the first quarter of 2009, there was constant takeover talk in connection with Nexen. However, from August 2008 through February of 2009, Dotson and TD were precluded from taking a long position in Nexen for the Firm because the Firm was handling a stock buy-back for Nexen. During this period TD took positions in Nexen for one or two days at a time for the purpose of facilitating customer trading. It was not until March 1, 2009, that TD could again take a long position in Nexen for its own account.[48]

Dotson traded CNQ as much as he traded Nexen. For that reason, information about CNQ was important to him even apart from any rumor about a CNQ and Nexen combination.[49]

d. *Unusual Trading In Nexen*

On Friday, March 27, 2009, Nexen outperformed other Canadian oil and gas stocks in trading. Its price went up while the price of other shares in the sector declined. The volume of

[42] RX-15; CX-30; CX-33; Hearing Tr. (Dotson) 223-25, 229-30.

[43] Hearing Tr. (Rankin) 86-88.

[44] Hearing Tr. (Dotson) 445-46; RX-19; CX-66, at 12-13, 28-29.

[45] Hearing Tr. (Dotson) 252.

[46] Hearing Tr. (Rankin) 87-88.

[47] Hearing Tr. (Dotson) 209.

[48] Hearing Tr. (Dotson) 213-14.

[49] Hearing Tr. (Dotson) 323.

trading in Nexen also was unusually high. The Nexen trading appeared to reflect the market's view that Nexen might be the next acquisition target.[50]

Dotson observed the unusual trading in Nexen. He also noted the identity of the buyers. He found it significant that they were "fundamental" accounts.[51]

Dotson explained that "fundamental" accounts are mutual funds and pension funds that are required to maintain a certain percentage of their assets in Canada.[52] The strategy for Canadian fundamental investors, who run public money, is to track and beat the relevant benchmark but not beat it by a significant amount, because beating the benchmark by a large amount would mean that the fund was taking undue risk. To do that, a fundamental account generally maintained the same "weight" in energy companies as the "weight" in the benchmark index. However, within the subgroup of energy companies a fundamental account might go "overweight" or "underweight" in particular companies.[53]

Dotson thought that the fundamental accounts were heavily buying more Nexen because they anticipated a potential acquisition of Nexen. They wanted to increase their holdings, having failed to anticipate Suncor's acquisition of Petro-Canada and having been "underweight" in Petro-Canada.[54] Dotson thought that the trading was based on the report from the investment bank and the anticipated expiration of Total's bid for UTS the next Monday.[55]

The trading in Nexen by the fundamental accounts was unusual, so Dotson sent emails about it to other people. He also received emails asking what was going on with Nexen.[56] Dotson told others who noticed the unusual trading that there was a "lot of takeover chatter."[57]

D. Original Alleged Inside Tip From Gas Plant Operator (Alleged Tipper) To Childhood Friend (First Tippee)

The conversation that started the alleged tipper-tippee chain occurred on Monday, March 30, 2009, the first trading day after the unusual Nexen trading the previous Friday.[58]

AA was the original alleged tipper in the chain leading to Dotson. AA was a field technician and gas plant operator for CNQ. He worked at a remote location in the backwoods of

[50] Hearing Tr. (Dotson) 227-28, 231-34; 449-50; CX-34; RX-22.

[51] Hearing Tr. (Dotson) 233-34.

[52] Hearing Tr. (Dotson) 403.

[53] Hearing Tr. (Dotson) 408-11.

[54] Hearing Tr. (Dotson) 412-15.

[55] Hearing Tr. (Dotson) 230-31; RX-33.

[56] Hearing Tr. (Dotson) 444-50, 455-58.

[57] Hearing Tr. (Dotson) 448-49; RX-21.

[58] Hearing Tr. (Benko) 151-52; CX-46, at 5.

northern British Columbia. That field office was between 750 and 1000 miles from Calgary, where CNQ's headquarters were located. AA would work for two weeks, seven days a week, and then return to "civilization" for a couple of weeks.[59] Because he craved human contact while he was at the remote site, he would spend time talking to friends by telephone.[60]

One of the people with whom AA had such conversations was a childhood friend BH.[61] At the time, BH worked at TD researching the oil and gas industry. AA and BH were accustomed to gossip about the industry and regularly traded information and speculation regarding the Canadian oil and gas sector.[62]

BH was the first alleged tippee in the alleged tipper-tippee chain. During the March 30 telephone call, AA and BH discussed the merger of Suncor and Petro-Canada that had been announced the previous week. Then they talked about CNQ.[63]

AA told BH that there were rumors within CNQ about a transaction with a company called "Occidental." AA conveyed his belief that "Occidental" was a reference to a California company named California Occidental.[64]

BH told AA that he thought the reference was to a Canadian company called Nexen, which had been known as Canadian Occidental. BH thought the pairing of CNQ and Nexen was plausible. He thought the California company was too large for CNQ to acquire.[65]

AA also told BH that he had received an email saying that CNQ was imposing an employee trading "blackout" period during which CNQ employees could not trade company stock. The blackout was scheduled for April 14 or 15, 2009. AA forwarded BH the email, but BH did not forward the email to anyone else at TD. He later told the Firm's investigators that it looked like a standard blackout email related to the timing of earnings results.[66]

BH did not view AA as having a position that would give him knowledge of merger activity. He understood that AA was a technician who was in a remote location where he had little contact with people.[67]

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[59] Hearing Tr. (Benko) 154-56; Hearing Tr. (Serin) 380-82; CX-46, at 3.

[60] Hearing Tr. (Benko) 165.

[61] Hearing Tr. (Benko) 144.

[62] Hearing Tr. (Rankin) 76-77; Hearing Tr. (Benko) 156-57; Hearing Tr. (Kirwan) 603-07.

[63] CX-46, at 5.

[64] CX-46, at 5.

[65] CX-46, at 5.

[66] CX-46, at 5.

[67] Hearing Tr. (Benko) 165.

Benko, the TD vice president of Human Resources who attended the BH interview during the Firm's investigation, had an impression of the conversation between AA and BH as a casual chat between friends. She described the discussion of CNQ as speculation that was consistent with the speculation generally in the marketplace about other potential mergers following the Suncor/Petro-Canada transaction. She was quite firm that AA received nothing in exchange for the information conveyed about CNQ.[68]

The Hearing Panel finds that AA and BH discussed a rumor. AA told BH that there was *talk*—generally and without further specifics—at CNQ of a potential acquisition. He did not tell BH that the company had any confidential intention, plan, or activity in process. Nor did he tell BH that he had heard the rumor from someone within the company who had access to the company's confidential information. Consistent with a discussion of a rumor, the two friends were unsure of the potential target that was the subject of the rumor and speculated that it might be either a California or a Canadian company. The conversation was much like any other conversation speculating on take-over possibilities in the Canadian oil and gas sector.

AA, the gas plant operator, did not have the kind of position that lent credibility to his mention of a potential transaction. He was far removed from CNQ's confidential strategies, plans, and activities. Even his alleged immediate tippee, BH, did not believe that AA was in a position of special knowledge or special access to confidential information. AA was not actually an insider with access to material non-public information.[69]

E. Conversation Between Childhood Friend And Analyst (Second Tippee)

The next morning, Tuesday, March 31, 2009, BH arrived at work as usual around 5:30 a.m. The TD oil and gas analyst with whom he worked, GH, was already at his desk.[70]

The two of them had joined TD together less than six months before. GH was an engineer who had previously evaluated oil reserves as assets. For TD he was gathering data on the oil and gas industry to prepare a report on assets that could be used for long-term trading strategies. BH was his research associate.[71]

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[68] Hearing Tr. (Benko) 148-152, 154-57, 163-65.

[69] From time to time, AA also gave BH information regarding CNQ's activities by email, and at least once BH relayed the information to others by email in circumstances showing an effort to conceal the source. CX-31; CX-32. When TD investigated the events at issue, it reviewed this email correspondence and concluded that the email contained a mix of information that might be broadly construed as public information with a few private details. CX-46, at 4.

Regardless of whether AA improperly disclosed inside information in the email, that information did not make its way to Dotson and is not part of the alleged tip in this case. The email does offer some evidence that the relationship between AA and BH was one in which the two traded information, including possibly confidential information, about the oil and gas industry.

[70] Hearing Tr. (Benko) 160.

[71] Hearing Tr. (Rankin) 76-77; Hearing Tr. (Dotson) 254; Hearing Tr. (Serin) 372, 382-83.

BH told GH, the analyst, about the rumor he had heard. He also told GH about the blackout period for trading CNQ securities.[72] When he told GH the rumor, BH speculated that the rumor was about Nexen.[73] This portion of the rumor came from BH, not from within CNQ.

When TD and its outside law firm later conducted their investigation, they concluded that the conversation between BH and GH was a casual discussion of a rumor. Benko, the TD vice president of Human Resources who participated in the investigation, summarized their conclusions.

> [BH] came in and stopped at [GH's] office and said, hey, you know what, I was talking to a friend last night who happens to work for CNQ and he was telling me some buzz that's going around his company, do you think there's anything to it, and so then [GH] and [BH] were batting back and forth with this information, what it might have meant, is there any validity to it and that sort of stuff.[74]

The analyst then began conveying the information he had heard from BH to others in the Firm's various offices. His call to Dotson was one of these conversations.[75]

F. Conversation Between Analyst And Dotson (Third Tippee)

The analyst called Dotson around 8:30 a.m. on Tuesday, March 31, 2009.[76] This was during the busiest part of Dotson's day, not long before the markets opened. When Dotson spoke to others later in the day, he told them that he could not hear everything on the call.[77]

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[72] CX-46, at 5.

[73] Hearing Tr. (Benko) 162.

[74] Hearing Tr. (Benko) 160-61.

[75] CX-46, at 6-7.

[76] CX-2A. All quotations from the telephone conversation are to the revised transcription of the audio file. The Hearing Panel listened to the audio file at the hearing.

[77] Hearing Tr. (Dotson) 309; CX-12.

After GH and Dotson greeted each other, the first portion of the conversation went as follows. It is this portion of the conversation that contains the alleged material non-public information.

> GH: Hey, just wanted to give you the heads up we had uh this morning we heard through somebody that works at CNQ that they are uh looking at acquiring Nexen.[78]
>
> DOTSON: Really?
>
> GH: So it sounds like CNQ is dropping uh all uh all halting on CNQ stock by CNQ employees as of April 14th or 15th. Which is rare and odd.
>
> DOTSON: They're dropping what? They're dropping?
>
> GH: They're dropping—they're putting a hold on trading CNQ.
>
> DOTSON: Oh, okay, okay.
>
> GH: And so looking at the dates when they report, they report on May 8th, so it is a little early to be relating to quarter. But it could be uh but CNQ staff are just saying or we heard from one fellow that uh there is quite the buzz within the organization that they're acquiring somebody and the name Oxy is going around. Which is of course the old name for Nexen.

Notably, GH told Dotson that there was a "buzz" within CNQ—the equivalent of a rumor or "water cooler talk." GH did not tell Dotson that there was any specific activity, study, negotiation, or plan. Nor did GH say that the rumor had any particular source within the company who would have special knowledge of any acquisition plans. GH said nothing about the gas plant operator who was the original source of the rumor. Furthermore, GH told Dotson that the "buzz" was going around the company. He did not characterize it as a secret or confidential.

With respect to the blackout on employee trading in CNQ shares, although GH said that it was "rare" and "odd," that was GH's interpretation of the information—not something from inside CNQ. GH indicated that it was an interpretation when he acknowledged that the trading blackout "could be" just an ordinary blackout.

[78] In the revised transcription of the audio file, the transcript mistakenly attributes this portion of the conversation to Dotson. In context, it is clear that it is GH talking.

The conversation continued with a discussion of the potential synergy between CNQ and Nexen. Dotson and GH speculated that CNQ might want to spin off some assets to Total. GH commented at the conclusion of that discussion:

> GH: So I would say this isn't, uh you know, definitely not confirmed at this point.

Dotson then talked about the unusual trading in Nexen that he had seen on the preceding Friday. He called it "weird." He said that Nexen's stock price was up 3% when everything else was down. He talked about how there were multiple buyers that Friday and that he had fielded many questions from customers and others. However, he noted, "I get this a lot and then nothing happens."

GH then repeated that the rumor was not a sure thing, saying,

> GH: Yeah. Well I wouldn't say this is at this point and I wouldn't say it's uh strongly substantiated.
>
> DOTSON: Right, right.
>
> GH: You can keep it on your radar. If you hear anything independently from this, then let me know because uh you know there is often some uh some smoke or there's fire where there's smoke.
>
> DOTSON: Right. Right. Okay. I will. Thank you.

The two said good-bye and ended the call.

In the last portion of the conversation, GH emphasized the uncertainty of the information. He also asked Dotson to let GH know if he heard any information from another source about the possible acquisition.

Dotson testified that the information regarding the blackout period for employee stock trading did not strike him as rare or odd. In his view, the dates discussed were within the standard window before an earnings announcement.[79]

The Hearing Panel finds that when the information was passed to Dotson it was described as a rumor. GH did not tell Dotson that the information came from any particular source and did not indicate that the source of the information had any special access to CNQ's acquisition plans or strategies. GH told Dotson nothing about the relationship between the gas plant operator and the childhood friend. GH described the rumor as uncertain information and sought Dotson's

[79] Hearing Tr. (Dotson) 464-68.

agreement to let him know if he heard independently something that would lend more substance to the rumor.

G. First Conversation Between Dotson And His Boss

Dotson called his boss, Scott MacNicol shortly afterward, at approximately 8:48 a.m., before the markets opened.[80] This was the first call the two had had since MacNicol had returned from a two-week vacation. During this call, Dotson did not request permission to take a position in Nexen and did not treat the rumor as anything more than one piece of information among many.

Dotson began the conversation by filling MacNicol in on events that had occurred while MacNicol was away. Dotson talked about what happened after the Suncor/Petro-Canada merger was announced on Monday, March 23, 2009. He told his boss that Ranken had done some quick calculations and thought that CNQ would "probably have to do the same thing." He also told his boss that two names were discussed as possible acquisition targets, Nexen and Talisman.[81]

Dotson discussed the up-tick in Nexen stock price on the preceding Friday in comparison to the downward trend on other stocks. He said, "[I]t's just like stood out like a beacon on my screen, you know, up, up, up, up."[82] Dotson told his boss that he had had a long conversation with a senior TD manager who had spoken with Nexen's CEO, who also was curious about the trading in Nexen stock on the previous Friday.

Toward the middle of the conversation, Dotson mentioned his conversation with GH. He told his boss that he had gotten a call from GH who had reported that "the scuttlebutt in Calgary is that CNQ is really looking hard at Nexen."[83]

Dotson told his boss about the trading blackout, but he got the date wrong. He told MacNicol it was to begin April 10.[84] That date was earlier than Dotson had been told, and was therefore further from the May 8 earnings report and more unusual.

Even so, MacNicol discounted the blackout information as being connected to any acquisition plan. He said, "It's an unbelievable tell [as in signal] for management to give—a bunch of loose lips if that's indeed what it is."[85] Essentially, MacNicol expressed the view that it would make no sense to give advance notice of highly confidential information concerning an

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[80] CX-3A; CX-66, at 27. All quotations in the section below are to the revised transcript of the audio file. The Hearing Panel listened to the audio file at the hearing. Hearing Tr. (Dotson) 264.

[81] The corrected transcript for this conversation refers to Rankin as "Franken," and Talisman as "Tousman." CX-3A.

[82] CX-3A, at 4.

[83] CX-3A.

[84] CX-3A, at 4.

[85] CX-3A, at 4.

imminent merger to every employee in the company. CNQ had 7,000 employees.[86] MacNicol explained in his testimony that he did not believe that management would tell CNQ employees that they could not trade stock because of an impending merger for the reason that it is a "fast and loose environment" in Calgary. The market would gain insight by such a restriction on stock sales.[87]

Dotson then discussed how the rumor fit with Rankin's thesis, and the two men talked about various trades, long and short, they had in place on Suncor and Petro-Canada.

MacNicol told Dotson, "We're having a meeting tonight to talk about this trade." He invited Dotson, saying, "So why don't you at 4:30 we're going to sit down and go through every Tuesday at 4:30 we sit down with the three analysts and myself and these three guys and one of [a couple of other senior managers]." MacNicol explained, "Just to go through what positions we have, what positions we're looking at. And then you know, if it's something like I was going to call you this morning anyways, if we're going to deal with the oil, we'll get someone like you to come in." MacNicol asked Dotson to be prepared to talk at the meeting.[88]

Then the call ended.

The Hearing Panel observes that Dotson did not emphasize the information he learned from GH. The GH information was only mentioned after Dotson discussed at greater length events in the Canadian oil and gas marketplace and, in particular, the anomalous up-tick in Nexen stock the previous Friday. Dotson characterized the rumor as "scuttlebutt" from Calgary, an extremely vague description. Dotson and his boss discussed instead Rankin's suggestion that they go long Suncor and short CNQ and made plans to talk about their trades at the late afternoon meeting.

It is particularly significant that in this first call Dotson did not request permission to take a position in Nexen. Rather his boss asked Dotson to prepare to talk at a late afternoon meeting about a possible trade in light of the various factors he had discussed with MacNicol. Those factors included the rumor, but also Rankin's analysis and the unusual trading in Nexen the preceding Friday. There was no sense of urgency as there likely would have been if Dotson thought he had received a hot tip that would give him a trading advantage.

[86] Hearing Tr. (Dotson) 265-68.

[87] CX-66, at 15.

[88] CX-3A, at 6-7.

H. Dotson Asks GH For Further Analysis

Dotson enlisted GH to assist him in preparing for the afternoon call. In an email that morning, he asked GH to "do a little write up on CNQ's need to do a deal and synergies of assets."[89]

I. The Analyst Spreads Rumor

GH, the analyst, talked to others in addition to Dotson about the rumor that CNQ was considering acquiring Nexen. He told at least some of those people that the information came from inside CNQ.

In its investigation, TD identified six other TD employees in addition to Dotson with whom GH spoke about the rumor: SM, JPB, TW, TS, CR, and JD. The Firm then identified clients and other persons to whom the six passed on the rumor. The Firm found that the six TD employees had contacted a total of over 70 persons about the rumor. Among the people contacted were employees of dozens of different investment firms, hedge funds, and mutual funds.[90]

In sharing the rumor, at least one of the six persons GH told about the CNQ-Nexen rumor specifically identified it to others as coming from "insiders" at CNQ. The other five called it a rumor "out of Calgary." All of them emphasized that they were passing on a rumor.[91]

Dotson knew that GH was telling others what GH had told him. A salesman who sat near Dotson told Dotson that GH had spoken to him about the rumor. Because Dotson thought that salesman would not be a priority contact for GH, Dotson concluded that GH must be talking with all of the Firm's salespeople. That would include twelve to fifteen people in Toronto, three in Montreal, five in London, and the other people in New York.[92]

Dotson also knew that GH had spoken to TD's head of sales about the rumor. As a result, he expected that the sales force would be talking about the rumor with others. He noted that a rumor could be discussed as long as a balanced view was presented, discussing the reasons that it might be true and the reasons that it might not be.[93]

Notably, the rumor actually generated little in the way of trading. Of the fifteen or so firms SM informed of the rumor, only two traded in a manner that might appear suspicious. Others actually traded in a manner that appeared to discount the validity of the rumor, on the

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[89] CX-38; Hearing Tr. (Dotson) 281-83.

[90] CX-50.

[91] CX-50.

[92] Hearing Tr. (Dotson) 271-76, 470-74.

[93] Hearing Tr. (Dotson) 275-76. MacNicol also knew that GH was talking about the rumor with TD traders and salespeople and that there was a good deal of speculation regarding CNQ and Nexen. CX-66, at 8-9.

"wrong side of the market." Of the 27 clients JPB informed of the rumor, only one traded in CNQ and Nexen. JPB's client bought 3,900 shares of Nexen and sold short 2,800 shares of CNQ. TD deemed the trading by JPB's client de minimis. Of the approximately 40 clients TS informed of the rumor, none engaged in suspicious trading.[94]

J. Second Conversation Between Dotson And His Boss

Dotson called his boss a second time later the morning of Tuesday, March 31, 2009, around 9:07 a.m.[95] Dotson did so because he had learned that GH was talking to TD salesmen about the rumor and he knew that the salesmen would talk to their customers. Dotson thought it would cause some buying of Nexen stock. Dotson anticipated that he would be busier than normal in Nexen that day.[96]

Dotson recommended to his boss that they buy some Nexen stock and hedge it with another investment (in a basket of securities referred to as XEGs). He described the proposed trade as contingent on any consensus developed in the conference call scheduled for later that afternoon, saying "And then we can talk about the trade. And if it doesn't make sense to people, we'll just unwind it." MacNicol responded, "Okay, that's fine. Just put 100 on to start with and then we'll discuss it tonight."[97]

The Hearing Panel finds three things significant about this call.

First, the decision to trade was made only after the rumor had been widely distributed to TD salesmen, who were talking about it with their clients and spreading it even more widely. This undercuts the assertion that the rumor constituted material non-public information. At that point the rumor lost any quality of confidentiality it might have had, and Dotson was unlikely to believe that he was trading while in possession of material non-public information.

Second, Dotson and his boss viewed the initial position in Nexen as contingent, one that could be unwound if the discussion in the afternoon call led to a different consensus. Dotson did not press his boss to take and keep the position.

Third, Dotson's recommendation to purchase some Nexen stock was a response to anticipated market trading. It was not based on the likelihood of a CNQ-Nexen transaction.

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[94] CX-43; CX-50.

[95] CX-4A; Hearing Tr. (Dotson) 279. All quotations in the section below are to the revised transcription of the audio file. The Hearing Panel listened to the audio file at the hearing.

[96] Hearing Tr. (Dotson) 277, 475-76, 483-84.

[97] CX-4A.

K. The Analyst Tells Others That The Rumor Came From Inside CNQ

(1) The Analyst's Telephone Call With AC and SC

The morning of March 31, 2009, AC, a TD investment banker, and SC, a TD senior executive in the equity capital markets department, discussed the rumor with GH, the analyst. GH told them that the rumor came from CNQ staff on the operations side, not from finance. GH said that CNQ was "abuzz" with a "rumor of an acquisition." According to GH, a code name of "Oxi" was going around and that was believed to be a code name for Nexen.[98] AC and SC expressed skepticism about the code name.[99] Because Nexen had formerly been Occidental, the purported code name seemed too obvious if it was meant to conceal Nexen as the target of an acquisition.

SC also commented that the rumor was consistent with what he would expect all the companies in the sector to be doing in an effort to keep current on the market. He said, "[I]f you're running corporate development that's what you do … run a file on every company …."[100]

This call is significant in part for what AC and SC did afterward. Instead of treating the rumor as information that needed to be kept confidential in order to take advantage of it in trading, they called the CEO of Nexen and told him about the rumor. SC later told Dotson about the call and said that the CEO "appreciates the feedback. He was laughing just about how, you know these things happen and everything."[101]

The Hearing Panel also notes that senior managers at the Firm were discussing the rumor with Dotson without suggesting to him that he was restricted from trading. The conversation would have been different if they had thought that the rumor was material non-public information.

(2) The Analyst's Telephone Call With Rankin

In the early afternoon of Tuesday, March 31, 2009, GH and Rankin discussed the rumor in a telephone call, and GH told Rankin: "[S]o we heard this morning coming out of CNQ from internally at CNQ, is that they're looking at acquiring Nexen. So this is unsubstantiated at this point." GH characterized the rumor in the telephone call as "fairly credible."[102]

When Rankin was asked whether it raised any red flags for him that GH said the information was coming from inside CNQ, he testified that it did in "hindsight," but not at the

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[98] CX-13A, at 3.

[99] CX-13A, at 3; CX-46, at 5-7.

[100] CX-17A, at 5.

[101] CX-17A, at 3.

[102] Hearing Tr. (Rankin) 98-100; CX-5.

time.[103] Rankin said he wished he had realized the significance of saying the information came from CNQ "internally."[104] Rankin said that he "cringed" when he first heard the tape and heard GH say that the information was "internally" generated from CNQ.[105] He conceded, however, that he "absolutely … missed this." He went on to say: "[I]f I had been more on the ball, if I had realized what had just transpired, if I was not preoccupied with other stuff, I would have taken some action I would think, I would like to think I would have taken action."[106]

Rankin described the call with GH as "40 minutes of going through all of the possible permutations, the combinations of all sorts of different companies buying everybody because everybody is thinking about it." Rankin concluded that the fact that GH was telling him that CNQ was thinking about a possible combination with Nexen was "like telling me it's snowing outside," meaning that it was telling him something obvious.[107] Rankin said that the rumor was meaningless because "everybody was evaluating everything."[108]

The Hearing Panel notes that Rankin, like Dotson, was told that the rumor came from inside CNQ, but he likewise failed to recognize the significance of this statement. The Hearing Panel also notes that speculation about CNQ and Nexen was common.

(3) The Analysts's Other Calls Generally

The Firm reported to regulators that GH called a number of people within TD about the rumor. Although those calls might vary in detail, the Firm found that GH "generally conveyed … that the rumor was coming from inside CNQ, and/or that there was a blackout at CNQ."[109] Some of the TD employees who discussed the rumor with clients "explicitly stated … that the information came from an insider."[110]

The Hearing Panel finds that the market was awash with the same information—an unspecified employee of CNQ had indicated that a rumor was circulating at CNQ that the company was looking at an acquisition, and CNQ had notified its employees of an upcoming stock trading blackout. The Panel also notes that no one was treating that information as information that should be kept secret in order to take trading advantage of it.

[103] Hearing Tr. (Rankin) 98-100, 124-26.

[104] Hearing Tr. (Rankin) 99.

[105] Hearing Tr. (Rankin) 124.

[106] Hearing Tr. (Rankin) 99-100.

[107] Hearing Tr. (Rankin) 126.

[108] Hearing Tr. (Rankin) 125-26.

[109] CX-46, at 6.

[110] CX-46, at 7.

L. Doubts About The Rumor

A public report revealed that the CEO of CNQ was selling substantial amounts of CNQ stock during the same period that the CNQ-Nexen rumor was circulating. In late morning of Tuesday, March 31, 2009, MacNicol brought up the CEO stock sales in a telephone conversation with Dotson. MacNicol noted in that conversation that if CNQ was planning to do a deal with Nexen such trading would be unlawful.[111] MacNicol had talked with another TD executive who viewed the CEO's stock sales as evidence that CNQ was not considering the acquisition of Nexen. MacNicol told Dotson that the other executive had said "somebody might be taking a run at Nexen …. I just don't think it's CNQ based on that."[112]

GH also brought up the CEO stock sales in an email he sent Dotson. He told Dotson that the CEO had been selling shares recently "which would suggest nothing is in the works as he should be locked down."

Dotson responded by email that he "still would appreciate the synergies with CNQ or any other predator you could think of …."[113]

Dotson testified regarding this email exchange,

> [When news of the CEO's stock sales] comes out and [GH] asks me – he basically says to me I'm not going to do the write-up for you because it doesn't look like it is going to happen and I say to him I still want it, and the reason why I want it is because four months later if I hear the same rumor again, I have a file on it, I understand everything that's going on.
>
> A lot of what I do is [to] try to connect the dots ….

Dotson thought that the CEO's stock sales were not an absolute bar to a CNQ-Nexen deal. In other telephone calls in which the stock sales were discussed, Dotson reminded people that sometimes senior executives hold shares in a blind trust and the blind trust can trade even if the executive could not.[114]

The Hearing Panel finds it significant that GH—the person who allegedly tipped Dotson with material non-public information—seemed to view the CEO's sales of CNQ stock as definitive evidence that the rumor was wrong. Such doubt suggests that even GH viewed the information as no more than a rumor.

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[111] Hearing Tr. (Dotson) 313-14; CX-16.

[112] CX-16, at 3.

[113] CX-42, at 2; Hearing Tr. (Dotson) 315-17.

[114] CX-17; CX-19, at 2-3; CX-39; CX-66, at 20; Hearing Tr. (Dotson) 321-25.

M. Dotson's Trading In Nexen

Shortly after the Canadian market opened, at 9:31 a.m. on Tuesday, March 31, 2009, Dotson placed his first order to buy Nexen shares.[115] It was his intention to end the day 100,000 shares long in Nexen.[116] In the course of the day, he both bought and sold Nexen shares. He ended the trading day with a little more than 100,000 shares of Nexen.[117] He hedged the position, at least in part, with a basket of stocks referred to as XEGs.[118]

N. 4:30 p.m. Conference And Plan To Sell Nexen Before Its Earnings Announcement

Dotson attended the 4:30 p.m. conference call by telephone. The group discussed the CNQ CEO's stock sales, and Dotson suggested that the stock could have been in a blind trust that activated every quarter.

Then Rankin discussed at length his analysis, focusing on Suncor and CNQ.[119] He said that combining CNQ and Nexen did not create much value.[120] He noted that Nexen was trading down compared to the rest of the sector, and he speculated "that's probably why people were talking about it being an acquisition candidate right 'cause it is trading like a weak step-sister.'"[121] Rankin reiterated that Nexen was cheap.[122] Rankin concluded, however, that a "plain old" Suncor long position and XEG short position would be the "safe stable trade," not Nexen.[123]

In response, Dotson suggested replacing the Petro-Canada short position with a short position in the XEG basket of stocks.[124]

The conversation segued into a discussion of GH, the analyst who had been spreading the CNQ-Nexen rumor. The group commented that he did not understand how stocks trade, as opposed to the fundamentals of the oil companies. Dotson told the group that GH found Nexen "a little more attractive" than Rankin did. Dotson told the group to talk to GH if they wanted to

[115] Hearing Tr. (Dotson) 289-91; CX-6.

[116] Hearing Tr. (Dotson) 243, 500-03.

[117] Hearing Tr. (Dotson) 291-306, 491-503; CX-7; CX-8; CX-9; CX-11; RX-97.

[118] Hearing Tr. (Dotson) 311-12.

[119] CX-19A.

[120] CX-19A, at 13.

[121] CX-19A, at 23.

[122] CX-19A, at 24.

[123] CX-19A, at 25.

[124] CX-19A.

get a sense of his view. Dotson then reported that he had bought just over 100,000 shares of Nexen that day and paired it with a short position in the XEG basket of stocks.[125]

MacNicol commented on Dotson's acquisition of the Nexen long position, calling it a "rumor trade."[126] Others discussed Nexen's assets and debt position.[127] The group moved on to other topics. Dotson said nothing more regarding Nexen or CNQ or the rumor.[128]

The Hearing Panel notes that there were conflicting opinions on the call about whether a CNQ-Nexen combination made sense. It is also apparent that the group considered the rumor in its analysis. However, Dotson did not argue particularly hard for the trade, and the group discussed many factors in addition to the rumor that might make it prudent to hold a position in Nexen.[129]

MacNicol testified that a number of factors had accumulated to lead them to take a position in Nexen, including the Nexen trading on the preceding Friday and the competitors who had gone out to the market with the Nexen thesis during the preceding week. MacNicol testified that the market believed that Nexen would be acquired.[130]

The day after the group call, Dotson and MacNicol spoke. Dotson recommended that they sell the Nexen position before the company issued its earnings announcement because the stock had a history of declining around the time of its earnings announcement.[131] This recommendation shows that Dotson was focused on trading patterns and not the likelihood of a takeover bid by CNQ.

O. Resolution Of The Nexen Position

The long position in Nexen was later unwound at a profit of approximately $170,000.[132] However, the profit was not the result of the fruition of the rumored merger of CNQ and Nexen. That transaction did not happen. Nexen was not bought by another company until three years after the events at issue here.[133]

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[125] CX-19A, at 29-30.

[126] CX-19A, at 30.

[127] CX-19A, at 31-33.

[128] CX-19A, at 33-41.

[129] CX-19A, at 29-30.

[130] CX-66, at 30.

[131] Hearing Tr. (Dotson) 332-33; CX-20.

[132] CX-46, at 7.

[133] Hearing Tr. (Dotson) 342.

P. Rumor Was False

The rumor that CNQ was considering the acquisition of Nexen was false. CNQ told FINRA staff during its investigation that during the relevant period (March 1, 2009, through April 1, 2009) CNQ was not considering an acquisition of Nexen, that it did not have any project with a code name of "Occi" or "Oxi," and that the company-wide trading blackout from April 16, 2009, through May 8, 2009, was standard procedure in advance of the company's earnings announcement.[134]

IV. CREDIBILITY FINDINGS

A. Benko Testimony And Investigative Evidence

As discussed above, when Dotson's Firm learned that its employees had information that came from within CNQ, the Firm immediately conducted an investigation. Among other people, the Firm and its lawyers interviewed BH, the childhood friend who was the initial alleged tippee, and GH, the oil and gas analyst who was the second tippee. Information gathered in the Firm's investigation is reflected in written notes of the Firm's outside attorneys, letters to regulators from the law firm summarizing the results of the investigation, and in the telephone testimony of Benko, the Firm's then-vice president of Human Resources, who participated in interviews conducted in the investigation.

The Hearing Panel considered the evidence available from the Firm's investigation. In particular, the Hearing Panel relies on this evidence for its findings regarding the conversation between AA, the initial tipper, and BH, the initial tippee, and the conversation between BH and GH, the oil and gas analyst who passed on the rumor to Dotson. The investigative evidence also demonstrates that the rumor was widely circulating in the market at the time of Dotson's trading, and that a number of people knew that the rumor came from inside CNQ.

Although the investigative evidence and Benko's testimony about it constitute hearsay, hearsay is permitted in this forum,[135] and the Hearing Panel finds the evidence and Benko's testimony credible and reliable. The participants in the investigation had reason to be as careful and accurate as they could be in describing what they discovered. The investigative evidence and Benko's testimony reflect an attention to detail and an effort to be accurate. In addition, that evidence and Benko's testimony are consistent with other evidence in the record.

B. Dotson Testimony

Dotson testified that he did not "register" the significance of what GH told him. He said that it was only when, in the context of the investigation, he went to his lawyer's office and

[134] Hearing Tr. (Kirwan) 631-35, 640-41; CX-46; RX-87.

[135] *Dep't of Enforcement v. Padilla*, No. 2006005786501, 2012 FINRA Discip. LEXIS 46, at *36 (NAC Aug. 1, 2012) (citing *Scott Epstein*, Exchange Act Release No. 59328, 2009 SEC LEXIS 217, at *46-47 (Jan. 30, 2009)).

listened to the audio recording of the Tuesday morning call with GH that he realized the significance.[136] He testified,

> [GH] definitely said it to me, I heard it; didn't register with me, I glossed over it, obviously I shouldn't have done that …. [As I said in my OTR] I absolutely should have heard that and I didn't – I am saying I should have heard it, I should have heard it, registered it and questioned him about it.[137]

Dotson explained some of the circumstances that contributed to his failure to notice the significance of GH's remark that the information came from inside CNQ. He noted that the call had occurred during the busiest period of his day, that he would never have expected that a colleague would call him on a recorded telephone line to tell him improper inside information, and that his mind had gone immediately to the Nexen trading activity the preceding Friday and the potential synergies of a CNQ-Nexen transaction.[138]

Dotson did not treat those circumstances as a justification or excuse, however. Dotson vehemently condemned his failure to notice the significance of what GH told him, as demonstrated by the following exchange:

> Q: Having looked back at this, you'll concede, right, that what you really should have done with [Mr. GH's] call, had you heard and registered everything … that you should have stopped him and told him if you're talking to someone that you shouldn't be talking to, you shouldn't be talking to me, you should have told him that?
>
> A: Absolutely, I conceded that three weeks into the investigation, I conceded it at the [OTR] and I even feel stronger about it now, I absolutely should have done that.
>
> And that phone call right now would last all of three seconds, because I would say to him, before you even tell me what you want to say, who are you talking to.
>
> Q: Another thing you should have done is you should have called your compliance department, correct?
>
> A: Correct.[139]

[136] Hearing Tr. (Dotson) 258-59.

[137] Hearing Tr. (Dotson) at 258.

[138] Hearing Tr. (Dotson) 259-60.

[139] Hearing Tr. (Dotson) 348-49.

Dotson accepted responsibility for making a serious mistake. He admitted that there is a qualitative difference between someone saying that he heard information in "the marketplace" and someone saying that the information came from an employee inside one of the companies at issue.[140] He exhibited dismay that he had made such a mistake and did not attempt to minimize the seriousness of the error.

The Hearing Panel finds Dotson credible when he testified that he failed to focus on the fact that the rumor came from inside CNQ. He only realized there was an issue after he heard a recording of his telephone conversation undistracted by his noisy and chaotic work environment and the various concerns, conversations, and trades that he was juggling.

This conclusion is bolstered by Rankin's testimony. When Rankin was told that the rumor came from someone internal at CNQ, he also did not at the time register the significance of that fact. He said he was preoccupied with other matters. It was only when he later listened to an audio recording that he "cringed" in recognition of the issue. Thus, Dotson was not the only person who failed to recognize the significance of what he was told about the source of the rumor being inside CNQ.

The Hearing Panel further notes that many people inside and out of TD knew that the source of the rumor worked at CNQ and did not treat that fact as a bar to discussion or trading. The general indication of an inside source did not diminish the vagueness of the rumor.

Furthermore, the Hearing Panel finds Dotson credible generally. Dotson made an effort to be clear and did not obfuscate. He straightforwardly confessed his mistake.

Market Regulation made much of two discrepancies between Dotson's OTR and his testimony at the hearing. The Hearing Panel does not find those discrepancies damaging to Dotson's credibility. They appear the product of faulty precision and recollection at the OTR.

In the first instance, Dotson testified at his OTR that he had never done a trade for the TS Prop Account before Nexen; but he testified at the hearing that he had done one previous trade for the TS Prop Account. He testified at the hearing that a few days before accumulating the Nexen position he had done a Suncor/Petro-Canada transaction for the TS Prop Account. Dotson explained the discrepancy, suggesting that the Suncor/Petro-Canada transaction was so close in time to the Nexen transaction that he was "just thinking Nexen." It appeared that he thought of both transactions as part of the same Nexen complex of events. In any case, his hearing testimony, as opposed to his OTR testimony, appears to be accurate. Dotson noted that the Suncor/Petro-Canada transaction could be verified because it was discussed in some of the telephone calls that were transcribed for purposes of the proceeding.

In the second instance, Dotson testified at his OTR that before the events at issue he had never taken a position in Nexen that lasted more than a day or two; but he testified at the hearing

[140] Hearing Tr. (Dotson) 263-64.

that he had previously purchased 32 million shares of Nexen in three tranches over the course of thirty months, and some of those shares went into a proprietary account. Dotson did acknowledge at the hearing that when he accumulated Nexen shares on March 31, 2009, it was the first time that he had taken a long position in Nexen that he anticipated keeping more than a week.[141] Accordingly, his testimony regarding the discrepancy rendered the evidence at the hearing more precise.

V. CONCLUSIONS OF LAW

A. Standard Of Proof

Market Regulation has the burden of proof. That burden is met if Market Regulation establishes the violations by a preponderance of the evidence.[142] The preponderance of evidence standard of proof requires that the complainant "prove it is more likely than not" that the allegations are true.[143] Essentially, the balance of the evidence must tip at least slightly in favor of the complainant.

The preponderance of the evidence standard requires evidence, not speculation. Here, Market Regulation depends unduly on speculative possibilities. It asserts, for example, that AA was in a position to know his company's acquisition plans even though he worked in northern British Columbia because this is the age of the cell phone and email. That is pure speculation. It falls far short of showing by a preponderance of the evidence that AA actually had access to confidential information about his company's acquisition plans.[144]

Market Regulation also attempts to shift its burden of proof to Respondent. It characterizes Dotson as speculating that AA was not in a position to know his company's merger and acquisition plans by virtue of his backwoods location. However, it is Market Regulation's burden to show that AA in fact had access to confidential information and breached a duty of trust and confidence when he conveyed the rumor to BH. Market Regulation proved only that AA was a CNQ employee. From that single fact, Market Regulation infers that AA had access

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[141] Hearing Tr. (Dotson) 198-200, 203-05.

[142] *Dep't of Enforcement v. Claggett*, No. 2005000631501, 2007 FINRA Discip. LEXIS 2, at *25 (NAC Sept. 28, 2007) (Enforcement had burden of proof, which it had to satisfy by a preponderance of the evidence).

See also Luis Miguel Cespedes, Exchange Act Release No. 59404, 2009 SEC LEXIS 368, at *18 and n.11 (Feb. 13, 2009) (citing *David M. Levine*, 57 S.E.C. 50, 73 n.42 (2003) (holding that preponderance of the evidence is the standard of proof in self-regulatory organization ("SRO") disciplinary proceedings)); *Kirk A. Knapp*, 51 S.E.C. 115, 130 n.65 (1992) (stating the "the correct standard is preponderance of the evidence" in an SRO proceeding).

The Second Circuit Court of Appeals noted in *Gonchar v. SEC*, 2010 U.S. App. LEXIS 25763, at **3-4 (Dec. 17, 2010) that the U.S. Supreme Court held in *Steadman v. SEC*, 450 U.S. 91 (1981) that SEC disciplinary proceedings are governed by the preponderance of the evidence standard. The Second Circuit concluded that there is no reason to apply a different standard where discipline is initially imposed by an SRO and then sustained by the SEC. *Id.*

[143] *Herman & MacLean v. Huddleston*, 459 U.S. 375, 390 (1983) (discussing nature of standard and holding that it applies to civil damage actions for securities fraud).

[144] Mkt. Reg. PH Br. at 17.

to highly sensitive and confidential information and breached a duty to CNQ when he disclosed it. Dotson countered that weak inference of special access by showing that the nature and location of AA's work made it unlikely that he had confidential information regarding CNQ's acquisition plans and strategies. It is not Respondent's burden to prove more.[145]

In this case, although Dotson's trading warranted investigation, the Hearing Panel concludes that the record does not support the conclusion that Dotson engaged in the alleged violations. What Dotson heard was a widely circulating rumor—not material non-public information—and Dotson understood it to be no more than a rumor, as did many others who discussed the rumor.

B. First Cause Of Action

(1) Insider Trading Law

Section 10(b) of the Securities Exchange Act of 1934 makes it unlawful, directly or indirectly, to use or employ a manipulative or deceptive device in connection with a purchase or sale of a security in contravention of a rule promulgated by the Securities and Exchange Commission ("SEC") for the protection of investors.[146] Rule 10b-5 is one of the SEC rules intended to protect investors. Among other things, Rule 10b-5 makes it unlawful "to employ any device, scheme, or artifice to defraud…." [147] A violation of these provisions must involve a "manipulation or deception."[148]

It is well established that insider trading is a type of securities fraud and violates these provisions.[149] Illegal insider trading refers generally to buying or selling a security, in breach of a fiduciary duty or other relationship of trust and confidence, while in possession of material,

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[145] There was scant evidence that AA, the gas plant operator, had access to material non-public information or that CNQ had imposed on him a duty of trust and confidence. In contrast, in *SEC v. Musella*, 748 F. Supp. 1028, 1031-32 (S.D.N.Y. 1989) there were stipulations establishing that the initial tipper, a law firm employee, had access to confidential information and had received memoranda imposing a duty to protect that information. The Hearing Panel's decision does not turn, however, on the absence of that proof in this case. Even assuming that AA did have access to confidential information, and that he breached a duty to his company when he told BH about the rumor, Market Regulation failed to prove other required elements of its case.

[146] 15 U.S.C. § 78j(b).

[147] 17 CFR §240.10b-5(a) (1996).

[148] *Dirks v. SEC*, 463 U.S. 646, 654 (1983) (citing *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 472 (1977)).

The elements of a FINRA Rule 2020 violation, which also is alleged in the First Cause of Action, are the same as a securities fraud violation except for the interstate commerce requirement. The FINRA Rule 2010 violation that is alleged in the First Cause of Action depends on whether the other charges in the First Cause of Action are proven. Accordingly, only the alleged federal securities law violation is discussed here.

[149] *See Dirks*, 463 U.S. at 653-54; *Chiarella v. United States*, 445 U.S. 222, 226-30, (1980); *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 847-48 (2d Cir. 1968) (en banc), *cert. denied*, *Coates v. SEC*, 394 U.S. 976 (1969). *See generally In re Cady, Roberts & Co.*, 40 S.E.C. 907 (1961).

non-public information about the security.[150] It is the breach of fiduciary duty or other relationship of trust and confidence that qualifies as a "deceptive device" under Section 10(b). The insider deceives the person or entity to whom he owes the duty when he uses the information to his own advantage in order to make secret profits.[151]

In the so-called "classical" type of insider trading, a corporate insider owes a duty to the company and its shareholders to use the company's material non-public information only for the intended corporate purposes. The insider breaches that duty if he or she exploits the company's confidential information for a personal benefit. Similarly, in the so-called "misappropriation" type of insider trading, the misappropriator owes a duty to his or her employer, client, or other person to access and use material non-public information only as authorized and for the purposes intended. To use the information for trading to obtain a personal benefit breaches that duty.[152]

Dirks

An insider cannot avoid liability by refraining from trading but, instead, "tipping" someone else who trades.[153] As the Supreme Court noted in *Dirks*, the securities laws make it unlawful to do indirectly what one is prohibited from doing directly. An insider is forbidden from giving confidential information to an outsider for the same improper purpose of exploiting it for a personal benefit. If a tipper receives a personal benefit for disclosing the information to the tippee, the tipper has breached his duty.[154] A personal benefit may be a tangible, pecuniary *quid pro quo*, but it also may be reciprocal information or other things of value. The Supreme Court suggested in *Dirks* that it could even be a gift of confidential information to a trading relative or friend, which resembles trading by the insider followed by a gift of the profits to the friend.[155]

A tippee also can be liable.[156] However, in *Dirks* the Supreme Court specifically rejected the argument that anyone who knowingly receives material non-public information from an insider has a duty to disclose that information or abstain from trading. The Court said: "[M]ere possession of non-public information does not give rise to a duty to disclose or abstain; only a specific relationship does that. And we do not believe that the mere receipt of information from an insider creates such a special relationship between the tippee and the corporation's

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[150] Company executives and employees may legally trade in their company's securities in certain circumstances, but references here to insider trading are to the illegal form of insider trading.

[151] *SEC v. Sabrdaran*, 2015 U.S. Dist. LEXIS 25051, at *24-25 (N.D. Cal. Mar. 2, 2015).

[152] *United States v. O'Hagan*, 521 U.S. 642, 651-52 (1997); *Chiarella*, 445 U.S. at 228; *United States v. Evans*, 486 F.3d 315, 321 (7th Cir. 2007) (quoting *Dirks*, 463 U.S. at 654); *SEC v. Jafar*, 2015 U.S. Dist. LEXIS 74281, at *5-12 (S.D.N.Y. June 8, 2015); *United States v. Rajaratnam*, 802 F. Supp. 2d 491, 497 (S.D.N.Y. 2011).

[153] *Id*.

[154] *Dirks*, 463 U.S. at 659.

[155] *Dirks*, 463 U.S. at 664.

[156] *SEC v. Obus*, 693 F.3d 276, 289 (2d Cir. 2012).

shareholders."[157] Rather, under *Dirks*, a tippee is prohibited from trading while in possession of material non-public information only if the tippee knows or should know that he has received the information improperly as a result of a breach of fiduciary duty.[158]

Newman

In its recent decision in *Newman*, the Second Circuit reiterated the Supreme Court's conclusion in *Dirks* that a tippee may only be held liable for insider trading if the insider has breached his fiduciary duty and the tippee knows or should know that there has been a breach. The Second Circuit concluded that the exchange of information for a personal benefit is not separate from an insider's fiduciary breach, and, therefore, a tippee does not know that a breach has occurred unless he knows that the insider received a personal benefit.[159]

The *Newman* Court then discussed the nature of the evidence that would be sufficient to show that the inside source of the confidential information had disclosed it for a personal benefit. It said that to the extent that *Dirks* suggests that a personal benefit may be inferred from a personal relationship, "such an inference is impermissible in the absence of proof of a meaningfully close personal relationship that generates an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature."[160]

The *Newman* decision has been viewed as setting a more rigorous standard of proof than the courts have previously applied, and one that is particularly difficult to meet when the tippee is remote from the original source of the inside information. A remote tippee is less likely to know the circumstances of the original tip. There is disagreement over whether the *Newman* Court's interpretation of *Dirks* is correct.[161] The Parties here also dispute whether the *Newman* decision governs this proceeding.[162]

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[157] *Dirks*, 463 U.S. at 656 n.15.

[158] *Dirks*, 463 U.S. at 660.

[159] *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014). This approach differs from some earlier Second Circuit decisions, which treated the tipper's breach of duty and personal benefit as distinct elements, each of which had to be proven, but only the first of which had to be known by the tippee. *See United States. v. Steinberg*, 21 F. Supp. 3d 309, 314-15 (S.D.N.Y. 2014).

[160] *Newman*, 773 F.3d at 452.

[161] *See, e.g., SEC v. Payton*, 2015 U.S. Dist. LEXIS 44732, at *12-14 (S.D.N.Y. Apr. 6, 2015).

[162] Resp. PH Br. at 43-46; Mkt. Reg. PH Br. at 13-16.

Obus

The Parties do agree, however, on the less rigorous standard that applies if *Newman* does not. Both Parties cite the Second Circuit's prior decision in *Obus* for that standard.[163] The *Obus* Court first summarized the elements of tipper liability:

> [W]e hold that tipper liability requires that (1) the tipper had a duty to keep material non-public information confidential; (2) the tipper breached that duty by intentionally or recklessly relaying the information to a tippee who could use the information in connection with securities trading; and (3) the tipper received a personal benefit from the tip.[164]

The Court then summarized the elements of tippee liability:

> Tippee liability requires that (1) the tipper breached a duty by tipping confidential information; (2) the tippee knew or had reason to know that the tippee improperly obtained the information (i.e., that the information was obtained through the tipper's breach); and (3) the tippee, while in knowing possession of the material non-public information, used the information by trading or by tipping for his own benefit.[165]

Obus, like *Newman*, requires that a tippee know or have reason to know that the material non-public information was improperly obtained through the initial tipper's breach of a duty. However, *Obus* does not require that the tippee know that the tipper received a personal benefit or a personal benefit of a "consequential" or "pecuniary" or "valuable" nature.

The Second Circuit explained in *Obus* why a tippee's knowledge of the tipper's improper breach of duty is critical to finding that the tippee committed securities fraud. It said, "Liability for securities fraud requires proof of scienter, defined as a mental state embracing intent to deceive, manipulate, or defraud …. Negligence is not a sufficiently culpable state of mind to support a Section 10(b) civil violation."[166]

The Hearing Panel concludes that the proof in this case not only fails the *Newman* standard but also fails the *Obus* standard.

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[163] Resp. PH Br. at 20; Mkt. Reg. PH Br. at 16.

[164] *Obus*, 693 F.3d at 289.

[165] *Id*.

[166] *Obus*, 693 F.3d 286 (quoting *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 and n.12 (1976)).

(2) Analysis

Market Regulation failed to prove by a preponderance of the evidence that Dotson committed an insider trading violation for two independent reasons, either of which is sufficient to dismiss the insider trading charge. Accordingly, the Hearing Panel dismisses the First Cause of Action alleging that Dotson committed securities fraud in violation of Section 10(b) of the Securities Exchange Act, Rule 10b-5, and FINRA Rules 2020 and 2010.

First, under both *Newman* and *Obus*, Dotson had to be in possession of material non-public information. The information Dotson received in the telephone call with GH, however, was no more than a vague rumor that was widely circulating. It was not material non-public information.

Second, Market Regulation failed to prove that Dotson had scienter. His knowledge regarding the source of the alleged tip was clearly insufficient under *Newman* because he knew nothing about the circumstances of the initial alleged tip. The evidence also failed the *Obus* standard because Dotson's actions do not support an inference that he knew or should have known that he possessed material non-public information that restricted him from trading.

a. No Material Non-Public Information

The Supreme Court long ago established the test for materiality. Information is material if it "significantly alter[s] the 'total mix' of information made available," such that there is a "substantial likelihood that a reasonable investor would consider it important in deciding whether to buy or sell shares."[167] The information must not only "alter" the mix of information but it must do so "significantly."

The Supreme Court has reiterated more recently that information is material only if a "*reasonable* investor" would view the information as "*significantly*" altering the total mix of information.[168] Accordingly, information is not material merely because it might be of some interest to investors.[169] Information is material only if it achieves a certain level of practical significance. The Second Circuit has described the level of significance required, saying that the information must be "reasonably certain to have a substantial effect on the market price of the security."[170]

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[167] *TSC Indus., Inc. v. Northway, Inc*., 426 U.S. 438, 449 (1976). The Court later expressly adopted the *TSC* standard of materiality for the Section 10(b) and Rule 10b-5 context. *Basic v. Levinson*, 485 U.S. 224, 230-31 (1988).

[168] *Matrixx Initiatives, Inc. v. Siracusano*, __ U.S. __, 131 S. Ct. 1309, at **412-13, 2011 U.S. LEXIS 2416, at ***30 (2011) (emphasis in original).

[169] In fact, in *TSC* the Supreme Court specifically rejected the Seventh Circuit's standard of materiality, which defined materiality as whatever "a reasonable shareholder might consider important." *TSC Indus*., 426 U.S. at 445-50. In so doing, the Supreme Court drew a clear line between material facts and interesting or even important facts.

[170] *SEC v. Texas Gulf Sulphur Co*., 401 F.2d at 854-55.

To be material, information "must be specific."[171] A rumor that "reveals no concrete offers, specific discussions, or anything more than vague expressions of interest" is not material.[172] This is because "[a]ny reasonably sophisticated investor in securities buying shares in a large corporation would expect that, from time to time, other corporations might express an interest in buying, or that the large corporation's directors might discuss what it should do if it obtains such offers."[173]

Furthermore, material non-public information must be "more private than general rumor."[174] Information is not material if it is "already common knowledge among analysts" or is "fairly obvious to all who follow[] the stock."[175] Information is not material non-public information, although known only by a few persons, if their trading on it has caused the information to be fully impounded into the price of the particular stock.[176] "The issue is not the number of people who possess it but whether their trading has caused the information to be fully impounded into the price of the particular stock."[177]

In connection with information regarding a potential merger or acquisition, the Supreme Court established in *Basic v. Levinson* that materiality "will depend at any given time upon a balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity."[178] Analysis of whether information is material is an inherently fact-specific exercise that must encompass all the facts and circumstances of the particular case.[179] Only then can the potential impact of information on investors, price, and the market be evaluated.

GH told Dotson that there was a "buzz" at CNQ that it was "acquiring somebody," and that the name "Nexen" was going around. The information that GH conveyed to Dotson had none of the attributes of material non-public information.

On its face, that information was too vague, unspecific, and uncertain to be material to an investment decision. GH provided no concrete fact to elevate the "buzz" that was "going around" the company beyond "water cooler talk." The rumor contained no information by which

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[171] *United States v. Rajaratnam*, 802 F. Supp. 2d at 498 (quoting *United States v. Mylett*, 97 F.3d 663, 666 (2d Cir. 1996)).

[172] *Jackvony v. RIHT Fin. Corp.*, 873 F.2d 411, 415 (1st Cir. 1989) (Breyer, J.).

[173] *Id*.

[174] *Rajaratnam*, 802 F. Supp. 2d 498 (quoting *United States v. Mylett*, 97 F.3d 663, 666 (2d Cir. 1996)).

[175] *Elkind v. Liggett & Myers, Inc*., 635 F.2d 156, 166 (2d Cir. 1980); *SEC v. Anton*, 2009 U.S. Dist. LEXIS 34889, at *31 (E.D. Pa. 2009).

[176] *Rajaratnam*, 802 F. Supp. 2d at 498 (citing *Mayhew*, 121 F.3d at 50 and *United States v. Libera*, 989 F.2d 596, 601 (2d Cir. 1993)).

[177] *Id.*

[178] *Basic v. Levinson*, 485 U.S. at 238 (quoting *SEC v. Texas Gulf Sulphur Co*., 401 F.2d at 849).

[179] *SEC v. Geon Indus., Inc*., 531 F.2d 39, 47-48 (2d Cir. 1976).

to evaluate the likelihood of a transaction between CNQ and Nexen, as required under *Basic v. Levinson*.

Recipients of the rumor treated it as a rumor. No one treated it as material non-public information that needed to be concealed in order to preserve a trading advantage. Instead, GH told many people the same rumor, and they in turn told many other people. Dotson talked about the rumor with his boss and other senior executives at his Firm. A couple of them even told the CEO of Nexen about the rumor. The widespread circulation of the rumor also robbed it of any non-public character.

Dotson did not immediately seek to trade after hearing the rumor, although Market Regulation emphasizes that Dotson sought his boss's permission to take the long position in Nexen within 35 minutes of his telephone call with GH. In fact, Dotson first spoke to his boss about GH's rumor without suggesting any trade, and they agreed to discuss it at the end of the day. It was only after he knew that the rumor was widely circulating that Dotson asked permission to take the position in Nexen. Even then, he and his boss agreed it could be unwound if the consensus was not to do it.

There was substantial skepticism and doubt about the validity of the rumor. Dotson and others treated the rumor as speculation to be analyzed in light of other information. Even GH, who had conveyed the rumor to Dotson, doubted its validity in a conversation with Dotson later the same day. Senior executives at the Firm thought the idea that "Occi" was a code name for Nexen was laughable because the purported code name was too obvious. As for the halt in CNQ stock trading, Dotson and others discounted its significance. They thought that the halt in CNQ stock trading was consistent with a standard stock trading blackout prior to CNQ's earnings announcement in early May. They also thought it unlikely that CNQ would risk exposing confidential information of an impending acquisition by announcing weeks in advance of a related company-wide stock trading blackout.

The rumor, in fact, conveyed only what everyone involved in the Canadian oil and gas sector assumed that CNQ and the other Canadian oil and gas companies were doing—looking into potential mergers and acquisitions. There was rampant speculation about potential mergers in the industry, and Rankin testified that the CNQ-Nexen rumor was meaningless and obvious. SC, a senior executive at Dotson's Firm, thought that the rumor simply reflected CNQ's effort to keep tabs on the entire market.

There is no evidence that the source of the rumor had any special knowledge or access to CNQ's confidential information or its acquisition plans and prospects. The source was a gas plant operator located in a backwoods field office who enjoyed gossiping about the industry with a childhood friend. Even his alleged tippee did not believe he had special access to CNQ's confidential acquisition plans, and his lack of access was later confirmed when CNQ told regulators that the rumor was false. CNQ was *not* considering the acquisition of Nexen, and the

company-wide trading blackout was simply the standard trading blackout in advance of CNQ's earnings announcement.[180]

b. No Scienter

If *Newman* applies here, Market Regulation must show that Dotson knew that the original tipper, AA, breached a duty he owed CNQ and received a personal benefit. Dotson's knowledge regarding the source of the alleged tip was clearly insufficient under *Newman* because he knew nothing about the circumstances of the initial alleged tip or the tipping chain through which the rumor eventually reached him. Although Market Regulation asserts that the relationship between AA and BH involved an exchange of valuable information that would constitute a personal benefit, based on prior email correspondence, Dotson knew nothing at all about that.

Under *Obus*, the proof fails, too. GH did not tell Dotson anything regarding the source of the original tip except that the person was a CNQ employee. Dotson was not required on the basis of that information to assume that the source breached a duty to his company. In *Dirks*, the Supreme Court specifically rejected the argument that merely knowing that material non-public information comes from an insider is enough to impose tippee liability. To be liable, a tippee must know or have reason to believe that a breach of duty has occurred.

Market Regulation argues that Dotson learned certain other facts that gave him the requisite knowledge. For example, Market Regulation notes that SC told Dotson that GH was discussing project names at CNQ, and a project or code name would signify that the company considered the information confidential. That effort to protect confidential information could support an inference that the recipient of the information had reason to believe that the information was disclosed in breach of a duty.[181]

In context, the Hearing Panel finds that SC's comment to Dotson about project names is insufficient to alert Dotson that he should not trade. It was apparent that GH was sharing the project or code name widely and not treating it as confidential. Dotson also heard that fact from a senior manager at TD who did not suggest that Dotson was barred from trading. The purported code name was treated by SC and others as laughable because it was so obvious a reference to Nexen.

Market Regulation's reliance on *SEC v. Musella*[182] to support its assertion that Dotson had scienter because he heard about a code name is far off the mark. *Musella* involved a

[180] The Hearing Panel does not decide whether a tippee may be liable for insider trading even if the tipped information is false. That question—which might arise, for example, if an administrative assistant to an executive involved in acquisition discussions misinterpreted confidential information and tipped someone with the false interpretation in breach of a duty of confidence and trust—is left for another case. The falsity of the rumor here is treated as evidence that the backwoods gas plant operator did not have any special access to the company's confidential information. It also is consistent with the uncertain and vague nature of the information Dotson received.

[181] Mkt. Reg. PH Br. at 24 and n.117.

[182] Mkt. Reg. PH Br. at 24 n.118. *SEC v. Musella*, 748 F. Supp. 1028 (S.D.N.Y. 1989).

conspiracy to trade on stolen inside information. The tippee in that case was acquainted with the person who conducted the improper trades on behalf of the conspirators. The tippee engaged in a pattern of trading that paralleled the conspirators' trading. He did so in a manner that suggested he thought he had little risk. His explanations for his trades were found lacking in credibility. He falsely denied even knowing the friend whose trading he was following. Compelling evidence showed that the tippee in that case knew that he had obtained the information he used to trade improperly.

Nor do Dotson's actions support the conclusion he had scienter. His trading in Nexen did not have the unusual character Market Regulation ascribes to it and does not support the inference that Dotson knew or should have known that he was in possession of material non-public information when he traded. Dotson had taken proprietary positions for his Firm in the past, including positions in Nexen. Neither he nor his boss regarded Dotson's recommendation of the Nexen position as unusual. Dotson did not seek permission to take a position in Nexen immediately after GH's call or in his first conversation with his boss. He only sought permission after the rumor was widely circulating in the market.

The way the rumor was treated in the market as it was passed around and analyzed also did not alert Dotson that it would be improper for him to trade. Neither Dotson nor anyone else at his Firm who discussed the rumor treated it as a hot tip that should be concealed in order to take advantage of it. The analyst who called Dotson discussed the rumor with many other people that day, as did Dotson and the Firm's salespeople. One of TD's senior executives even called Nexen's CEO and told him about the rumor, as the TD executive later told Dotson. Because the rumor was widely circulating, Dotson did not have reason to think that he was trading on confidential information.

Market Regulation makes much of the fact that Dotson repeatedly confessed that he had mishandled the call with GH.[183] The Hearing Panel does not take this as evidence of scienter, but, rather, as evidence of remorse. Dotson took responsibility for his mistake, but he did not confess to knowing at the time that he was culpable.

For all the foregoing reasons, the Hearing Panel dismisses the First Cause of Action.

C. Second Cause Of Action

Market Regulation's stand-alone charge that Dotson violated FINRA Rule 2010 also fails. GH told Dotson that the rumor about CNQ came from inside CNQ, which meant it *could* have been material non-public information improperly obtained. The Firm's policies and procedures required that Dotson report his receipt of insider-derived information to compliance personnel so that the circumstances could be investigated before trading. Accordingly, Dotson violated his Firm's policies and procedures. The Firm appropriately disciplined him for that compliance violation.

[183] Mkt. Reg. PH Br. at 25-27.

However, Dotson's violation of his Firm's policies and procedures is not automatically a violation of the ethical conduct Rule. A FINRA Rule 2010 violation requires either bad faith or a breach of ethical norms in the industry.[184] In the context of a Rule 2010 violation, the SEC has defined bad faith as a dishonest belief or purpose, and unethical conduct as conduct inconsistent with the moral norms or standards of professional conduct.[185]

In this case, Dotson did not act in bad faith. As discussed above, Dotson did not trade while he knew or should have known he was in possession of material non-public information. At most, he negligently failed to attend to what the analyst said about the source of the information coming from inside CNQ. The record contains evidence to explain this lapse, and Dotson displayed credible dismay and remorse for the lapse.

The Hearing Panel also concludes that Dotson did not violate ethical norms in the industry, although the Panel acknowledges that MacNicol and others testified that it was improper to trade on information that comes from within a company without investigating the source of the information further. Even Dotson himself concedes that he should have admonished GH not to share inside information and investigated further, as well as notified his compliance department.

The Hearing Panel bases its conclusion on the record as a whole. Dotson heard only a vague rumor, and many other persons inside and outside of Dotson's Firm heard the same widely circulating rumor. Dozens of professionals were including that rumor in their trading analysis and testing its validity against other data points. Senior executives at the Firm discussed the rumor with him without suggesting that there was anything improper about discussing it or trading afterward.

Given that evidence, the Hearing Panel dismisses the Second Cause of Action alleging that Dotson violated FINRA Rule 2010.

[184] *E.g.*, *Blair Alexander West*, Exchange Act Release No. 74030, 2015 SEC LEXIS 102, at *20 (Jan. 9, 2015).

[185] *Edward S. Brokaw*, Exchange Act Release No. 70883, 2013 SEC LEXIS 3583, at *33 (Nov. 15, 2013). *See also Simpson v. Bear, Stearns & Co.*, No. C07950030, 1997 NASD Discip. LEXIS 13, at *27 n.9 (NAC Jan. 29, 1997) ("Term 'bad faith' is not simply bad judgment or negligence, but rather it implies the conscious doing of a wrong because of dishonest purpose of moral obliquity ….").

VI. ORDER

The Complaint against Paul Charles Dotson is dismissed.[186]

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Lucinda O. McConathy
Hearing Officer
For the Hearing Panel

[186] The Hearing Panel has considered and rejects without discussion any other arguments made by the Parties that are inconsistent with this decision.