

Re Sutton

IN THE MATTER OF:

The Rules of the Investment Industry Regulatory Organization of Canada

and

Brian Michael Sutton

2018 IIROC 03

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

Heard: November 16, 2017

Decision: January 31, 2018

Hearing Panel:

John Lorn McDougall QC, Chair, Richard E. Austin and Peter Gribbin

Appearances:

Rob DelFrate, IIROC Enforcement Counsel

Charles Corlett, IIROC Enforcement Counsel

Kenneth Dekker, For the Respondent

Brian Michael Sutton, In Person

REASONS FOR PENALTY

I. INTRODUCTION

¶ 1 This Hearing Panel, as it stated in the Reasons for Decision on Liability, regarded this case as singularly unique. Not the least of the reasons for holding this view was Mr. Sutton's long and distinguished career in the securities industry and his behaviour during these proceedings. While we found he was mistaken as to what constituted an "active market" which triggered the breach of IIROC Dealer Member Rule 38.6 (c), there was no intent to do wrong. In other words, it was an honest mistake. Having reached that unanimous decision for the reasons expressed, the Hearing Panel's view of the matter was clear. Indeed, at the end of those reasons we wrote: "If required, a Sanction Hearing will take place at a date and place to be determined".

¶ 2 It was our hope that a contested hearing to determine the appropriate penalty would not be necessary. That hope was not realized. The parties could not be further apart in their respective views as to the appropriate sanctions to impose on Mr. Sutton.

II. STAFF'S POSITION ON PENALTY

¶ 3 Staff submits that the following sanctions are warranted in this case:

- i) A permanent prohibition on Mr. Sutton's approval for registration as a CFO with an IIROC Dealer Member;
- ii) A fine in the amount of \$100,000;
- iii) Costs in the amount of \$50,000.

III. MR. SUTTON'S POSITION ON PENALTY

¶ 4 Counsel for Mr. Sutton made the following submission as to the appropriate sanctions:

- i) A reprimand;
- ii) Perhaps an order that Mr. Sutton rewrite the CFO Examination offered by the Canadian Securities Institute before seeking re-registration in that capacity;
- iii) There be no fine;
- iv) There be no order for costs against Mr. Sutton.

IV. THE PRINCIPLES WHICH SHOULD GUIDE THE PANEL

¶ 5 The IIROC Sanction Guidelines provide a framework which Hearing Panels are advised to consider in connection with the imposition of sanctions in all cases. Of those Guidelines, the following excerpts are particularly apposite in this case:

Purpose of Sanction Guidelines

...

The primary purpose of IIROC disciplinary proceedings is to maintain high standards of conduct in the securities industry and to protect market integrity.

The *Sanction Guidelines* are intended to assist:

- IIROC Enforcement Staff and respondents in the negotiation of settlement agreements;
- hearing panels in determining whether to accept settlement agreements; and
- hearing panels in the fair and efficient determination of appropriate sanctions after disciplinary hearings.

The determination of the appropriate sanction in any given case is discretionary and a fact specific process. The appropriate sanction depends on the facts of a particular case and the circumstances of the conduct. Hearing panels retain the discretion to impose the sanctions they consider appropriate. [emphasis added]

The general principles and key factors set out in the *Sanction Guidelines* are not intended to fetter the discretion of a hearing panel in determining an appropriate sanction.

...

Part I – Sanction Principles for IIROC Disciplinary Proceedings

The following principles provide a framework that should be considered in connection with the imposition of sanctions in all cases.

1. Disciplinary sanctions are preventative in nature and should be designed to protect the investing public, strengthen market integrity, and improve overall business standards and practices.

The purpose of sanctions in a regulatory proceeding is to protect the public interests by restraining future conduct that may harm the capital markets.¹ In order to achieve this, sanctions should be significant enough to prevent and discourage future misconduct by the respondent (specific deterrence), and to deter others from engaging in similar misconduct (general deterrence).

When considering specific and general deterrence in the imposition of sanctions, consideration should be given to the size of the Dealer Member, including the firm's financial resources, nature of the firm's business, and the number of individuals associated with the firm, with a view toward

¹ See for example, *Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission)*, [2001] 2 S.C.R. 132 at para. 43.

ensuring that the sanctions imposed are sufficient to achieve deterrence. Similarly, with respect to an individual respondent, consideration should be given to a *bona fide* inability to pay when imposing a fine (see General Principle no. 7).

General deterrence can be achieved if a sanction strikes an appropriate balance by addressing a Regulated Person's specific misconduct but is also in line with industry expectations.² Any sanction imposed must be proportionate to the conduct at issue and should be similar to sanctions imposed on respondents for similar contraventions in similar circumstances. The sanction should be reduced or increased depending on the relevant mitigating and aggravating factors. [emphasis added]

...

4. Sanctions should ensure that a respondent does not financially benefit as a result of the misconduct.

It is a fundamental tenet that wrong-doers should not benefit from their wrong-doing. Accordingly, in cases where the respondent benefited financially from the misconduct, the sanction, where possible, should include a disgorgement of the amount of any such financial benefit. Financial benefit would include any profits, commissions, fees, or any other compensation or other benefit received by the respondent, directly or indirectly, as a result of the misconduct. Financial benefit may include any loss avoided as a result of the misconduct.

5. A suspension should be considered where:

- there has been one or more serious contraventions;
- there has been a pattern of misconduct;
- the respondent has a prior disciplinary history;
- the contraventions involved fraudulent, willful and/or reckless misconduct; or
- the misconduct in question has caused some measure of harm to investors, the integrity of a marketplace or the securities industry as a whole.

6. A permanent bar should be considered where:

- the contraventions involve significant harm to the investing public, the integrity of the market or the securities industry;
- the misconduct had an element of criminal or quasi-criminal activity; or
- there is reason to believe that the respondent cannot be trusted to act in an honest and fair manner in their dealings with the public, their clients, and the securities industry as a whole.

A fine and/or disgorgement should be considered even where a permanent bar is imposed in egregious cases involving significant harm to investors or to the integrity of the securities industry as a whole.

V. STAFF'S SUBMISSIONS ON SANCTIONS

¶ 6 Staff counsel opened his submissions by stating the rule Mr. Sutton was found to have breached, Rule 38.6 (c), and went on to argue:

² In *Re Mills*, [2001] I.D.A.C.D. No. 7 at p. 3, the Hearing Panel observed: "Industry expectations and understandings are particularly relevant to general deterrence. If a penalty is less than industry understandings would lead its Members to expect for the conduct under consideration, it may undermine the goals of the Association's disciplinary process; similarly, excessive penalties may reduce respect for the process and concomitantly diminish its deterrent effect. Thus the responsibility of the [hearing panel] in a penalty hearing is to determine a penalty appropriate to the conduct and respondent before it, reflecting that its primary purpose is prevention, rather than punishment." [emphasis added]

...and that's the rule that says that the CFO must monitor adherence to the Dealer Member's policies and procedures as necessary to provide reasonable assurance that the Dealer Member complies with the financial rules of the corporation.

And it's Staff's view that is an important rule. IIROC relies on Dealer Members to establish internal policies and procedures to meet these minimum sets of standards. These policies and procedures can vary from firm to firm, but when it comes to financial issues, it is the CFO's responsibility to ensure that the policies and procedures that are in place at that firm are in fact being followed.

And any breach of that rule is serious, and it requires significant sanctions. And it's Staff's view in this case, that means a permanent prohibition on Mr. Sutton's registration as a CFO and a significant fine in the amount of \$100,000.

¶ 7 Staff's view of the primary objective of the sanctions in this case was to provide a general deterrent. Staff relied particularly on the Supreme Court of Canada's decision in *Cartaway Resources Corp. et al v. Hartvikson and Johnson*, [2004] 1 S.C.R. 672. Two paragraphs from the judgment of the Court given by Justice LeBel are particularly helpful in illuminating how the Court thought the objective of creating a general deterrence should fit into the matrix of considerations applicable when fashioning appropriate sanctions:

60 In my view, nothing inherent in the Commission's public interest jurisdiction, as it was considered by this Court in *Asbestos*, *supra*, prevents the Commission from considering general deterrence in making an order. To the contrary, it is reasonable to view general deterrence as an appropriate, and perhaps necessary, consideration in making orders that are both protective and preventative. Ryan J.A. recognized this in her dissent: "The notion of general deterrence is neither punitive nor remedial. A penalty that is meant to generally deter is a penalty designed to discourage or hinder like behaviour in others" (para. 125).

61 The Oxford English Dictionary (2nd ed. 1989), vol. XII, defines "preventive" as "[t]hat anticipates in order to ward against; precautionary; that keeps from coming or taking place; that acts as a hindrance or obstacle". A penalty that is meant to deter generally is a penalty that is designed to keep an occurrence from happening; it discourages similar wrongdoing in others. In a word, a general deterrent is preventative. It is therefore reasonable to consider general deterrence as a factor, albeit not the only one, in imposing a sanction under s. 162. The respective importance of general deterrence as [page698] a factor will vary according to the breach of the Act and the circumstances of the person charged with breaching the Act. [emphasis added]

64 The weight given to general deterrence will vary from case to case and is a matter within the discretion of the Commission. Protecting the public interest will require a different remedial emphasis according to the circumstances. Courts should review the order globally to determine whether it is reasonable. No one factor should be considered in isolation because to do so would skew the textured and nuanced evaluation conducted by the Commission in crafting an order in the public interest. Nevertheless, unreasonable weight given to a particular factor, including general deterrence, will [page699] render the order itself unreasonable. Iacobucci J. in *Pezim*, *supra*, at p. 607, suggested that an example of such unreasonableness would be the exercise of the Commission's discretion in a manner that was capricious or vexatious. [emphasis added]

¶ 8 We will review the matters that the guidelines indicate we should consider in fashioning the remedy again later in these Reasons, but it needs to be kept firmly in mind what the Hearing Panel did not find, and what was not alleged: to wit a *mens rea* on the part of Mr. Sutton, recklessness on his part nor the deriving of a profit from his activities. No allegations of such behaviour were made in the liability phase, no evidence was called in support of such allegations and Mr. Sutton was not cross-examined with respect to any of them.

¶ 9 These allegations of misconduct on the part of Mr. Sutton were made by Staff for the first time in the sanction proceeding. Again, no evidence was called to support them. Each of the three allegations will be reviewed in what follows.

¶ 10 To be specific, at the sanction hearing Staff made the following written submissions:

27. Mr. Sutton's conduct in this case should be characterized as wilfully blind and reckless.

28. Mr. Sutton was the sole independent person within FLSI. He had significant experience in the securities industry. He highlighted his expertise throughout his evidence in chief. He was in the best position to detect and to recognize that something was amiss. Instead, he chose to continue to simply "bill them a lot" and allow the WALP Funds to continue to be priced inaccurately.

¶ 11 During the oral argument, Staff made lengthy submissions on the subject of recklessness including the following:

One of the other factors, whether it was an intentional, willfully blind or reckless, you know, again that is not alleging that Mr. Sutton was the mastermind behind the First Leaside group. But he did play an important role, and it required him to be diligent, and in Staff's view, his failure in this case amounts to recklessness.

¶ 12 With respect to *mens rea*, the Hearing Panel expressly found there was none; Mr. Sutton made, in our view, an honest mistake. *Mens rea* wasn't needed for a conviction under Rule 38.6(c) and the conviction which was a consequence of the finding he had made a mistake cannot be now used to implicate an intention to do wrong on his part.

¶ 13 Similarly with respect to the allegation of recklessness. Staff now submits that we should make a finding that Mr. Sutton was guilty of recklessness. The Hearing Panel was not asked to make a finding of recklessness in the first proceeding and we heard no evidence that would suggest to us at this late date that he was reckless. In our view Mr. Sutton's conduct did not constitute reckless behaviour.

¶ 14 The Hearing Panel finds Staff's attempt to introduce in the sanction hearing an argument made for the first time that Mr. Sutton financially benefited as a result of the misconduct and thus by implication was motivated to act as he did, both procedurally incorrect and unfair. In support of the allegation, Staff relied on snippets of transcripts of pre-charge interviews of Mr. Sutton held in 2012. The thrust of these examinations was to ascertain the nature of the work Mr. Sutton and Mr. Sutton's firm were doing for First Leaside, including Mr. Sutton's performance of his role as CFO.

¶ 15 The evidence of the admittedly high level of billing by Mr. Sutton's firm was given in the context of demonstrating to IIROC Staff that they were doing a great deal of work for the firm to keep it onside with the regulators. The evidence does not support the assertion now made by Staff that he financially benefited from his misconduct and to now suggest it implies a *mens rea* is quite wrong. If such a suggestion was to have been made, at the very least it should have been put to Mr. Sutton when he was in the witness box. It was not.

¶ 16 When one strips away these three late added allegations of misconduct, *mens rea*, recklessness and improper profiting from misconduct, one is left with only the core submission advanced by Staff as the basis for a permanent prohibition on Mr. Sutton's registration: that is, general deterrence. Staff submitted that the conviction alone justifies the imposition of the penalties sought but obviously felt the need to buttress that submission by the late addition of the three added allegations. It was wrong to do so.

¶ 17 The function of the Hearing Panel is to decide itself what is the appropriate sanction having regard to all the circumstances. In doing so, it must balance all the various facts and circumstances in reaching a result which will be viewed by the public, and particularly by members of the securities industry, as one which is just and appropriate and in accordance with the facts before the Hearing Panel.

¶ 18 This is not a settlement approval proceeding where the Hearing Panel defers to the judgment of Staff that the settlement should be accepted except where the Hearing Panel determines that the settlement falls outside "a reasonable range of appropriateness"³. No such deference is owed in a case such as this. To the contrary, it is the judgment of the Hearing Panel, and only the Hearing Panel, that is required. With two industry

³ *Milewski (Re)*, [1999] IDACD No. 17

representatives, the Hearing Panel is ideally positioned to decide what the industry expectations would be in any particular case, including this one.

¶ 19 One other point should be made before turning to analysis of Mr. Sutton's submissions on sanction. At the end of Staff's submissions, counsel suggested that because Mr. Sutton stated under cross-examination during the liability hearing that he did not intend to apply for re-registration, that is a factor that could be taken into account when considering whether a permanent ban was appropriate. The Hearing Panel does not accept that submission. Subjective elements such as a current intention regarding rejoining the securities industry on some date in the future should have no place in the analysis we are expected to perform. The permanent ban is either appropriate or it is not. It should not vary with the age or future intentions of the Respondent.

VI. ANALYSIS

¶ 20 As a starting point in the consideration of an appropriate sanction or sanctions on Mr. Sutton, it is important to identify the factors which are relevant to the determination of the appropriate sanction. The law identifies a myriad of such factors as do the IIROC Sanction Guidelines. However, as discussed earlier, the misconduct was what we found to be a mistaken view as to what constituted an active market which mistake persisted over approximately two years. The two of the many factors which are most relevant in this case are harm to the investors and harm to the industry.

¶ 21 The extent of the harm to the securities holders is unknown. We were presented with an excerpt from the fourth report from the Monitor of the FL Group, dated August 12, 2012, that was prepared as a part of the FL Group's CCAA restructuring. It provides no reliable indication of what the total loss resulting from the position of the FL Group and nothing about what the losses, if any, of the holders of the FL Funds might have been.

¶ 22 As counsel for Mr. Sutton put it in his written submissions and which seems to accurately summarize the reasons why the Monitor's Report doesn't establish any losses by the FL Funds, the putative claimants against First Leaside and Mr. Sutton:

In other words, the Monitor recommended not pursuing the properties under the CCAA Proceedings because it was likely that any proceeds would be paid to the FL Funds with little left over for the other FL Group members. The Monitor *did not* say that the FL Funds would themselves suffer a shortfall but only that, after the FL Funds were paid, there would not be enough money left to the other entities covered by the CCAA proceedings to make it worthwhile to pursue the US Properties.

¶ 23 Of course, there were losses suffered in the FL Group failure, but that fact alone is not nearly enough to fix the responsibility for harm to the unidentified holders of FL Funds on Mr. Sutton. To be clear, we heard no evidence in the liability phase that would support a conclusion that Mr. Sutton's breach caused some measure of harm to investors.

¶ 24 On the other hand, Mr. Sutton had a 37 year career at the highest levels of securities industry regulation without any blemish to his record at all. His advice was sought after by industry participants, including regulators themselves.

¶ 25 We have already reviewed *mens rea*, allegations of recklessness and profiting from wrongdoing in paragraphs 8 to 15 above. We have determined that there is nothing to them and they cannot and do not form part of our analysis as to the appropriate sanctions in this case.

¶ 26 We do not believe that it is appropriate to impose a permanent ban when the only remaining basis upon which it is sought is general deterrence. We are in some doubt whether such a penalty would ever be appropriate when the purpose is only to deter others. The excerpt from Justice LeBel's judgment in *Cartaway* quoted in paragraph 7 above seems to suggest that to rely on a single factor, such as general deterrence, would render the sanction order unreasonable. However, we do not have to base our decision on that point as all the facts and circumstances in this case, taken together, simply do not support a permanent ban at all.

¶ 27 The real question that we had to determine was whether a suspension of any kind was warranted. We

concluded it was not. We reached that conclusion by asking ourselves the classic question of what would a reasonable member of the industry in possession of all the relevant facts think of a suspension being imposed. We carefully considered both sides and deliberated at length as we had when we determined that Mr. Sutton had made an honest mistake. An honest mistake alone does not justify a suspension and, in our view, it does not alone create a need for a general deterrent.

¶ 28 We concluded that the appropriate remedy is a reprimand instead of a suspension of any length. In its way, particularly for Mr. Sutton given his long career and position within the securities regulatory industry, a reprimand is at least as significant as a suspension and may in fact carry more opprobrium with it.

¶ 29 In addition to a reprimand, we have concluded that we should order a fine against Mr. Sutton. We do not accept Staff's submission that it should be \$100,000. That would clearly be punitive, particularly having in mind the expense to which Mr. Sutton has been put defending himself vigorously, which was obviously his right.

¶ 30 We looked to the cases to determine the order of magnitude of fines for mistakes, such as that committed by Mr. Sutton. There are virtually none, but reviewing all cases put before us by the parties and relying on our experience in other cases, we concluded that a fine of \$25,000 would send the appropriate message to the industry participants without being regarded as disproportionately punitive. It also recognizes, together with the reprimand, that Mr. Sutton breached Rule 38.6 (c) which is a serious matter and for which there must be meaningful consequences.

¶ 31 Finally, on the question of costs. As is well known, the IIROC costs regime is asymmetric; IIROC can be awarded costs but costs cannot be awarded against it. In our view, having regard to all the circumstances, which are described in these reasons and the reasons relating to liability, this is not an appropriate case to award costs and we decline to do so.

VII. CONCLUSION

¶ 32 In summary, we make the following order:

- i) A reprimand;
- ii) A fine in the amount of \$25,000;
- iii) No order as to costs.

DATED this 31 day of January, 2018.

John Lorn McDougall

Richard E. Austin

Peter Gribbin

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