Re Lilly

IN THE MATTER OF:

The Rules of the Investment Industry Regulatory Organization of Canada

and

Patrick John Lilly

2020 IIROC 21

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

Heard: June 10, 2020 in Toronto, Ontario (electronically)
Decision and Reasons: July 13, 2020

Hearing Panel:
Paul M. Moore, Q.C., Chair, Steven Garmaise, Vanessa Gardiner
Appearance:
April Engelberg, Enforcement Counsel
Hugh Lissaman, Respondent's Counsel
Patrick John Lilly (present)

DECISION AND REASONS FOR ACCEPTANCE OF SETTLEMENT AGREEMENT

Procedure and Decision

¶ 1 A settlement hearing was held on June 10, 2020 pursuant to IIROC Rules by audio-video conference with all attendees connected by videoconference, except Vanessa Gardiner and the Respondent who were connected by audio only.

¶ 2 During brief adjournments in the hearing, the Panel deliberated *in camera*. At the end of the hearing, the Panel announced to the attendees that it was reserving its decision whether to accept or reject the Settlement Agreement.

¶ 3 The Panel has now decided to accept the Settlement Agreement for the following reasons.

Settlement Agreement

¶ 4 The Settlement Agreement is dated May 29, 2020 and was made between IIROC Enforcement Staff and the Respondent.

¶ 5 A copy of the Settlement Agreement is attached to these reasons.

Facts

¶ 6 The agreed facts on which the settlement was based are set out in Part III of the Settlement Agreement. The Panel elicited additional information provided by counsel and the Respondent. The agreed facts and the additional information provide reasonable grounds for the Panel to conclude that it was in the

public interest to accept the Settlement Agreement.

Contravention

¶ 7 In the Settlement Agreement, the Respondent admitted that between January and April 2018, while Chief Compliance Officer (CCO) of Dominick Capital Corp., he failed to disclose and obtain approval for an outside business activity, contrary to Dealer Member Rule 18.14.

¶ 8 We concluded that the admitted misconduct did in fact contravene the cited Rule as alleged.

Agreed Penalty

¶ 9 The agreed penalties were:

(1) a fine of $15,000;

(2) a 6 month-suspension as an Approved Person, effective from April 5, 2018 when the Respondent ceased to be an Approved Person;

(3) a requirement to successfully re-write the Conduct and Practices Handbook course prior to becoming an Approved Person; and

(4) payment of costs of $1,500.

¶ 10 The Respondent agreed to pay the amounts referred to above within 30 days of acceptance of the Settlement Agreement by the Panel unless otherwise agreed between Enforcement Staff and the Respondent.

Importance of the settlement process

¶ 11 It is usually in the public interest that matters be settled where possible rather than be determined through contested hearings. An earlier resolution of a dispute is better than a later determination. Settlements are usually less expensive than contested litigation, and there is less congestion in the dispute settling system when matters are taken out of the system through settlements. Finally, where both parties agree, the result is often more palatable to the parties and society than in a contested hearing where the winner takes all.

¶ 12 For these reasons, a panel considering the acceptance of a settlement agreement will try to reach a determination of acceptance. It will recognize that settlements are often hotly debated with much compromise and give-and-take between the parties in order to reach an acceptable position agreeable to both parties. Furthermore, the panel will recognize that it is not privy to all the facts, motivations and considerations of each party in arriving at a solution of the dispute agreeable to all.

Role of the panel

¶ 13 A panel considering whether to accept a settlement agreement and its agreed penalties is in a different position than a panel determining an appropriate penalty in a contested hearing.

¶ 14 Each needs to consider precedents and the law and, most importantly, the particular facts and circumstances of the case, including the particular circumstances of the specific respondent.

¶ 15 However, unlike a panel in a contested hearing that must set the actual penalties that appear appropriate to it, a panel in a hearing to consider a settlement agreement has only two options under the IIROC Rules:

1. to accept the agreed settlement with its penalties because the panel agrees that the penalties are acceptable, or

2. to reject the agreed settlement because the agreed penalties are not acceptable or because the panel has not been given enough information for it to come to a determination that the agreed

penalties are acceptable.

¶ 16 A panel considering whether to accept a settlement agreement cannot substitute for the agreed penalties those penalties that it might prefer to have in the circumstances. However, the parties can always be invited by the panel to provide additional information that the panel believes it needs in order to come to a favourable decision; and the parties may choose to provide it. Or indeed, the parties may agree to changes in the agreed penalties to meet what the panel believes is required for an acceptance, in order to avoid a rejection by the panel. But the panel cannot impose a change unilaterally.

¶ 17 In the final analysis, a panel will accept a settlement agreement where it is in the public interest to do so, as will almost always be the case where the panel is satisfied regarding the three considerations mentioned below.

Three Considerations

¶ 18 The Panel determined that it had to be satisfied regarding three considerations before it could accept the Settlement Agreement. First, the agreed penalties had to be within an acceptable range taking into account similar cases. Secondly, the agreed penalties had to be fair and reasonable, that is proportional to the seriousness of the contravention taking into consideration other relevant circumstances, and should appear to be so to members of the public and industry. Thirdly, the agreed penalties should serve as an adequate deterrent to the Respondent and to the industry.

¶ 19 To be satisfied on these three considerations required an understanding of the particular facts of the case, the circumstances of the Respondent, and the impact on him of the agreed penalties.

Matters of Concern

¶ 20 We were initially concerned that the agreed penalties were not reasonable, that they would not provide an adequate deterrent to the Respondent and to others, and that acceptance of the Settlement Agreement with the agreed penalties could bring the regulatory oversight regime by IIROC into disrepute.

The Respondent's Senior Regulatory Role

¶ 21 The Respondent was CCO of his Dealer Member during the events in question. He was responsible for overseeing compliance by Approved Persons at his Dealer Member of activities of the very nature that he undertook in contravention of the Dealer Member's policies and procedures and IIROC Rule 18.14.

Respondent's Prior Compliance Deficiencies

¶ 22 Furthermore, the Respondent had entered into a previous settlement agreement with IIROC in August 2016, in which it was admitted that he and his Dealer Member had failed to ensure compliance with regulatory requirements with respect to among other things:

1. avoiding the misuse of confidential information, and
2. identifying, managing and disclosing conflicts of interest, potential conflicts of interests, and outside business activities, and
3. the Respondent had failed to ensure his Dealer Member's undertakings made to IIROC that it would develop and improve its sales compliance program.

Apparent Serious Violation of Disclosure Requirements

¶ 23 Initially, it appeared to the Panel that the Respondent's misconduct was a continuation of failures to perform his regulatory duties to ensure compliance by Approved Persons, including himself, with disclosure and other requirements regarding outside business activities. The following was particularly troubling for the panel:

(1) Mr. Lilly, as the CCO, with a previous history of difficulties regarding outside business activities, should have known to file the disclosure forms.

(2) The fact that he prepared required disclosure forms but failed to submit them to his Dealer Member could be an indication of an intention to delay unreasonably disclosure of the outside business activity rather than a belief that no business activity had yet come into being.

(3) The Settlement Agreement mentions that Mr. Lilly participated in at least one pre-marketing meeting for the planned limited partnership offering, raising questions as to his judgment that no outside business activity had yet come into being.

(4) The failure to disclose only came to light with the filing of a press release by the issuer's parent company, not through any voluntary disclosure by Mr. Lilly.

Importance of Rule 18.14

¶ 24 We considered the Respondent's misconduct in light of David Lang's comments in *Trueman (Re)* 2016 IIROC 29, paragraphs 35, 36 and 39 where he stated:

> **35** Disclosure of outside business activities is one of the fundamental principles of the securities regulatory framework. It allows a firm on a Tier 1 basis [Tier 1 is at the business supervisor level at the firm] to look at all the activities that a sales person is undertaking and to make sure that they are in the client's best interests and that issues such as conflicts of interest and potential for client confusion are identified and addressed. It also allows that activity to be monitored at the Tier 2 level [an independent compliance review].
>
> **36** When a person undertakes activity outside the auspices of the firm, that fundamental protection provided for in the securities regulation is unable to occur.
>
> **39** One should never forget the fundamental principle of outside business activity and disclosure. For the respondent and anybody else who might read these reasons in the future, it should be very clear that these are fundamental protections in the securities regulatory framework and we cannot tolerate people who do not adhere to them.

Adequacy of the Financial Penalties

¶ 25 In view of the forgoing, the Panel was initially concerned that the proposed penalties – a fine of $15,000, payment of costs of $1,500, and a retroactive suspension – would not serve as an adequate deterrence.

¶ 26 Given the seriousness of the misconduct, the repeated pattern of failure to disclose outside business activities, and the possibly premeditated non-disclosure by the Respondent, the fine appeared to fall below an acceptable range discerned from comparable cases and to be too low in absolute terms. We worried that if we accepted the Settlement Agreement, this case would serve as a bad precedent for lower penalties and inadequate sanctions for serious regulatory violations in the future.

¶ 27 However, the additional information provided to the Panel, which unfortunately was not included in the Settlement Agreement despite the importance of the information and its centrality to our determination that the financial penalties alone were sufficient and adequate to serve as a deterrent, ultimately satisfied us that the financial penalties were acceptable in the particular circumstances.

Additional Information Provided to the Panel

¶ 28 The Respondent stated that he never intended not to disclose to his Dealer Member and not to obtain any required consents regarding his involvement with the outside business activity if, as, and when it turned into an activity and a business. He believed that it was premature to disclose anything at the preliminary

planning or exploratory stages of the potential outside business activity. In fact, nothing ever came of the proposed business activity.

¶ 29 He now admits in the Settlement Agreement that he was wrong in his view that he had no obligation to disclose earlier than he did and that his conduct was in contravention of Dealer Member Rule 18.14.

¶ 30 However, he had no intention to deceive or not to comply with the requirements of Rule 18.14; no business was ever done; he received no benefit from his conduct; no persons suffered loss because of his misconduct or the proposed outside business activity; and this was an isolated incident.

¶ 31 The Respondent was fully co-operative with IIROC from the start of its investigation into all aspects and facts of this matter.

¶ 32 The Respondent is 60 years old. He has been out of the securities business since April 2018. His prospects of ever working again in the securities industry are limited.

¶ 33 We noted that IIROC Sanction Guidelines provide that inability to pay is a factor when considering an appropriate monetary sanction or costs when raised by a respondent, as it was in this case.

¶ 34 Enforcement Staff advised us of its investigation of the Respondent's financial circumstances. Staff was satisfied that the Respondent has limited financial means to pay the $15,000 fine and $1,500 costs award, and that their payment will have a significant financial impact on him.

Deterrence

¶ 35 In *Rotstein (Re)* 2014 IIROC 34, the hearing panel accepting the settlement agreement considered by it and said, at paragraph 8, quoting from IIROC's Dealer Member Disciplinary Guidelines:

> A prior disciplinary history may highlight a concern about individual or specific deterrence, an important objective of the disciplinary process and the need to impose progressively escalating sanctions on repeat offenders.

¶ 36 Enforcement Staff advised the Panel that the financial sanction for the Respondent in the earlier settlement with IIROC in August 2016 was for $7,500. The fine and costs award in the current Settlement Agreement are double that amount.

¶ 37 We concluded that the financial penalties in the Settlement Agreement will have a greater impact on the Respondent than the financial penalties in the prior settlement agreement had on him at that time. In light of all the circumstances referred to above, the financial penalties in the Settlement Agreement do serve as an adequate deterrent to the Respondent and, therefore, to the industry.

Retroactive Suspension

¶ 38 We failed to see any deterrent or other regulatory purpose for the 6 months suspension, retroactive to the time the Respondent ceased to be an Approved Person, and expiring more than a year and a half ago.

¶ 39 Enforcement Staff was unable to articulate for us what it saw as regulatory merit for such a suspension. Staff cited another settlement, which included a retroactive suspension as one of the sanctions, but the facts were not the same as the facts in his case. That other settlement was not a good precedent for us.

¶ 40 We determined that the retroactive suspension sanction in the Settlement Agreement was not necessary, useful, or meaningful, and we gave it no weight in determining the acceptability of the agreed sanctions.

Precedent cases

¶ 41 We reviewed the precedent cases submitted by the parties and compared the financial penalties in

the Settlement Agreement with the range of penalties in these cases. In doing this, we also reviewed the unique facts and circumstances of each case and compared and contrasted them with the unique facts and circumstance set out in the Settlement Agreement.

¶ 42 Because no case has the same facts and circumstances, it is an art, not a science, (adjusting for particular facts and circumstances) to determine what is an acceptable range for penalties in a situation like the one before us. However, we were satisfied that the financial penalties in the Settlement Agreement, although at the lowest of the low end of any reasonable range we could construct, were acceptable in this case.

Fair and Reasonable

¶ 43 What is fair and reasonable will depend to a large degree on the particular facts and circumstances of a matter. Where both parties to a settlement agreement are represented by counsel, and have the means to undergo a contested hearing, but have reached a settlement, it would be unusual that a panel would ever conclude that the settlement was unfair and not reasonable.

Conclusion

¶ 44 We concluded that the financial penalties were within an acceptable range based on the precedents, would serve as a specific and general deterrent, and were fair and reasonable under the particular circumstances of this case. We, therefore, decided that it was in the public interest that we accept the Settlement Agreement.

Dated at the City of Toronto, in the Province of Ontario, this 13 day of July 2020.

Paul M. Moore

Steven Garmaise

Vanessa Gardiner

SETTLEMENT AGREEMENT

PART 1 – INTRODUCTION

1. The Investment Industry Regulatory Organization of Canada ("IIROC") will issue a Notice of Motion 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 the staff of IIROC ("Staff") and Patrick Lilly ("Respondent").

PART II – JOINT SETTLEMENT RECOMMENDATION

2. Staff and the Respondent 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 Respondent agrees with the facts as set out in Part III of this Settlement Agreement.

Overview

4. This matter involves the Respondent's conduct in relation to an outside business activity ("OBA") which he failed to disclose to his Dealer Member, Dominick Capital Corp. ("Dominick"), while he was its Chief

Compliance Officer ("CCO"). The Respondent was listed as the Chief Executive Officer ("CEO"), President and Director of a potential non-brokered private placement called Ring of Fire LP ("ROFLP"). Dominick's president and UDP only became aware of the Respondent's involvement with ROFLP upon reading a press release.

Background

5. The Respondent became the CCO of Dominick in 2008, and also acted as CEO and UDP from 2011 to September 2016.

6. In August 2016, a settlement agreement between the Respondent, Dominick and IIROC Staff was approved in which it was admitted that:

   (i) From 2011 to 2014, Dominick and the Respondent failed to ensure compliance with regulatory requirements with respect to (a) avoiding the misuse of confidential information, (b) identifying, managing and disclosing conflicts of interest, potential conflict of interest, and OBAs, and (c) supervising retail accounts, contrary to IIROC Dealer member Rules 38, 18.14 and 2500; and

   (ii) From January 2012 to May 2015, the Respondent engaged in conduct unbecoming a registrant by failing to ensure that Dominick fulfill representations made to IIROC that it would develop and improve its sales compliance program, contrary to IIROC Dealer Member Rule 29.1.

Respondent's OBA with Ring of Fire LP

7. The Respondent became involved with ROFLP in or prior to January 2018, while he was CCO of Dominick.

8. In February 2018, the draft Offering Memorandum (the "Draft OM") for ROFLP described the Respondent as the "President since February 1, 2018" and "Director". The Draft OM also described the Respondent as CCO of Dominick. The Respondent attended a meeting with ROFLP representatives and a potential distributor.

9. In March 2018, the Respondent learned of material non-public information regarding KWG Resources Inc. ("KWG"), the parent company of ROFLP. As a result, he grey listed KWG at Dominick but did not specify why, or disclose his involvement to Dominick. The Respondent prepared OBA disclosure forms that clearly identified his role at ROFLP, however he did not submit them to anyone at Dominick.

10. On March 5, 2018, a press release regarding ROFLP stated that the Respondent was CEO of ROFLP (the "Press Release"). The Respondent asserts that he was not the CEO, however, the Press Release was not amended. The Respondent did not disclose it to Dominick.

Dominick discovers the OBA and terminates the Respondent with Cause

11. On April 4, 2018, Michael McIntosh, president of Dominick, became aware of the Press Release. He immediately questioned the Respondent about his involvement with ROFLP. The Respondent provided McIntosh with a copy of the Draft OM.

12. On April 5, 2018, the Respondent was terminated for cause. The Respondent is no longer registered with IIROC.

13. Dominick was suspended as a Dealer Member on August 16, 2019.

PART IV - CONTRAVENTIONS

14. Between January and April 2018, the Respondent, while Chief Compliance Officer of Dominick Capital Corp., failed to disclose and obtain approval for an outside business activity, contrary to Dealer Member Rule 18.14.

PART V – TERMS OF SETTLEMENT

15. The Respondent agrees to the following sanctions and costs:

    a) A fine in the amount of $15,000; and

    b) 6 months suspension as an Approved Person, effective from April 5, 2018 when the Respondent ceased to be an Approved Person;

    c) Re-write and pass the Conduct and Practices Handbook course prior to becoming an Approved Person; and

    d) Costs in the amount of $1,500.

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

PART VI – STAFF COMMITMENT

17. If the Hearing Panel accepts this Settlement Agreement, Staff will not initiate any further action against the Respondent 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.

18. If the Hearing Panel accepts this Settlement Agreement and the Respondent fails to comply with any of the terms of the Settlement Agreement, Staff may bring proceedings under Rule 8200 against the Respondent. 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

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

20. 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.

21. Staff and the Respondent 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 Respondent does not appear at the settlement hearing, Staff may disclose additional relevant facts, if requested by the Hearing Panel.

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

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

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

25. 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.

26. If this Settlement Agreement is accepted, the Respondent agrees that neither he nor anyone on his behalf, will make a public statement inconsistent with this Settlement Agreement.

27. The Settlement Agreement is effective and binding upon the Respondent and Staff as of the date of its

acceptance by the Hearing Panel.

PART VIII – EXECUTION OF SETTLEMENT AGREEMENT

28. This Settlement Agreement may be signed in one or more counterparts which together will constitute a binding agreement.

29. A fax or electronic copy of any signature will be treated as an original signature.

DATED this "29" day of "May", 2020.

"Witness"
Witness

"Patrick Lilly"
Patrick Lilly

"Ricki Ann Newmarch "
Witness

"April Engelberg"
April Engelberg
Enforcement Counsel
on behalf of Enforcement Staff
of the Investment Industry Regulatory Organization of Canada

The Settlement Agreement is hereby accepted this "29" day of "June", 2020 by the following Hearing Panel:

Per: "Paul Moore"
Panel Chair

Per: " Steve Garmaise"
Panel Member

Per: "Vanessa Gardiner"
Panel Member