

Re Kennedy

IN THE MATTER OF:

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

and

Linda Kennedy

2016 IIROC 39

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

Heard: September 20, 2016 in Toronto, Ontario

Decision: September 20, 2016

Reasons: October 11, 2016

Hearing Panel:

Susan Lang, Chair; Edward Jackson; David Kerr

Appearances:

Kathryn Andrews, Enforcement Counsel

Robert Brush and Kate McGrann, for the Respondent

REASONS FOR DECISION

Introduction

¶ 1 Enforcement counsel for the Investment Industry Regulatory Organization of Canada (IIROC) and the Respondent, Linda Kennedy, put forward for the Panel's consideration a Settlement Agreement in which Ms. Kennedy acknowledges her failure as a branch manager to adequately supervise the account activity of a registered representative and the parties jointly propose that the Respondent pay a \$25,000 fine as well as costs of \$1,000.

¶ 2 The Settlement Agreement was reached in accordance with IIROC Dealer Member Rules 20.35 to 20.40, inclusive and Rule 15 of the Rules of Practice and Procedure.

¶ 3 After reviewing the Settlement Agreement and material filed and hearing oral argument, the Hearing Panel accepted the terms of the Settlement Agreement, including the proposed fine of \$25,000 and costs of \$1,000. These are our reasons for doing so.

THE CIRCUMSTANCES

¶ 4 The Settlement Agreement, which sets out the factual background that forms the basis for the settlement, is attached to these Reasons as Appendix A. What follows is a brief summary of the acknowledged background and circumstances.

¶ 5 Ms. Kennedy, who was registered with IIROC as a branch manager in 2003, was the branch manager at Assante Capital Management Ltd. (Assante) when Alistair Melville joined the branch in 2007 as a registered representative.

¶ 6 In addition to internal client accounts with Assante, between 2009 and 2012, Mr. Melville deposited more than \$2 million of client funds into external accounts, including an external pro account at BMO Investorline Inc. (the BMO account).

¶ 7 In the Settlement Agreement, Ms. Kennedy admits that between September 2010 and December 2012, she “failed to adequately supervise the account activity in an external account held by Registered Representative Alistair Melville at another Dealer Member firm, contrary to IIROC Dealer Member Rules 38.4(a) and 2500.”

¶ 8 At the time, Ms. Kennedy knew that Mr. Melville’s annual salary was approximately \$130,000 to \$140,000. Ms. Kennedy was aware that Mr. Melville was a professional poker player. Indeed, she had seen him win \$150,000 in a televised poker tournament. In September 2010 she accepted his assurance that he only used that account as a “slush fund” for his poker winnings.

¶ 9 Despite this assurance and as described in *Re Melville*, [2014] IIROC 51, paras. 17 and 18, Mr. Melville deposited \$2,158,000 of client funds into his pro BMO account. When Mr. Melville’s employment with Assante was terminated in December 2012 the account stood at \$250,000. Counsel advised that Assante paid approximately \$1.8 m of compensation to Mr. Melville’s former clients: see para 21 of the *Melville* decision.

¶ 10 In the Kennedy Settlement Agreement, Ms. Kennedy acknowledges her failure to supervise adequately the activity in the BMO account. She acknowledges that she should not have accepted Mr. Melville’s explanation and that various red flags should have caused her to escalate the matter to head office.

¶ 11 Those red flags included the following: more than \$20,000 was withdrawn monthly from the account between April and September 2011; in every 2011 month, also in smaller transactions, there “was at least \$20,000 in either withdrawals or total deposits; in August 2011 and November 2012, the deposits totalled more than \$70,000 and in 12 months in 2011 and 2012, deposits totalled more than \$40,000. In addition, deposits increased quite substantially in 2012.

¶ 12 Ms. Kennedy acknowledges that, with adequate supervision, client losses might have been discovered earlier.

¶ 13 These are the circumstances that form the basis for the Respondent’s acknowledgement of her failure as a branch manager to supervise adequately the activity in Mr. Melville’s external BMO account.

SERIOUSNESS OF THE CONTRAVENTION

¶ 14 Branch managers bear an important responsibility to provide adequate supervision of the accounts of registered representatives. Such supervision is essential to ensure ethical conduct, fair trading and the integrity of the investment industry. Contravention of this obligation must be treated as serious. See *Re Portfolio Strategies Securities*, [2012] IIROC 36, para 7. In describing a branch manager’s supervisory responsibility in *Re Mills*, [2000] IDACD No. 41, the Ontario District Council described the difficulty with placing too much trust on the explanation of a registered representative and the need to take further steps to “guard against” the “legitimate tendency of managers to trust registered representatives with whom they work closely”. See also the discussion of the responsibility of branch managers in *Re Youden*, [2005] IDACD No. 52. Branch managers must not simply accept the explanation of an individual registered representative at face value where the account activity raises concerns that require further review.

DUTY OF A HEARING PANEL IN A SETTLEMENT HEARING

¶ 15 In deciding whether to accept a Settlement Agreement, a panel is not asked whether it would reach the

same conclusion. Rather, it is charged with determining whether the proposed penalty falls within the range of being fair and reasonable in the circumstances of the case, including the objective of protecting the investing public, maintaining the integrity of the investment industry and the markets and of deterring misconduct. In addition, settlements are to be supported as a means of encouraging negotiation and compromise to arrive at an expeditious resolution of appropriate disciplinary proceedings. See: *Re Melville, supra* at paras 9-10; *Re Portfolio Strategies*, [2012] IIROC 36; *Re Ast*, [2012] IIROC 38.

GUIDELINES AND OTHER DECISIONS

¶ 16 The sanction must be appropriate to the circumstances of the particular conduct and respondent, recognizing the need for specific and general deterrence. The IIROC Sanction Guidelines, while not binding, are useful in providing guidance. Other decisions may also assist in determining the range of reasonableness of the proposed sanction.

¶ 17 Other cases involving branch managers in other circumstances were brought to our attention. See for example, *Re Mills, supra*. While *Mills* involved a fine of \$50,000 and costs of \$35,000, that respondent's conduct involved the conscious overriding of coding requirements. In *Re Youden, supra*, while the panel imposed a fine of \$70,000 and required a re-write of the branch managers' course, the facts of the failure to supervise were very different from those involving Ms. Kennedy. Moreover, the penalty was imposed following a lengthy hearing and not pursuant to a Settlement Agreement.

¶ 18 In *Re Richardson*, [2013] IIROC 50, the panel imposed a fine of \$15,000, a one-month suspension and required a re-write of the branch managers' course as well as costs of \$2,000. *Re Menzel*, [2015] IIROC 6 involved a \$20,000 fine and \$1,500 in costs in accordance with a Settlement Agreement involving the inadequate supervision of a registered representative. *Richardson* and *Menzel* describe a range in keeping with the one proffered in this case.

¶ 19 That said, each case must be determined on the basis of its own facts.

RANGE OF PENALTY

¶ 20 In considering the seriousness of the breach, Enforcement Counsel observes that Ms. Kennedy's supervisory failure continued for more than two years and did so in the face of red flags arising from both the number and the quantity of transactions.

¶ 21 The Settlement Agreement also refers to factors in mitigation, including that the Respondent received good reviews during an Assante internal audit in 2008-2009 and that there have been no issues with her supervision of internal client accounts at Assante during or since the relevant time. In other words, Ms. Kennedy's contravention was limited to her failure to supervise the external account.

¶ 22 Counsel advised during argument that "outside pro accounts are being reviewed by Assante head office compliance, per Assante policy" and that, as a branch manager, "Ms. Kennedy will not have a role in reviewing outside pro accounts." This is relevant to the likelihood of any reoccurrence.

¶ 23 In accepting the proposed penalty, we took into consideration the specific facts involving Ms. Kennedy, the nature of her lack of supervision, and the impact of the sanction for deterrence purposes. The panel concluded that the fine of \$25,000 and costs of \$1,000 fell within the reasonable and appropriate range to achieve the relative objective and encourage settlement. At the same time, this sanction demonstrates that breaches of supervisory duties by branch managers will be taken seriously and is tailored to the circumstances of Ms. Kennedy and her default.

¶ 24 We agree with the submissions of counsel that neither a suspension nor a requirement to take the branch managers' course was appropriate in the circumstances of this case, including the fact that the responsibility for reviewing external pro accounts is being done by Assante's head office and does not form part of Ms. Kennedy's responsibilities.

DECISION

¶ 25 These reasons explain why the Panel concluded that the settlement was reasonable and accepted its terms.

Dated at Toronto, Ontario this 7th day of October, 2016.

Susan Lang

Chair

Edward Jackson

David Kerr

APPENDIX A

INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

IN THE MATTER OF:

THE RULES OF THE INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF
CANADA (IIROC)

AND

LINDA KENNEDY

SETTLEMENT AGREEMENT

I. INTRODUCTION

1. IIROC Enforcement Staff (“Staff”) and the Respondent Linda Kennedy (the “Respondent”), consent and agree to the settlement of this matter by way of this agreement (the “Settlement Agreement”).
2. The Enforcement Department of IIROC has conducted an investigation (the “Investigation”) into the Respondent’s conduct.
3. The Investigation discloses matters for which the Respondent may be disciplined by a hearing panel appointed pursuant to IIROC Transitional Rule No.1, Schedule C.1, Part C (the “Hearing Panel”).

II. JOINT SETTLEMENT RECOMMENDATION

4. Staff and the Respondent jointly recommend that the Hearing Panel accept this Settlement Agreement.
5. The Respondent admits to the following contravention of IIROC Dealer Member Rules, Guidelines, Regulations or Policies:

From September 2010 to December 2012, the Respondent failed to adequately supervise the account activity in an external account held by Registered Representative Alistair Melville at another Dealer Member firm, contrary to IIROC

Dealer Member Rules 38.4 (a) and 2500.

6. Staff and the Respondent agree to the following terms of settlement:
 - a. Payment of a fine in the amount of \$25,000.
7. The Respondent agrees to pay costs to IIROC in the sum of \$1,000.

III. STATEMENT OF FACTS

(i) Acknowledgment

8. Staff and the Respondent agree with the facts set out in this Section III and acknowledge that the terms of the settlement contained in this Settlement Agreement are based upon those specific facts.

(ii) Factual Background

Overview

9. Kennedy was the Branch Manager at an Assante Capital Management Ltd. (“Assante”) branch located in Hamilton, Ontario. Registered Representative Alistair Melville (“Melville”) joined the branch in 2007.
10. From September 2010 through to December 2012, Kennedy failed to adequately question the account activity conducted by Melville in an external pro account held by him at BMO Investorline Inc. (the “BMO Account”).
11. Kennedy did not thoroughly question the numerous deposits and withdrawals made by Melville in the BMO Account. Kennedy told Staff that she was aware that Melville was a professional poker player. Kennedy relied solely on Melville’s assurances that his BMO Account was used as his “slush fund” for his poker tournaments. Kennedy failed to conduct any other due diligence to satisfy herself regarding the numerous activities in the BMO Account. In fact, Melville used the BMO Account to deposit and to withdraw funds provided by his clients.

Background

12. Kennedy was registered with IIROC as a Branch Manager in 2003. From September 2010 until December 2012 (the “Relevant Time Period”) Kennedy was the Branch Manager responsible for supervising Melville.
13. Kennedy remains a Branch Manager at Assante and does not have her own book of business. Kennedy did not have her own book of business during the Relevant Time Period.

Melville’s conduct

14. Between 2009 and 2012, Melville obtained funds from numerous clients totaling over \$2 million and deposited these funds into bank accounts then into discount brokerage accounts held by him at two other Dealer Member firms.
15. By way of Settlement Agreement accepted by a Hearing Panel in October 2014, Melville agreed to a permanent ban on registration in any capacity, a fine of \$400,000 and to pay costs in the amount of \$10,000.

Inadequate Supervision

16. Kennedy failed to conduct adequate supervision of Melville’s BMO Account activity during the Relevant Time Period.

Red Flags in the BMO Account

17. A review of the BMO Account monthly statements indicates that, for example, between April 2011 and September 2011, a total of over \$20,000 was withdrawn every month from the BMO Account in a series of smaller transactions. In addition, in every month during 2011, there was at least \$20,000 in either total withdrawals or total deposits each month done in a series of smaller transactions.
18. In addition, there were two months (August 2011 and November 2012) where the series of deposits to the BMO Account totalled more than \$70,000 in each of those months. There were also twelve months

in 2011 and 2012 where the series of deposits totalled more than \$40,000 in each of those months.

19. The total amount of withdrawals and deposits in the BMO Account increased quite substantially during 2012 as compared to 2010 and 2011.

Lack of due diligence

20. Kennedy told Staff that she asked Melville in September 2010 about the BMO Account and that he replied that it was his “slush fund” for poker winnings. Kennedy told Staff that she had seen Melville in a televised poker tournament where he won \$150,000. As a result, Kennedy believed Melville’s explanation. Kennedy should not have simply relied on Melville’s response. She should have made other efforts to ascertain whether or not the numerous withdrawals and deposits to the BMO Account were legitimate.
21. Kennedy told Staff that Melville’s salary during the Relevant Time Period was approximately \$130,000 to \$140,000. Kennedy should have paid greater attention to, and made additional inquiries about the numerous deposits, given Melville’s own salary and his explanation for the source of the funds.
22. Kennedy acknowledges that she should not have accepted Melville’s explanation at face value, and should instead have recognized the “red flags” in the account statements and escalated the matter to head office.
23. While Melville did not transfer funds from Assante client accounts directly into the BMO Account, some of the clients’ losses might have been discovered earlier had the Respondent escalated the matter to head office.
24. Kennedy did not make any notes or provide Staff with any written evidence of queries made of Melville regarding activity in the BMO Account during the Relevant Time Period.

Other

25. The Respondent’s supervisory practices at the branch received good reviews during a 2008-2009 internal audit by Assante. There have been no issues with the Respondent’s supervision of client accounts at Assante during the Relevant Time Period or since.
26. The Respondent does not have a previous disciplinary history with IIROC.

IV. TERMS OF SETTLEMENT

27. This settlement is agreed upon in accordance with IIROC Dealer Member Rules 20.35 to 20.40, inclusive and Rule 15 of the Dealer Member Rules of Practice and Procedure.
28. The Settlement Agreement is subject to acceptance by the Hearing Panel.
29. The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.
30. The Settlement Agreement will be presented to the Hearing Panel at a hearing (the “Settlement Hearing”) for approval. Following the conclusion of the Settlement Hearing, the Hearing Panel may either accept or reject the Settlement Agreement.
31. If the Hearing Panel accepts the Settlement Agreement, the Respondent waives his rights under IIROC rules and any applicable legislation to a disciplinary hearing, review or appeal.
32. 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 in relation to the matters disclosed in the Investigation.
33. The Settlement Agreement will become available to the public upon its acceptance by the Hearing

Panel.

34. Staff and the Respondent agree that if the Hearing Panel accepts the Settlement Agreement, they, or anyone on their behalf, will not make any public statements inconsistent with the Settlement Agreement.
35. Unless otherwise stated, any monetary penalties and costs imposed upon the Respondent are payable immediately upon the effective date of the Settlement Agreement.
36. Unless otherwise stated, any suspensions, bars, expulsions, restrictions or other terms of the Settlement Agreement shall commence on the effective date of the Settlement Agreement.

AGREED TO by the Respondent at the City of “Toronto” in the Province of Ontario, this “8” day of July, 2016.

“Witness”

Witness

“Linda Kennedy”

LINDA KENNEDY

AGREED TO by Staff at the City of Toronto in the Province of Ontario, this “8th” day of July, 2016.

“Witness”

Witness

“Kathryn Andrews”

Kathryn Andrews

Senior Enforcement Counsel on behalf of Staff of
the Investment Industry Regulatory Organization of
Canada

ACCEPTED at the City of Toronto in the Province of Ontario, this “20th” day of “September”, 2016,
by the following Hearing Panel:

Per: “Susan Lang”

Panel Chair

Per: “David Kerr”

Panel Member

Per: “Edward Jackson”

Panel Member

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