

Re Richardson GMP & Pytak

IN THE MATTER OF:

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

and

Richardson GMP Limited and Blair Robert Pytak

2020 IIROC 41

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

Heard: June 30, 2020 in Toronto, Ontario via conference call

Decision: June 30, 2020

Reasons for Decision: November 16, 2020

Hearing Panel:

Thomas J. Lockwood, Q.C., Chair, Paul Bates and Arnold Hochman

Appearance:

Charles Corlett, Enforcement Counsel

David DiPaolo, for the Respondents

Maureen Doherty, for the Respondents

REASONS FOR DECISION

I. INTRODUCTION

¶ 1 Staff of the Investment Industry Regulatory Organization of Canada (“IIROC”) entered into a Settlement Agreement with Richardson GMP Limited (“RGMP”) and Blair Robert Pytak (“Pytak”) (collectively, the “Respondents”). A copy of the Settlement Agreement is attached to these Reasons for Decision.

¶ 2 The Settlement Agreement was presented to the Hearing Panel for acceptance in an initially closed session on June 30, 2020.

¶ 3 The Respondents and Staff of IIROC jointly recommended that the Hearing Panel accept the Settlement Agreement. The Settlement Agreement sets out the facts, the admitted contraventions, the agreed upon sanctions, as well as mitigating and other factors relevant in determining the appropriateness of the proposed sanctions.

¶ 4 After hearing counsel for IIROC and the Respondents and considering the material filed, the Hearing Panel accepted the Settlement Agreement. These are our reasons for so doing.

II. BACKGROUND

¶ 5 RGMP is a Dealer Member with its head office in Toronto, Ontario.

¶ 6 On November 1, 2013, RGMP purchased all of the issued and outstanding shares of Macquarie Private Wealth Inc. (“Macquarie”).

¶ 7 Pytak became a Registered Representative in 1999. He was a Branch Manager with another Dealer Member from 2005 until 2011 when he joined Macquarie as an Assistant Branch Manager. When Macquarie was acquired by RGMP, Pytak continued as an Assistant Branch Manager until August of 2014 when he became the Branch Manager. He is currently a Registered Representative but is no longer a Supervisor.

III. THE CONTRAVENTIONS

¶ 8 RGMP failed to supervise the activities of two of its Registered Representatives, namely Preston Henry Smith (“Smith”) and Adam William Woodward (“Woodward”), for extended periods and to meet the minimum standards for retail customer account supervision, contrary to Dealer Member Rules 38.1 and 2500.

¶ 9 As Woodward’s Supervisor, Pytak failed to fully and properly supervise him in accordance with the supervisory responsibilities he was assigned and to conduct sufficient follow-up and review of supervisory functions he delegated, contrary to Dealer Member Rule 38.4.

¶ 10 There was an admitted internal control failure by RGMP between June of 2013 and November of 2015 in relation to the pricing of certain options positions held in two account holders’ accounts that resulted in the equity of the accounts being incorrect, contrary to Dealer Member Rule 17.2A.

IV. PROPOSED SANCTIONS AND COSTS

¶ 11 RGMP will pay a fine of \$500,000 and costs of \$50,000 within 30 days of the acceptance of the Settlement Agreement.

¶ 12 Pytak will pay a fine of \$24,000 within 30 days of the acceptance of the Settlement Agreement. There will be a two-year prohibition on Pytak’s approval as a Supervisor. He will also have to re-write the Branch Manager’s Examination prior to being approved as a Supervisor.

V. DEALER MEMBER RULES

¶ 13 The Settlement Agreement outlines a number of IIROC Dealer Member Rules which were contravened by the actions or inactions of the Respondents. They are:

- a) Rule 2500 sets out the minimum standards which a Dealer Member must observe to ensure the proper supervision of retail customer account activity. The Rule provides detailed guidance regarding both the structural features and operational outcomes expected of a Dealer Member’s supervisory system.
- b) Rule 38 relates to Compliance and Supervision. Rule 38.1 specifically requires a Dealer Member to establish and maintain a supervisory system that, among other things, is reasonably designed to achieve Registered Representatives’ compliance with the Rules and other regulatory requirements. Rule 38.4 requires individuals, such as the Respondent Pytak, who are responsible for supervising Registered Representatives, to do so in a manner that, among other things, ensures their compliance with the Rules and other regulatory requirements.
- c) Rule 17.2A states that “every Dealer Member shall establish and maintain adequate internal controls in accordance with the internal control policy statements in Rule 2600.” Rule 2600 consists of a number of detailed internal control policy statements.

VI. AGREED FACTS

¶ 14 The Settlement Agreement describes in detail the breaches of these Rules by each of the named Respondents.

¶ 15 RGMP acknowledged that it failed in its obligations to conduct adequate supervision of Smith in respect of the advice and services he provided to six identified client groups (the “Smith Clients”). The supervision failures occurred at the Tier 1 supervision level at the branch office in Calgary, and the Tier 2 supervision level at the head office in Toronto (collectively known as the “Supervisors”). The Supervisors failed to identify and address red flags.

¶ 16 On April 5, 2019, an IROC Hearing Panel accepted a Settlement Agreement between IROC Staff and Smith in which Smith admitted that, during the period between July 2011 and October 2015, he contravened IROC requirements with respect to the Smith Clients. Smith admitted that he failed to know the Smith Clients and recommended investments that were inconsistent with their personal and financial circumstances.

¶ 17 Further details of the actions of Smith and the resultant impact on the Smith Clients are found in paragraphs 13 to 20 of the Settlement Agreement.

¶ 18 Overall, the Supervisors failed to identify that the Smith Clients’ stated risk tolerances and investment objectives were inconsistent with the personal and financial information found in their New Client Application Forms (“NCAFs”). This included 100% high risk tolerances allocated to the entirety of the liquid assets of the Smith Clients, many of whom were nearing retirement age.

¶ 19 The Supervisors also failed to question the Smith Clients’ increasing risk tolerance as they aged. Originally, all of the Smith Clients’ NCAFs identified the high-risk allocations as conservative. In most cases, those allocations increased to levels ranging from 85% to 100% high risk.

¶ 20 As detailed in paragraphs 27 to 32 of the Settlement Agreement, the supervision deficiencies played a role in RGMP’s failure pertaining to the Smith Clients’ debenture purchases. The Supervisors identified that Smith misunderstood the risk of the debentures. However, RGMP admitted that it failed to respond adequately.

¶ 21 RGMP also acknowledged, in the Settlement Agreement, that it failed in its obligations to conduct adequate supervision of Woodward in respect of the advice and services he provided to seven identified clients (the “Woodward Clients”). The supervision failures occurred at the Tier 1 supervision level at the branch office in Calgary, which was the responsibility of Pytak, as well as the Tier 2 supervision level at the head office in Toronto. It was acknowledged that the Supervisors had an insufficient understanding of their areas of responsibility and failed to identify and address red flags.

¶ 22 Pytak acknowledged that he failed to adequately discharge the supervisory responsibilities assigned to him after he became Branch Manager in August of 2014 and failed to conduct sufficient follow-up and review of the supervisory functions he delegated up to and including December of 2015.

¶ 23 On January 12, 2018, an IROC Hearing Panel found that between approximately August of 2012 and December of 2015, Woodward contravened IROC requirements with respect to the Woodward Clients. The Hearing Panel found that the Woodward Clients were vulnerable, with limited investment knowledge, and that they experienced substantial declines in the value of their portfolios.

¶ 24 The Hearing Panel found that Woodward failed to know the clients, failed to use due diligence to ensure that recommendations were suitable for the Woodward Clients and engaged in discretionary trading in the client accounts.

¶ 25 Further details of the actions of Woodward and the resultant impact on the Woodward Clients are

found in paragraphs 36 to 39 of the Settlement Agreement.

¶ 26 Further details of the Respondents' failure to supervise Woodward are found in paragraphs 43 to 47 of the Settlement Agreement.

¶ 27 Overall, the Respondents acknowledged that they failed to:

- (a) ensure that all of the Woodward Clients' stated risk tolerances and investment objectives were consistent with their financial circumstances, investment knowledge and investment objectives;
- (b) make the necessary queries and ensure that Woodward provided adequate responses or properly addressed the queries, for the purpose of ensuring that all trading was conducted with the necessary authority and without discretion;
- (c) make the necessary queries and ensure that Woodward provided adequate responses or properly addressed the queries, for the purpose of ensuring that all of the trading and holdings in the Woodward Clients' accounts were suitable for each of them;
- (d) properly address the risks of Woodward's strategy for each of the Woodward Clients, which ultimately resulted in losses to the clients; and
- (e) ensure that each of the Woodward Clients who purchased prospectus exempt securities qualified for the claimed prospectus exemptions.

¶ 28 IIROC Staff acknowledged that RGMP has spent a significant amount of time, effort and resources to enhance and heighten its compliance structure since 2016. It has implemented significant measures to address the compliance deficiencies which could have contributed to the acknowledged failure to supervise Smith and Woodward.

¶ 29 These measures include the following:

- (a) increased overall risk and compliance staffing including hiring a new Chief Risk and Compliance Officer, other senior level compliance staff and additional Tier 1 and 2 Compliance Officers;
- (b) enhanced management level risk management and governance;
- (c) significantly enhanced executive and board visibility into compliance risks;
- (d) updated policies and procedures and designed and implemented new employee trainings;
- (e) introduced risk operations, including risk classification methodology, reporting, and governance tools to improve overall culture of risk; and
- (f) upgraded technology, including:
 - (i) exception Reporting for Transactional and Managed Accounts; and
 - (ii) implemented a universal security risk rating standard.

¶ 30 In the Settlement Agreement, RGMP also acknowledged that, between June of 2013 and November of 2015, it failed to establish and maintain adequate internal controls relating to certain options trading. The details of this failure are outlined in paragraphs 50 to 78 of the Settlement Agreement.

¶ 31 In essence, two clients opened two fee-based accounts with RGMP. The clients paid annual fees for both accounts, based on the market value of the assets in the accounts. RGMP was responsible for calculating and charging the annual fee.

¶ 32 The clients were experienced in options trading. The clients used the margin made available to them,

as calculated by RGMP's system, licensed from a third party provider (the "System").

¶ 33 Beginning in June of 2013, certain of the positions held by the clients in the accounts had a market value of over \$999.99. However, the System defaulted to a market value of \$999.99 for options on the S&P 500 ("SPX") and Nasdaq 100 ("NDX") for positions with a market value of over \$1,000.00.

¶ 34 As a result of the mispricing, the System:

- (a) displayed an incorrect market price of \$999.99 for SPX and NDX positions above that amount;
- (b) calculated excessive equity in the accounts for margining purposes in certain circumstances; and
- (c) calculated excessive cash available for withdrawals in certain circumstances.

¶ 35 RGMP's trading software displayed the correct prices for the SPX and NDX positions, such that all trading took place at the correct price.

¶ 36 In the Settlement Agreement, RGMP acknowledged that it knew, or should have known, of the fact of the pricing error in or around February of 2014. However, as a result of inadequate internal controls, RGMP did not take proper action to investigate and correct the mispricing.

¶ 37 RGMP was responsible for ensuring that there was adequate equity in the accounts to support the positions held on margin through adequate internal controls. This required that all positions held in accounts be marked to market on at least a daily basis and that equity deficiencies, if any, be remedied in a timely manner by the clients.

¶ 38 As a result of the mispricing, the true equity in the accounts was frequently less than what was calculated by the System. In addition, the mispricing resulted in the stated market values, which were used to determine the annual fee, being significantly different from the actual account value.

¶ 39 On or around October 21, 2015, RGMP's carrying broker raised concerns with respect to a large equity deficiency in the accounts. After applying the marked to market calculations, with the correct market values, the accounts were showing an equity deficiency of \$7,700,000.00 on October 26, 2015.

¶ 40 RGMP requested the account holders to remedy the equity deficiency and reduce the risk in the accounts. When the clients did not remedy the equity deficiencies and did not otherwise reduce the risk, the SPX and NDX positions were liquidated. Legal action ensued, which was still ongoing as of the date of the Settlement Agreement.

VII. PRINCIPLES REGARDING THE ACCEPTANCE OF SETTLEMENT AGREEMENTS

¶ 41 The role of a hearing panel in a settlement hearing is not the same as its role in making a penalty determination after a contested hearing. In a contested hearing, the hearing panel attempts to determine the correct penalty. In a settlement hearing, the hearing panel takes into account the settlement process itself and the fact that the parties have agreed to the penalties set out in the settlement agreement. In our view, a hearing panel should not interfere lightly in a negotiated settlement and should not reject a settlement agreement unless it views the penalty as clearly falling outside a reasonable range of appropriateness.

¶ 42 The IIROC Sanction Guidelines set out a number of principles that should be considered in connection with the imposition of sanctions. One of the key principles is that 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.

¶ 43 In urging us to accept the Settlement Agreement, IIROC Staff referred us to a number of previous IIROC decisions in an attempt to show that the penalties proposed in the case before us fell within the reasonable

range of appropriateness.

¶ 44 The following cases were referred to:

- (a) *Re CIBC World Markets & Trickey* 2018 IIROC 50 (Settlement Agreement)
- (b) *Re Scotia Capital* 2017 IIROC 15 (Settlement Agreement)
- (c) *Re Edward Jones* 2016 IIROC 42 (Settlement Agreement)
- (d) *Re CIBC World Markets* 2011 IIROC 38 (Settlement Agreement)

VIII. DECISION

¶ 45 After a thorough review of the factors and principles by which we should be guided, and the facts of this case, as reflected in the Settlement Agreement, we were, unanimously, of the view that this Settlement Agreement was reasonable, in the public interest, and should be accepted by the Hearing Panel. We so informed the parties at the conclusion of the Settlement Hearing.

Dated at Toronto this 16 day of November 2020.

Thomas J. Lockwood

Paul Bates

Arnold Hochman

SETTLEMENT AGREEMENT

PART I – INTRODUCTION

1. The Investment Industry Regulatory Organization of Canada (“IIROC”) will issue a Notice of Application to announce that it will hold a settlement hearing to consider whether, pursuant to Section 8215 of the Consolidated Enforcement, Examination and Approval Rules of IIROC, a hearing panel (“Hearing Panel”) should accept the settlement agreement (“Settlement Agreement”) entered into between Enforcement Staff of IIROC (“Staff”) and Richardson GMP Limited (“RGMP”) and Blair Robert Pytak (“Pytak”) (collectively, the “Respondents”).

PART II – JOINT SETTLEMENT RECOMMENDATION

2. Staff and the Respondents jointly recommend that the Hearing Panel accept this Settlement Agreement in accordance with the terms and conditions set out below.

PART III – AGREED FACTS

3. For the purposes of this Settlement Agreement, the Respondents agree with the facts as set out in Part III of this Settlement Agreement.

Overview

4. This Settlement Agreement concerns: (1) RGMP’s failure to supervise the activities of Preston Henry Smith and Adam William Woodward, for extended periods, and meet the minimum standards for retail customer account supervision; (2) Pytak’s failure, as Woodward’s Supervisor, to fully and properly supervise him in accordance with the supervisory responsibilities he was assigned and to conduct sufficient follow-up and review of supervisory functions he delegated; and (3) an internal control failure by RGMP in relation to the pricing of certain options positions held in two account holders’ accounts that

resulted in the equity of the accounts being incorrect.

5. The facts and admissions in respect of Pytak relate only to the supervision of Woodward and do not relate to the balance of the admissions contained in this Settlement Agreement.

Background

4. On February 1, 2010, Blackmont Capital Inc. (“Blackmont”) changed its name to Macquarie Private Wealth Inc. (“Macquarie”) and continued to carry on business as Macquarie.
5. On November 1, 2013, RGMP purchased all of the issued and outstanding shares of Macquarie, amalgamated with the same and continued to carry on business as RGMP.
6. RGMP is a Dealer Member with its head office in Toronto, Ontario.
7. Pytak became a Registered Representative in 1999 with another Dealer Member. He was a Branch Manager from 2005 until 2011 when he joined Macquarie as an Assistant Branch Manager in a Calgary branch. In November 2013, when Macquarie was acquired, Pytak continued as an Assistant Branch Manager. In August 2014, he became the Branch Manager. Pytak is currently a Registered Representative but no longer a Supervisor.
8. In May 2008, Smith became a Registered Representative at Blackmont and subsequently at Macquarie and RGMP, where he remained until his employment was terminated in November 2015.
9. In July 2012, Woodward became a Registered Representative at Macquarie and subsequently RGMP, where he remained until his employment was terminated in July 2017.

Preston Smith

10. On April 5, 2019, an IIROC Hearing Panel accepted a Settlement Agreement between IIROC Staff and Smith (the “Smith Settlement”), in which Smith admitted that during the period between July 2011 and October 2015, he contravened IIROC requirements with respect to six client groups (the “Smith Clients”).
11. For the purposes of the Settlement Agreement, the parties agree to use the same clients referred to as the “Smith Clients” in that proceeding (being, BB and JB, DS and KS, GR and RR, JF and JOF, AJ and KS).
12. Between July 2011 and October 2015, Smith admitted that he failed to know the Smith Clients and recommended investments that were inconsistent with their personal and financial circumstances.
13. The Smith Clients were investing to fund their impending, or existing, retirement. In most cases, Smith was overseeing the majority, if not all, of the Smith Clients’ liquid assets. In some cases, the Smith Clients did not want excessive risk in their accounts, had limited investment knowledge, and were reliant on Smith for his investment advice.
14. During the relevant period, the high-risk allocations identified in some of the Smith Clients’ New Client Account Forms (“NCAFs”) grew to inappropriate levels. In some cases, the Smith Clients’ NCAFs would eventually identify risk tolerances of 100% high risk.
15. In several cases, the risk tolerances and objectives were changed to match the Smith Clients’ actual account holdings. In most cases, the Smith Clients’ account holdings were inconsistent with their personal and financial circumstances.
16. While the Smith Clients’ accounts contained a number of different types of high-risk securities, a significant factor contributing to their unsuitable holdings was Smith’s recommendations to invest in a number of high-risk corporate debentures.

17. Between June of 2011 and October of 2013, Macquarie was the agent for prospectus offerings for a number of corporate debentures. Smith recommended these investments to many of his clients, including the Smith Clients. Smith considered the debentures low risk investments and many of the clients thought they were purchasing low risk bonds. The debentures were actually high-risk investments.
18. RGMP received approximately \$2,187,930 in gross commissions from prospective offerings for these debentures, with Smith being compensated \$1,136,928 in net commissions. Smith earned approximately \$65,355.00 from approximately \$1,864,705.00 in sales of debentures to the Smith Clients.
19. Between August and September 2012, Smith was told by Macquarie that the debentures were high-risk investments. Smith continued recommending the debentures to a number of his clients.

Client Impact

20. The Smith Clients' losses during the relevant period ranged between 13% and 37%. In dollars, the accounts declined between \$9,086 and \$488,415. The value of the debentures fell significantly during this period, contributing to the overall decline of the Smith Clients' account performance.

Failure to Supervise Smith

21. RGMP failed in its obligations to conduct adequate supervision of Smith in respect of the advice and services he provided to the Smith Clients. The supervision failures occurred at the Tier 1 supervision level at the branch office in Calgary, and the Tier 2 supervision level at the head office in Toronto (collectively known as "the Supervisors"). The Supervisors failed to identify and address red flags.
22. The Supervisors maintained a log of supervision queries. The logs were uploaded on a monthly basis to a shared database, which was accessible to the relevant Supervisors at the branch. While many supervision concerns were flagged, RGMP failed to ensure identified issues were addressed sufficiently and a number of supervision concerns relating to the Smith Clients were left unresolved.
23. Overall, the Supervisors failed to identify that the Smith Clients' stated risk tolerances and investment objectives were inconsistent with the personal and financial information found in their NCAFs. This included 100% high risk tolerances allocated to the entirety of the Smith Clients' liquid assets, many of whom were nearing retirement age.
24. On some occasions, the Supervisors advised Smith to rebalance his account holdings for the Smith Clients' accounts or update NCAFs to match the account holdings. This resulted in a number of updates to the Smith Clients' risk tolerances. Smith had the Smith Clients match the risk tolerance to the account holdings. The updates were approved without any further inquiries, despite no changes to the Smith Clients' personal or financial circumstances.
25. The Supervisors failed to question the Smith Clients' increasing risk tolerances as they aged. Originally, all of the Smith Clients' NCAFs identified the high-risk allocation as conservative. In most cases, those allocations increased to levels ranging from 85% to 100% high-risk.
26. The Supervisors also failed to flag account holdings in the Smith Client's accounts that were concentrated in TSX Venture issuers, the Oil and Gas sector, the Industrial Sector, and corporate debentures.

Failure to Supervise the Purchases of Debentures

27. The supervision deficiencies played a role in RGMP's failure pertaining to the Smith Clients' debenture purchases. The Supervisors identified that Smith misunderstood the risk of the debentures. However, RGMP failed to respond adequately.

28. When Smith's misunderstanding of the risk of the debentures was identified, RGMP did not review the Smith Clients' accounts and the debenture purchases were not adequately queried because the Clients' NCAFs had inappropriate high-risk tolerances.
29. In two instances, the Smith Clients' debenture purchases resulted in the Supervisors directing Smith to rebalance the holdings or update the Smith Clients' NCAFs. This direction was inappropriate given that the Supervisors knew the Smith Clients had purchased debentures based on a misunderstanding that they were low risk investments and the Supervisors ought to have known that the debentures were illiquid.
30. In these two instances, the Supervisors approved high-risk allocation increases for the Smith Clients. The first Smith Client's allocation increased from 80% to 100% while the second increased from 10% to 100%. In both circumstances, there were no changes to these clients' personal and financial circumstances that would justify changing the risk tolerances.
31. For another client, the Supervisors failed to note two instances where debentures were purchased in an account that had no high-risk allocation.
32. The Supervisors did not question the further purchases of debentures after Smith was told that he had misunderstood the risk of the debentures.

Adam Woodward

33. On January 12, 2018, an IIROC Hearing Panel found that between approximately August 2012 and December 2015, Woodward contravened IIROC requirements with respect to seven clients (the "Woodward Clients").
34. For the purposes of the Settlement Agreement, the parties agree to use the same clients referred to as the Woodward Clients in that proceeding (being, WB, LV, JG, DJ, AJ, AF and KF).
35. The IIROC Hearing Panel found that the Woodward Clients were vulnerable with limited investment knowledge, and experienced substantial declines in the value of their portfolios. Specifically, the Hearing Panel found that Woodward failed to know the clients, failed to use due diligence to ensure that recommendations were suitable for the Woodward Clients, and engaged in discretionary trading in the client accounts.
36. The Woodward Clients were aware that Woodward focused on investment opportunities in local, early-stage energy sector companies. Woodward recommended several similar securities to many of the Woodward Clients, most of which were highly concentrated in the energy sector, including in several instances, purchases of securities in a handful of small energy sector companies. Many of these investments were private placements that required the Woodward Clients who purchased them to rely on prospectus exemptions. These private investments were extremely speculative and had little to no liquidity.
37. Woodward recommended and facilitated trades in high-risk energy sector investments for all of the Woodward Clients without sufficient regard for each clients' age, financial or personal circumstances, investment knowledge, actual investment objectives or actual risk tolerance.

Client Impact

38. Between January 2014 and January 2016, Woodward conducted a high volume of trades in the Woodward Clients' accounts, resulting in substantial declines in portfolio values:

Client	Portfolio Losses	Percentage Decline	Number of Trades
WB	(\$129,283)	(64.3%)	62
LV	(\$42,866)	(21.7%)	122
JG	(\$42,820)	(94.3%)	14
DJ	(\$92,148)	(56.3%)	55
AJ	(\$73,286)	(56.3%)	39
AF	(\$82,612)	(84.7%)	30
KF	(\$155,659)	(74%)	130

39. The Woodward Clients' accounts were all commission-based. In addition to his commission-based compensation, Woodward also received fees paid by issuers for certain private placements.

Failure to Supervise Woodward

40. RGMP failed in its obligations to conduct adequate supervision of Woodward, in respect of the advice and services he provided to the Woodward Clients. The supervision failures occurred at the Tier 1 supervision level at the branch office in Calgary, which was the responsibility of Pytak, and the Tier 2 supervision level at the head office in Toronto. Pytak failed to adequately discharge the supervisory responsibilities assigned to him and conduct sufficient follow-up and review of the supervisory functions he delegated. The Supervisors had an insufficient understanding of their areas of responsibility and failed to identify and address red flags.
41. Pytak became Branch Manager in 2014. Prior to that, the roles and responsibilities of the Branch Manager were performed by other individuals. Pytak's admission herein relates solely to the period during which he was Branch Manager and supervised Woodward.
42. As Branch Manager, Pytak was responsible for the approval and updates of New Client Application Forms ("NCAFs") and the supervision of daily and monthly trading activity.
43. Pytak delegated numerous supervisory tasks including daily trade reviews to an onsite Assistant Branch Manager. The Assistant Branch Manager compiled monthly trade reports for Pytak to review. The purpose of daily and monthly trade reviews and surveillance was to identify suitability and concentration issues or other compliance concerns.
44. If the Assistant Branch Manager identified an issue meriting further inquiry, she would email the Registered Representative to request further information, copying both Pytak and Tier 2 supervision. The Assistant Branch Manager kept Pytak informed by compiling regular summary reports of outstanding compliance queries and concerns.
45. Where a client sought to participate in a non-brokered private placement, a review was conducted by both Tier 1 and Tier 2 supervision to ensure that a prospectus exemption was available.
46. Tier 2 supervision also conducted daily and monthly trade reviews and surveillance, with a focus on accounts generating monthly commissions over \$3,000 and on identifying issues such as suitability, concentration, and other compliance concerns.
47. The investment strategy employed by Woodward in the Woodward Clients' accounts should have raised

numerous red flags, including:

- (i) the stated risk tolerances and investment objectives were high, and reflected a highly speculative investment strategy;
- (ii) virtually all of the investments were highly speculative, junior issuers in the energy sector;
- (iii) there were a large number of trades, nearly all of which were solicited;
- (iv) there were a large number of subscriptions to private placements that were illiquid; and
- (v) Woodward earned additional fees from the issuers for private placement investments.

48. The Supervisors identified many of these red flags and queried some of them accordingly. However, RGMP and Pytak failed to adequately address the red flags. Specifically, they failed to:

- (i) ensure that all of the Woodward Clients' stated risk tolerances and investment objectives were consistent with their financial circumstances, investment knowledge and investment objectives;
- (ii) make the necessary queries and ensure that Woodward provided adequate responses or properly addressed the queries, for the purpose of ensuring that all trading was conducted with the necessary authority and without discretion;
- (iii) make the necessary queries and ensure that Woodward provided adequate responses or properly addressed the queries, for the purpose of ensuring that all of the trading and holdings in the Woodward Clients' accounts were suitable for each of them;
- (iv) properly assess the risks of Woodward's strategy for each of the Woodward Clients, which ultimately resulted in losses to the clients; and
- (v) ensure that each of the Woodward Clients who purchased prospectus exempt securities qualified for the claimed prospectus exemptions.

Remedial Measures

49. RGMP has spent a significant amount of time, effort and resources to enhance and heighten its compliance structure since 2016. It has implemented significant measures to address the compliance deficiencies that could have contributed to the failure to supervise Woodward and Smith. These measures include but are not limited to the following:

- (i) increased overall risk and compliance staffing including hiring a new Chief Risk and Compliance Officer, other senior level compliance staff and additional Tier 1 and 2 Compliance Officers;
- (ii) enhanced management level risk management and governance;
- (iii) significantly enhanced executive and board visibility into compliance risks;
- (iv) updated policies and procedures and designed and implemented new employee trainings;
- (v) introduced risk operations including risk classification methodology, reporting,

- and governance tools to improve overall culture of risk;
- (vi) upgraded technology, including:
- i. exception Reporting for Transactional and Managed Accounts; and
 - ii. implemented a universal security risk rating standard.

Failure to Maintain Adequate Internal Controls

50. In addition to the above issues related to supervision, this settlement agreement also concerns an internal control failure by RGMP in relation to the pricing of certain options positions held in two account holders' accounts that resulted in the equity of the accounts being incorrect.
51. In November 2011, RH opened an account (the "Personal Account") with RGMP. RH initially deposited \$25,000 USD into the Personal Account. In or around August 2013, RH and his partners (collectively, the "Clients") opened a second account with RGMP. The second account holder was the KPH II L.P. Account (the "KPH Account"). RH initially deposited \$1,700,515 USD into the KPH Account. The Clients subsequently deposited and withdrew funds from the KPH Account.
52. Both the Personal Account and the KPH Account (collectively, the "Accounts") were fee based accounts. The Clients paid annual fees for both of the Personal Account and the KPH Account (the "Annual Fee"), charged quarterly, based on the market value of the assets in the account. RGMP was responsible for calculating and charging the Annual Fee. In total, RGMP charged the Clients an Annual Fee of approximately \$136,000 USD for the Personal Account and \$304,000 USD for the KPH Account.
53. The Clients were experienced in options trading and, at the time of the account openings and during most of the time they traded the Accounts, were duly registered portfolio managers with the Autorité des marchés financiers.
54. The Clients primarily traded European style options of the S&P 500 ("SPX") and the Nasdaq 100 ("NDX") in the Accounts. They purchased/sold short calls or puts of the SPX at various strike prices, which they paired by purchasing/selling short calls or puts in the same quantity of the SPX at the sale strike price but with a later expiry date.
55. They purchased/sold short calls or puts of the NDX at various strike prices. In some cases, they purchased/sold short calls or puts in the same or a lesser quantity of the NDX at the same strike price but with a later expiry date (similar to the SPX trading). In other cases, they simply held an uncovered position in the NDX.
56. At the time the SPX and NDX positions were initiated, the Clients used the margin made available to them as calculated by RGMP's system licensed from a third-party provider (the "System").
57. Up until October 2015, in the event RGMP issued a margin call to the Clients on either of the Accounts, the margin calls were addressed through the closing out of either the SPX or NDX positions.

The \$999.99 Mispricing

58. Beginning in June 2013, certain of the SPX and NDX positions held or sold short in the Accounts had a market value of over \$999.99. However, the System defaulted to a market value of \$999.99 for the SPX and NDX positions that had a market value of over \$1,000.00 (the "\$999.99 Mispricing"). The System was used by RGMP for, among other things, providing the market value of the SPX and NDX options that would be used to generate client statements, to calculate client margin in the Accounts and to determine cash available for withdrawals. The \$999.99 Mispricing did not affect the accounts of other clients as no

other clients were trading SPX or NDX options at values over \$999.99.

59. As a result of the \$999.99 Mispricing, the System generated account statements that displayed an incorrect market price of \$999.99 for the SPX and NDX positions above that amount. Similarly, the System calculated excessive equity value in the Accounts for margining purposes when defaulting to \$999.99 for the SPX and NDX positions with a market value over \$1,000.00. The System also calculated excessive cash available for withdrawals for the same reasons.
60. RGMP's trading software displayed the correct prices of those positions, such that all transactions in the SPX and NDX options took place at the correct price, regardless of whether the market value was over \$999.99.
61. RGMP knew, or should have known, of the fact of the pricing error in or around February 2014. As a result of inadequate internal controls, RGMP did not take proper action to investigate and promptly correct the \$999.99 Mispricing and the mispricing continued.
62. In October 2015, RGMP's carrying broker raised concerns about a large collateral deficiency, which was ultimately traced to the SPX and NDX positions in the Accounts. At this time, RGMP understood and recognized the impact of the \$999.99 Mispricing.

The Accounts' Equity and Collateral were Incorrect

63. RGMP was responsible for ensuring that there was adequate equity in the Accounts to support the positions held on margin through adequate internal controls. This required that all positions in the Accounts be marked to market on at least a daily basis and that equity deficiencies, if any, be remedied in a timely manner by the Clients.
64. The \$999.99 Mispricing prevented all SPX and NDX positions with a market value of over \$1,000.00 from being properly marked to market.
65. As a result, the true equity in the Accounts was frequently less than what was calculated by the System.
66. Between January 2015 and September 2015, the equity deficiencies in the KPH Account ranged from \$3,650,630.00 to \$16,451,101.00 and averaged \$9,146,656.67. Between January 2015 and September 2015, the equity deficiencies in the Personal Account ranged from \$1,720,750.00 to \$4,125,130 and averaged \$3,212,700.
67. In addition, the \$999.99 Mispricing resulted in the stated market values that were used to determine the Annual Fee being significantly different from the actual account value.
68. This value was used to determine the Annual Fees owed by RH pursuant to the fee-based account agreement.
69. RH paid an Annual Fee based on the market value of the assets in the Accounts. Between June 2013 and November 2015, RGMP charged Annual Fees of \$105,098.89 USD on the Personal Account and \$304,489.91 USD on the KPH Account. Had RGMP properly valued the positions held in the Accounts, these amounts would have been different.

Closing out of the Option Positions

70. On or around October 21, 2015, RGMP's carrying broker raised concerns with respect to a large equity deficiency in the Accounts.
71. After applying the mark to market calculations with the correct market values, the Accounts were showing an equity deficiency of \$7,700,000 on October 26, 2015. Margin calls were then issued in the

Accounts for the amount of the equity deficiency.

72. On October 28, 2015, RGMP discussed these concerns with a representative of the Clients. RGMP advised him that the Accounts were deficient after applying mark to market calculations with the correct market values.
73. RGMP then advised that the Clients needed to take steps to remedy the equity deficiency and reduce the risk in the Accounts. RGMP requested that the Clients deposit additional funds into the Accounts, immediately close out the positions or provide a personal guarantee and cross guarantee on the Accounts. The Clients were also offered the option of transferring the assets to another firm.
74. The Clients did not remedy the equity deficiency and did not otherwise reduce the risk in the Accounts.
75. Between November 2 and 4, 2015, RGMP liquidated all NDX positions and on November 30, 2015, RGMP liquidated all SPX positions.
76. Despite the October 2015 account statements showing a stated market value of \$1,609,728.64 in the Personal Account and \$15,757,637.44 in the KPH Account, following the liquidation of both the NDX and SPX positions, the December 2015 account statements showed an actual deficiency of (\$1,698,951.90) in the Personal Account and (\$3,231,367.91) in the KPH Account.
77. RGMP commenced an action against the Clients in the Québec Superior Court to recover the outstanding debit that resulted from the margin calls and the liquidation of the Accounts. The Clients issued a counterclaim against RGMP, alleging that there was no equity deficiency in the Accounts, that RGMP had no reason to issue margin calls and that the liquidation of the Accounts was reckless.
78. In a trial decision released on January 20, 2020, the Court granted RGMP's action and dismissed the Clients' counterclaim. As of the date of the Settlement Agreement, the Clients have appealed from that trial decision before the Québec Court of Appeal.

PART IV – CONTRAVENTIONS

79. By engaging in the conduct described above, the Respondents committed the following contraventions of IIROC's Rules:
 - (i) Between July 2011 and October 2015, as particularized above, RGMP failed to supervise the activities of Preston Henry Smith ("Smith") and between August 2012 and December 2015, failed to supervise the activities of Adam William Woodward ("Woodward") contrary to Dealer Member Rules 38.1 and 2500.
 - (ii) Between August 2014 and December 2015, as particularized above, Pytak, a Supervisor at Richardson GMP Limited in Calgary, failed to supervise the activities of Woodward contrary to Dealer Member Rule 38.4.
 - (iii) Between June 2013 and November 2015, as particularized above, RGMP failed to establish and maintain adequate internal controls relating to certain options trading contrary to Dealer Member Rule 17.2A.

PART V – TERMS OF SETTLEMENT

80. The Respondents agree to the following sanctions and costs:

Richardson GMP Limited

- (i) A fine of \$500,000; and

(ii) Costs of \$50,000.

Blair Robert Pytak

(i) a fine of \$24,000;

(ii) a 2 year prohibition on approval as a Supervisor; and

(iii) re-write of Branch Managers' Examination prior to being approved as a Supervisor.

81. If this Settlement Agreement is accepted by the Hearing Panel, the Respondents agree to pay the amounts referred to above within 30 days of such acceptance unless otherwise agreed between Staff and the Respondents.

PART VI – STAFF COMMITMENT

82. If the Hearing Panel accepts this Settlement Agreement, Staff will not initiate any further action against the Respondents in relation to the facts set out in Part III and the contraventions in Part IV of this Settlement Agreement, subject to the provisions of the paragraph below.

83. If the Hearing Panel accepts this Settlement Agreement and the Respondents fail to comply with any of the terms of the Settlement Agreement, Staff may bring proceedings under Rule 8200 against the Respondents. These proceedings may be based on, but are not limited to, the facts set out Part III of this Settlement Agreement.

PART VII – PROCEDURE FOR ACCEPTANCE OF SETTLEMENT

84. This Settlement Agreement is conditional on acceptance by the Hearing Panel.

85. This Settlement Agreement shall be presented to a Hearing Panel at a settlement hearing in accordance with the procedures described in Sections 8215 and 8428, in addition to any other procedures that may be agreed upon between the parties.

86. Staff and the Respondents agree that this Settlement Agreement will form all of the agreed facts that will be submitted at the settlement hearing, unless the parties agree that additional facts should be submitted at the settlement hearing. If the Respondents do not appear at the settlement hearing, Staff may disclose additional relevant facts, if requested by the Hearing Panel.

87. If the Hearing Panel accepts the Settlement Agreement, the Respondents agree to waive all rights under the IIROC Rules and any applicable legislation to any further hearing, appeal and review.

88. If the Hearing Panel rejects the Settlement Agreement, Staff and the Respondents may enter into another settlement agreement or Staff may proceed to a disciplinary hearing based on the same or related allegations.

89. The terms of this Settlement Agreement are confidential unless and until this Settlement Agreement has been accepted by the Hearing Panel.

90. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel and IIROC will post a full of copy of this Settlement Agreement on the IIROC website. IIROC will also publish a summary of the facts, contraventions, and the sanctions agreed upon in this Settlement Agreement.

91. If this Settlement Agreement is accepted, the Respondents agrees that neither they nor anyone on their behalf, will make a public statement inconsistent with this Settlement Agreement.

92. The Settlement Agreement is effective and binding upon the Respondents and Staff as of the date of its

acceptance by the Hearing Panel.

PART VIII – EXECUTION OF SETTLEMENT AGREEMENT

- 93. This Settlement Agreement may be signed in one or more counterparts, which together will constitute a binding agreement.
- 94. An electronic copy of any signature will be treated as an original signature.

DATED this “25th” day of June, 2020.

“Per: Richardson GMP Limited”

Per: Richardson GMP Limited

“Blair Robert Pytak”

Blair Robert Pytak

“Charles Corlett”

Charles Corlett

Director, Enforcement Litigation on behalf of
Enforcement Staff of the Investment Industry
Regulatory Organization of Canada

The Settlement Agreement is hereby accepted this “30” day of June, 2020 by the following Hearing Panel:

Per: “Thomas Lockwood”

Panel Chair

Per: “Paul Bates”

Panel Member

Per: Arnold Hochman”

Panel Member

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