

# Re Scotia Capital

IN THE MATTER OF:

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

**and**

**Scotia Capital Inc.**

2017 IIROC 48

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

Heard: July 5, 2017

Decision: July 5, 2017

Reasons: October 6, 2017

## **Hearing Panel:**

John Lorn McDougall, QC, Chair, Daniel Iggers and Richard E. Austin

## **Appearances:**

Elissa Sinha, Enforcement Counsel

David Di Paolo, Respondent Counsel

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## **REASONS FOR DECISION**

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### **I. INTRODUCTION**

¶ 1 By Notice of Application for Settlement Hearing dated June 7, 2017, the Investment Industry Regulatory Organization of Canada (“IIROC”) announced that a hearing would be held on July 5, 2017 to consider whether a hearing panel (“Hearing Panel”) of IIROC should accept a Settlement Agreement dated June 19, 2017 (“Settlement Agreement”) entered into by Staff of IIROC (“Staff”) and the Respondent Scotia Capital Inc. (“Respondent” or “Scotia”) pursuant to Section 8428 of the Consolidated Enforcement Examination and Approval Rules of IIROC.

¶ 2 IIROC had commenced a disciplinary proceeding in respect of the Respondent and alleged, and the Respondent has admitted for the purposes of the Settlement Agreement, that it committed the following contravention of IIROC Rules:

From January 2000 to October 2014, the Respondent Scotia Capital Inc. failed to adequately supervise two Registered Representatives when they recommended securities transactions that were not suitable for their clients and were not in keeping with good business practice contrary to IIROC Dealer Member Rules 38.1 and 2500.

¶ 3 In her opening submission Staff stated that the test to be applied in a Settlement Acceptance hearing is:

“...that the settlement is proportionate to the admitted offence and to the facts, and falls within a reasonable range of appropriateness and is met in this case”.

¶ 4 After considering the Settlement Agreement, which is appended to these Reasons for Decision, and

following the full submissions made by Staff and counsel for the Respondent during which both were closely questioned by the Hearing Panel members, the Hearing Panel unanimously accepted the Settlement Agreement. The Hearing Panel made an order to that effect and indicated that Reasons for Decision would follow in due course. These are those Reasons.

## **II. FACTS**

¶ 5 The portions of the Settlement Agreement which are relevant to these Reasons for Decision are:

### **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. Between January 2010 and October 2014, two Registered Representatives with Scotia, an IIROC Dealer Member firm, implemented an investment strategy for many of their clients which attempted to take advantage of the difference between the price of new issues and initial public offerings of securities (“New Issues”) and the price on the secondary market (the “New Issue Strategy”).
5. Scotia was aware of concerns raised by its compliance officers and the relevant supervisor about the risks associated with the New Issue Strategy. However, Scotia approved numerous clients for high risk short term trading without adequately considering whether that was suitable for them, failed to fully investigate concerns about the New Issue Strategy, and failed to take effective action.
6. Overall, Scotia failed to adequately supervise the two Registered Representatives and failed to prevent trading for at least three clients that was unsuitable and not consistent with good business practice.

#### **The New Issue Strategy**

7. Scotia employed David Chabassol (“Chabassol”) and David Bugden (“Bugden”) as Registered Representatives. They worked in a partnership called the Chabassol Bugden Group (“CBG”) from a satellite location of Scotia’s Halifax branch in New Glasgow, Nova Scotia.
8. As of at least 2010, CBT implemented the New Issue Strategy for many of their clients. The New Issue Strategy seeks returns from high-volume short-term trading and thus is only suitable for clients with high risk tolerance and whose objectives include short-term trading. The use of leveraged funds for the New Issue Strategy by some of CBG’s clients further increased their risks.
9. In each of 2010, 2011, 2012, 2013 and 2014, the value of purchases that CBG made in all of its accounts was approximately double the value of their total assets under management. New Issues accounted for a significant majority of CBG purchases made in each of those years.
10. When CBG purchased New Issues for their clients, the issuers paid a commission to Scotia, which was shared by Scotia and CBG. Due to the commissions paid by issuers and high turnover, the New Issue Strategy was more profitable than a conventional investment approach.

#### **Concerns about CBG and the New Issue Strategy**

11. In late 2009 and early 2010, Scotia compliance officers issued multiple queries related to suitability, high turnover, and concentration in a number of CBG accounts. Significant queries were escalated to CBG's supervisor (the "Supervisor") and senior management for Scotia's compliance department ("Scotia Compliance").
12. In response, Chabassol proposed a so-called "Risk Management Program" specific to certain CBG clients who were involved in the New Issue Strategy. The Risk Management Program defined risk conservatively in order to highlight the high risk nature of the trading strategy. However, this increased the likelihood that for those clients who wished to engage in the strategy, the client risk tolerance and objectives would be set for high risk active trading. It also encouraged risk tolerance and objectives to be set based on the type of trading the clients wished to engage in. Clients received customized risk disclosure packages and more frequent reporting due to the short-term trading.
13. CBG's Supervisor sought guidance from Scotia Compliance about the proposed Risk Management Program. Senior management and the Supervisor expressed concerns that the Risk Management Program did not adequately account for clients' personal and financial circumstances and would result in a significant number of CBG clients with 100% high risk tolerance and objectives of 100% short-term capital appreciation ("STCA").
14. Although these concerns were not addressed, Scotia permitted CBG to implement the Risk Management Program. Thereafter, Scotia approved numerous account documents that recorded high risk tolerance of 100% and an objective of 100% STCA.
15. In or about July 2010, a compliance officer noted "*an overall concern with regards to the margin use and the suitability of trading*" in CBG's accounts and undertook a special project on CBG's highest revenue generating households for review by Compliance senior management.
16. Throughout the relevant period, Scotia compliance officers issued numerous queries to CBG relating to the New Issue Strategy. They expressed concerns about suitability, high turnaround, high commissions, conflict of interest, concentration, and use of margin.
17. CBG represented that their clients were comfortable with the New Issue Strategy and frequently responded to queries by increasing high risk tolerance.
18. Scotia relied on CBG's assurances, the updated risk tolerance and the additional reporting clients received under the Risk Management Program.
19. In late 2012, the Supervisor became concerned about the activity in CBG's accounts and undertook a review, which ultimately focused on CBG's top 8 revenue producing clients. Scotia Compliance assisted with the review, but there were delays and it took over a year to complete.
20. In April 2014, Scotia Compliance recommended that the Supervisor contact the 8 clients whose accounts were reviewed to determine whether there were concerns with account activity or performance. This was the first time that Scotia took steps independent of CBG to confirm that clients were comfortable with their account activity and it was limited to the top 8 clients. One client declined to participate further in the New Issue Strategy and made a formal complaint to Scotia.
21. In April 2014, Scotia Compliance also suggested account restrictions that limited New Issue trading by CBG, but none were implemented.
22. In October 2014, Chabassol commenced a medical leave of absence. In the 11 months following, Scotia received 13 complaints from clients of CBG alleging a variety of issues including unsuitable recommendations and discretionary trading.

23. In April 2017, Bugden entered into a Settlement Agreement with IIROC in which he admitted to making unsuitable recommendations to Client A referred to below and to approving account documentation for Clients B and C without adequate due diligence.
24. Scotia has paid compensation to the complainants in the total amount of \$2,501,729.

### **Unsuitable Trading**

25. The New Issue Strategy was not suitable for at least three CBG clients, having regard to their personal and financial circumstances. The trading in their accounts was not consistent with good business practice due to the significant commissions generated as compared to the unsuitable risk undertaken.

### **Inadequate Supervision**

50. Scotia's approval of the Risk Management Program facilitated mischaracterization of client risk tolerance and objectives by CBG and impeded effective supervision.
51. Scotia routinely approved CBG clients for high risk short-term trading. As of November 2015, approximately half of CBG clients had a high risk tolerance of 100% and an investment objective of 100% STCA.
52. The risk tolerance and objectives for many CBG clients was not consistent with their age, investment knowledge, financial and other circumstances. In approving the risk tolerance and investment objectives, Scotia did not take adequate steps to confirm whether they were suitable for the clients and placed undue reliance on the Risk Management Program.

### **Mitigating Factors**

57. Individual Scotia compliance officers and the Supervisor took proactive and persistent steps to address suitability and other issues associated with CBG's use of the New Issue Strategy. There were numerous queries and several attempts to analyze the impact of the New Issue Strategy on client accounts.
58. Scotia required the Supervisor to contribute \$100,000 to client remediation by way of salary disgorgement.
59. Scotia has paid \$2,501,729 in compensation to clients of CBG.

## **PART V – TERMS OF SETTLEMENT**

61. The Respondent agrees to the following sanctions and costs:
  - a) A fine of \$200,000; and
  - b) The amounts disgorged from the Supervisor in the amount of \$100,000 will be donated by the Respondent to charity.
62. The Respondent will also pay costs to IIROC in the amount of \$20,000.
63. 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.

## **III. ANALYSIS AND REASONS**

¶ 6 During the course of the hearing and in its deliberations the Hearing Panel was concerned, primarily, with two matters:

1. The formulation of the test to determine whether the agreed sanctions and penalty constitute an acceptable disposition of the matter;

2. What is the appropriate procedure to follow when the Hearing Panel requests additional facts which are not included in the Settlement Agreement.

### **The Test to Be Applied**

¶ 7 The leading case of *Milewski (Re)*, [1999] IDACD No. 17 has long been the leading authority on the test to be applied by a Hearing Panel when considering a joint settlement submission. At page 9 of that decision, the Hearing Panel, then called a District Council, wrote as follows:

Although a settlement agreement must be accepted by a District Council before it can become effective, the standards for acceptance are not identical to those applied by a District Council when making a penalty determination after a contested hearing. In a contested hearing, the District Council attempts to determine the correct penalty. A District Council considering a settlement agreement will tend not to alter a penalty that it considers to be within a reasonable range, taking into account the settlement process and the fact that the parties have agreed. It will not reject a settlement unless it views the penalty as clearly falling outside a reasonable range of appropriateness. Put another way, the District Council will reflect the public interest benefits of the settlement process in its consideration of specific settlements.

This understanding is reflected in paragraph 20.26 of the By-laws which authorizes the District Council to “accept”, rather than approve, a settlement agreement. In each case a District Council must determine appropriateness, but the standards applicable to its doing so on a settlement hearing differ from those in a contested hearing. Thus, the penalties imposed under settlement agreements, while relevant to a District Council exercising its discretion to penalize, provide only limited assistance in a hearing like this one.

¶ 8 In the recent case *Bugden (Re)*, 2017 IIROC 30, after considering the test established in *Milewski*, the Panel stated as follows with respect to the settlement process:

[...] The efficacy of the settlement process is a cornerstone of effective and efficient regulatory process. Parties who have engaged in good faith negotiations to reach an agreement that is appropriate in the circumstances and is reasonable in its application of the principles of general and specific deterrence, remedial intent and public interest are entitled to expect the agreement to receive appropriate consideration by a panel. If in its due consideration the panel determines the agreement falls within the governing parameters it should be accepted; if not the agreement should be rejected. The parties would then be free to enter into a subsequent agreement or proceed to a hearing on the merits.

¶ 9 During argument, Staff submitted that the Panel’s role ought to be “somewhat non-interventionist”: there should be no interference with a settlement agreement unless it results in a settlement that is outside the reasonable range of appropriateness. In support of that submission we were referred to *R. v. Anthony-Cook* [2016] 2 S.C.R. 204 in which the Supreme Court of Canada dealt with joint settlement agreements in a criminal case. Moldaver J. wrote the decision for a unanimous court and with respect to the test to be applied in deciding whether to accept or reject the submission said as follows:

[41] But as I have said, for joint submissions to be possible, the parties must have a high degree of confidence that they will be accepted. Too much doubt and the parties may choose instead to accept the risks of a trial or a contested sentencing hearing. The accused in particular will be reluctant to forgo a trial with its attendant safeguards, including the crucial ability to test the strength of the Crown’s case, if joint submissions come to be seen as an insufficiently certain alternative.

[42] Hence, the importance of trial judges exhibiting restraint, rejecting joint submissions only where the proposed sentence would be viewed by reasonable and informed persons as a breakdown in the proper functioning of the justice system. A lower threshold than this would cast the efficacy of resolution agreements into too great a degree of uncertainty. The public interest test ensures that these resolution agreements are afforded a high degree of certainty.

[43] At the same time, this test also recognizes that certainty of outcome is not “the ultimate goal of the sentencing process. Certainty must yield where the harm caused by accepting the joint submission is beyond the value gained by promoting certainty of result” (*R. V. DeSousa*, 2012 ONCA 254, 109 O.R. (3d) 792, per Doherty J.A., at para. 22).

¶ 10 The test propounded by Moldaver J. is one of approval or acceptance of a joint settlement agreement unless to do so would be viewed by reasonable and informed persons as a breakdown in the proper functioning of the justice system. In more traditional words, it is to ascertain whether acceptance would bring the system of justice into disrepute. The Hearing Panel is of the view that viewing the two formulations of the test side by side, they are virtually the same. If anything, the Moldaver test presents a stronger presumption in favour of acceptance of joint settlement submissions than does *Milewski*.

¶ 11 The views of the Hearing Panel in *Bugden (Re)* above quoted are closely parallel to the views expressed by the Supreme Court of Canada in *R. v. Anthony-Cook*. It is in the public interest that joint settlement agreements be encouraged. The standard to be applied by the approving body should be lowered from that which would be applicable in a contested hearing, as it is in the public interest to do so. That fundamental principle applies to all levels of courts and boards and regulatory hearing panels and is not restricted to criminal proceedings alone.

¶ 12 As stated earlier, it is our view that the tests for approval of a joint settlement by the courts applying the *Anthony-Cook* case and an IIROC hearing panel applying the *Milewski* case are so close as to be in substance identical. There is one apparent important difference between the two approval processes which needs to be considered and reconciled if possible. We think it can be.

#### **Where Additional Facts Are Sought**

¶ 13 Section 8428(6) of the IIROC Consolidated Rules is as follows:

##### **8428. Settlement Hearings**

(6) At a settlement hearing, facts that are not contained in the settlement agreement must not be disclosed to the hearing panel without the consent of all parties, unless the respondent does not appear, in which case Enforcement Staff may disclose additional relevant facts, if requested by the hearing panel.

(The sub-rule is also an express term of the Settlement Agreement, paragraph 68.)

¶ 14 There is no similar term in the Criminal Code which applied in the *Re Anthony-Cook* case. There, Moldaver J. had the following to say about disclosure of facts to the court considering the joint settlement:

[54] Counsel should, of course, provide the court with a full account of the circumstances of the offender, the offence, and the joint submission without waiting for a specific request from the trial judge. As trial judges are obliged to depart only rarely from joint submissions, there is a “corollary obligation upon counsel” to ensure that they “amply justify their position on the facts of the case as presented in open court” (Martin Committee Report, at p. 329). Sentencing – including sentencing based on a joint submission – cannot be done in the dark. The Crown and the defence must “provide the trial judge not only with the proposed sentence, but with a full description of the facts relevant to the offender and the offence”, in order to give the judge “a proper basis upon which to determine whether [the joint submission] should be accepted” (*DeSousa*, at para. 15; see also *Sinclair*, at para. 14).

¶ 15 The obligation on Staff in an IIROC case is the same as owed by any lawyer in a prosecutorial role: that is that he or she must make full disclosure to the tribunal of all material facts which bear on the case before it. In terms specific to the present circumstances, Staff must ensure that the hearing panel charged with whether or not to accept a joint settlement has all the facts in Staff’s possession which might reasonably be expected to be material to that decision. If the hearing panel were deprived of such information, it would not only be contrary

to the public interest, it also would hold the administration of justice in disrepute, the measures of both the tests discussed.

¶ 16 Clearly, Staff has the express power to withhold facts and, if it does so, it is open to the hearing panel to refuse to accept the joint settlement. But to do so, it has to know what information has been withheld. If the facts withheld are material but their nature is unknown, there is a serious breakdown in the administration of justice. Thus the role of Staff is crucial in ensuring that the hearing panel has the facts necessary to decide whether to accept a settlement agreement. The right of Staff to withhold facts is unchallenged except to the extent it prevents a hearing panel from having facts material to the exercise of its discretion.

¶ 17 In the course of the hearing in this matter, the Hearing Panel sought further information from the parties, particularly in reference to the book of business affected by the New Issues Strategy. Following a polite discourse between the members of the Hearing Panel and counsel, some information was provided and some was not. After considering the matter, we concluded that the withheld information must not have been material or we would have been given it and therefore we proceeded to accept the joint settlement.

#### IV. THE SANCTIONS

¶ 18 While this case concerns the activities of one of Canada's largest financial institutions, it does not concern a systemic failure of any kind. What is under discussion here is the admitted failure to supervise two registered representatives which resulted in the Respondent having to provide compensation of \$2,501,729 to 13 clients. Further it appears Scotia's somewhat belated investigation of the activities of the registered representatives itself triggered the compensation. There appears to have been no previous history of complaints regarding these registered representatives before Scotia intervened.

¶ 19 Scotia led the internal investigation proactively and cooperated fully with IIROC in bringing it to a resolution; one facet of which was the disciplinary proceedings against one of the registered representatives, D.C. Bugden, the decision in which is referred to earlier in these reasons.

¶ 20 One of the factors we are to consider in assessing the joint agreement is the Respondent's prior regulatory history. We were referred specifically to the decision in *Re Scotia Capital 2015 IIROC 27*, a case in which the Respondent assumed responsibility for the misconduct of an entity which was subsequently acquired by the Respondent's parent and amalgamated with it. As Scotia was simply a successor, we do not regard the case to be a significant consideration in assessing the appropriateness of the present settlement agreement.

¶ 21 For a large financial institution, the magnitude of the fine is less important than the damage to its reputation caused by the notoriety of proceedings such as the present. That said, the fines should be consistent with those levied against similar sized institutions in similar circumstances. The fines must satisfy the principle established in the IIROC Sanction Guidelines that:

The purpose of sanctions in a regulatory proceeding is to protect the public interest by restraining future conduct that may harm the capital markets.<sup>1</sup> 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).

¶ 22 The cases cited by Staff all suggest that the sanctions proposed by the parties are well within the zone of appropriateness and would not bring the administration of justice into disrepute. Our conclusion in that regard was the reason we accepted the settlement. A review of the facts of these cases to identify similarities and differences between each of them and the present case would not be useful. All these cases ultimately turn on their own facts and, particularly when considering a joint settlement agreement, the zone of what is acceptable is quite wide.

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<sup>1</sup> 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.

## V. CONCLUSION

¶ 23 It was for the foregoing reasons that the Hearing Panel granted its acceptance of the Settlement Agreement on the completion of argument and issued an order to that effect on July 5, 2017.

**DATED** this 6<sup>th</sup> day of October, 2017.

John Lorn McDougall

Chair

Daniel Iggers

Panel Member

Richard E. Austin

Panel Member

## APPENDIX

### 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 the staff of IIROC (“Staff”) and Scotia Capital Inc. (“Scotia” or the “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. Between January 2010 and October 2014, two Registered Representatives with Scotia, an IIROC Dealer Member firm, implemented an investment strategy for many of their clients which attempted to take advantage of the difference between the price of new issues and initial public offerings of securities (“New Issues”) and the price on the secondary market (the “New Issue Strategy”).
5. Scotia was aware of concerns raised by its compliance officers and the relevant supervisor about the risks associated with the New Issue Strategy. However, Scotia approved numerous clients for high risk short term trading without adequately considering whether that was suitable for them, failed to fully investigate concerns about the New Issue Strategy, and failed to take effective action.
6. Overall, Scotia failed to adequately supervise the two Registered Representatives and failed to prevent trading for at least three clients that was unsuitable and not consistent with good business practice.

#### The New Issue Strategy

7. Scotia employed David Chabassol (“Chabassol”) and David Bugden (“Bugden”) as Registered Representatives. They worked in a partnership called the Chabassol Bugden Group (“CBG”) from a satellite location of Scotia’s Halifax branch in New Glasgow, Nova Scotia.

8. As of at least 2010, CBG implemented the New Issue Strategy for many of their clients. The New Issue Strategy seeks returns from high-volume short-term trading and thus is only suitable for clients with high risk tolerance and whose objectives include short-term trading. The use of leveraged funds for the New Issue Strategy by some of CBG's clients further increased their risks.
9. In each of 2010, 2011, 2012, 2013 and 2014, the value of purchases that CBG made in all of its accounts was approximately double the value of their total assets under management. New Issues accounted for a significant majority of CBG purchases made in each of those years.
10. When CBG purchased New Issues for their clients, the issuers paid a commission to Scotia, which was shared by Scotia and CBG. Due to the commissions paid by issuers and high turnover, the New Issue Strategy was more profitable than a conventional investment approach.

### **Concerns about CBG and the New Issue Strategy**

11. In late 2009 and early 2010, Scotia compliance officers issued multiple queries related to suitability, high turnover, and concentration in a number of CBG accounts. Significant queries were escalated to CBG's supervisor (the "Supervisor") and senior management for Scotia's compliance department ("Scotia Compliance").
12. In response, Chabassol proposed a so-called "Risk Management Program" specific to certain CBG clients who were involved in the New Issue Strategy. The Risk Management Program defined risk conservatively in order to highlight the high risk nature of the trading strategy. However, this increased the likelihood that for those clients who wished to engage in the strategy, the client risk tolerance and objectives would be set for high risk active trading. It also encouraged risk tolerance and objectives to be set based on the type of trading the clients wished to engage in. Clients received customized risk disclosure packages and more frequent reporting due to the short-term trading.
13. CBG's Supervisor sought guidance from Scotia Compliance about the proposed Risk Management Program. Senior management and the Supervisor expressed concerns that the Risk Management Program did not adequately account for clients' personal and financial circumstances and would result in a significant number of CBG clients with 100% high risk tolerance and objectives of 100% short-term capital appreciation ("STCA").
14. Although these concerns were not addressed, Scotia permitted CBG to implement the Risk Management Program. Thereafter, Scotia approved numerous account documents that recorded high risk tolerance of 100% and an objective of 100% STCA.
15. In or about July 2010, a compliance officer noted "*an overall concern with regards to the margin use and the suitability of trading*" in CBG's accounts and undertook a special project on CBG's highest revenue generating households for review by Compliance senior management.
16. Throughout the relevant period, Scotia compliance officers issued numerous queries to CBG relating to the New Issue Strategy. They expressed concerns about suitability, high turnaround, high commissions, conflict of interest, concentration, and use of margin.
17. CBG represented that their clients were comfortable with the New Issue Strategy and frequently responded to queries by increasing high risk tolerance.
18. Scotia relied on CBG's assurances, the updated risk tolerance and the additional reporting clients received under the Risk Management Program.
19. In late 2012, the Supervisor became concerned about the activity in CBG's accounts and undertook a review, which ultimately focused on CBG's top 8 revenue producing clients. Scotia Compliance assisted with the review, but there were delays and it took over a year to complete.
20. In April 2014, Scotia Compliance recommended that the Supervisor contact the 8 clients whose

accounts were reviewed to determine whether there were concerns with account activity or performance. This was the first time that Scotia took steps independent of CBG to confirm that clients were comfortable with their account activity and it was limited to the top 8 clients. One client declined to participate further in the New Issue Strategy and made a formal complaint to Scotia.

21. In April 2014, Scotia Compliance also suggested account restrictions that limited New Issue trading by CBG, but none were implemented.
22. In October 2014, Chabassol commenced a medical leave of absence. In the 11 months following, Scotia received 13 complaints from clients of CBG alleging a variety of issues including unsuitable recommendations and discretionary trading.
23. In April 2017, Bugden entered into a Settlement Agreement with IIROC in which he admitted to making unsuitable recommendations to Client A referred to below and to approving account documentation for Clients B and C without adequate due diligence.
24. Scotia has paid compensation to the complainants in the total amount of \$2,501,729.

### **Unsuitable Trading**

25. The New Issue Strategy was not suitable for at least three CBG clients, having regard to their personal and financial circumstances. The trading in their accounts was not consistent with good business practice due to the significant commissions generated as compared to the unsuitable risk undertaken.

### ***Client A***

26. Client A became a client of CBG in 2008. Her Know Your Client (“KYC”) information reflected the following circumstances:
  - a) born in 1939;
  - b) retired and widowed;
  - c) “low” investment knowledge;
  - d) income in the range of \$51,000-\$74,000 per year; and
  - e) entire net worth of \$700,000, all of which was liquid and invested with Scotia.
27. As of October 2010, the risk tolerance for Client A’s RRIF was set at 30% low, 60% medium and 10% high and her investment objectives were 30% income, 60% Long Term Capital Appreciation (“LTCA”), and 10% STCA. In June 2013, the high risk tolerance was increased to 35% and STCA allocation was increased to 45% STCA.
28. As of March 2010, the risk tolerance for Client A’s cash account was set at 25% low, 40% medium and 35% high and her investment objectives were 50% LTCA and 50% STCA. In August 2014, Client A’s risk tolerance was slightly increased to 20% low, 45% medium and 35% high.
29. The risk increases in Client A’s accounts were made in response to suitability queries.
30. Between 2012 and 2014, CBG implemented the New Issue Strategy in Client A’s accounts. During these two years, CBG purchased a total of 97 New Issues in her portfolio.
31. In 2012, the value of the New Issues purchased in both of Client A’s accounts was more than double the account holdings.
32. The New Issues traded in Client A’s accounts from 2012-2014 generated approximately \$47,000 in gross commissions for Scotia and CBG, in addition to regular account fees.
33. The trading in Client A’s account exceeded her stated risk tolerance and was unsuitable as well as inconsistent with good business practice due to the commissions generated.

### ***Client B***

34. Client B became a client of CBG in 2010 when she opened an RRSP and margin account. The KYC information reflected the following circumstances:
- a) born in 1971;
  - b) widowed with two dependent children;
  - c) “low” investment knowledge;
  - d) income of less than \$25,000 per year;
  - e) fixed assets of \$200,000 and liquid assets of \$400,000, all of which was invested with Scotia; and
  - f) risk tolerance 100% high and investment objectives 100% STCA.
35. In May 2011, Client B opened an RESP account. The KYC form reflected the same circumstances, risk tolerance and objectives.
36. Scotia approved the account opening forms for Client B without query, even though the risk tolerance, investment objectives and use of margin did not appear suitable for someone with Client B’s personal and financial circumstances.
37. Client B was added to the Risk Management Program, even though she had low investment knowledge, and relatively modest financial means.
38. CBG implemented the New Issue Strategy in Client B’s account. From January 2010 until November 2014, CBG effected 280 purchases in Client B’s accounts, including 70 New Issues.
39. In 2012, Client B’s entire portfolio was turned over more than 3 times and in 2013, her entire portfolio was turned over more than 5 times.
40. The trading in Client B’s accounts generated approximately \$60,000 in gross commissions for Scotia and CBG. Approximately \$31,000 of this amount related to New Issues.
41. Client B’s risk tolerance and investment objectives were overstated and permitted too much risk for her personal and financial circumstances. The trading in Client B’s accounts exceeded her actual risk tolerance and was unsuitable and inconsistent with good business practice due to the commissions generated.
42. Client B was in a transaction-based account and she paid commissions to Scotia on purchases of non-New Issue securities and sales of all securities in her account. Due to the active trading in Client B’s account, a fee-based account would have been more suitable.
43. Client B suffered significant losses in the approximate amount of \$190,000. Scotia proactively reached out to client B in order to facilitate the compensation process despite the fact that Client B had not complained. Scotia offered her full compensation.

### ***Client C***

44. Client C had been a client of CBG since 2004 with a single cash trading account. In June 2012, Chabassol submitted an Account Agreement Modification Form which reflected the following circumstances:
- a) born in 1919;
  - b) homemaker;
  - c) “moderate” investment knowledge;

- d) income in the range of \$25,000-\$50,000 per year;
  - e) fixed assets of \$80,000 and liquid assets of \$210,000, all of which was invested with Scotia; and
  - f) risk tolerance increased from 100% medium, to 70% medium and 30% high, and investment objectives changed from 90% LTCA and 10% STCA to 70% LTCA and 30% STCA.
45. Scotia approved the Account Agreement Modification Form without query, even though the high risk tolerance and investment objectives did not appear suitable for someone with Client C's personal and financial circumstances.
46. CBG implemented the New Issue Strategy in Client C's account. From January 2010 until November 2014, CBG effected 117 purchases for Client C, including 80 New Issues.
47. In 2012 Client C's account was turned over approximately 4.8 times and in 2013 her account was turned over approximately 2.9 times.
48. The New Issues traded in Client C's accounts generated approximately \$31,000 in gross commissions for Scotia and CBG, in addition to regular account fees.
49. Between 2010 and 2014, Client C experienced modest returns. However, Client C's risk tolerance and investment objectives were overstated and permitted too much risk for her personal and financial circumstances. The trading in Client C's account exceeded her actual risk tolerance and was unsuitable and inconsistent with good business practice due to the commissions generated.

#### **Inadequate Supervision**

50. Scotia's approval of the Risk Management Program facilitated mischaracterization of client risk tolerance and objectives by CBG and impeded effective supervision.
51. Scotia routinely approved CBG clients for high risk short-term trading. As of November 2015, approximately half of CBG clients had a high risk tolerance of 100% and an investment objective of 100% STCA.
52. The risk tolerance and objectives for many CBG clients was not consistent with their age, investment knowledge, financial and other circumstances. In approving the risk tolerance and investment objectives, Scotia did not take adequate steps to confirm whether they were suitable for the clients and placed undue reliance on the Risk Management Program.
53. Given the high volume of trading associated with the New Issue Strategy, Scotia had many opportunities to detect and query unsuitable risk tolerance, objectives, and trading on daily and monthly reviews. For example, the accounts of Clients A, B and C exceeded the threshold for monthly review by Tier 1 as follows:
- a) for Client B, 11 times between January 2010 and November 2014;
  - b) for Client C, 6 times between January 2010 and November 2014; and
  - c) for Client A, 4 times in 2012.
54. Client B's accounts also exceeded the commission threshold for monthly review by Tier 2 in September 2012.
55. The daily and monthly reports include summaries of KYC information. Compliance officers queried CBG about potentially unsuitable trading and, in some cases, risk tolerance and objectives. Many queries were escalated to senior management, however Scotia did not take effective action and CBG was permitted to continue the New Issue Strategy for Clients A, B, and C and others for whom it was potentially unsuitable.
56. Since Clients A, B, and C were not among CBG's top 8 revenue producing clients, their accounts were

not examined by Scotia in the 2010 or 2012 reviews. Scotia's reviews were inadequate in that they did not include clients with smaller accounts who were vulnerable, despite documented concerns.

### **Mitigating Factors**

57. Individual Scotia compliance officers and the Supervisor took proactive and persistent steps to address suitability and other issues associated with CBG's use of the New Issue Strategy. There were numerous queries and several attempts to analyze the impact of the New Issue Strategy on client accounts.
58. Scotia required the Supervisor to contribute \$100,000 to client remediation by way of salary disgorgement.
59. Scotia has paid \$2,501,729 in compensation to clients of CBG.

### **PART IV – CONTRAVENTIONS**

60. By engaging in the conduct described above, the Respondent committed the following contravention of IIROC's Rules:

From January 2010 to October 2014, the Respondent Scotia Capital Inc. failed to adequately supervise two Registered Representatives when they recommended securities transactions that were not suitable for their clients and were not in keeping with good business practice, contrary to IIROC Dealer Member Rules 38.1 and 2500.

### **PART V – TERMS OF SETTLEMENT**

61. The Respondent agrees to the following sanctions and costs:
  - a) A fine of \$200,000; and
  - b) The amounts disgorged from the Supervisor in the amount of \$100,000 will be donated by the Respondent to charity.
62. The Respondent will also pay costs to IIROC in the amount of \$20,000.
63. 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**

64. 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 following paragraph.
65. 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**

66. This Settlement Agreement is conditional on acceptance by the Hearing Panel.
67. 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.
68. 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.

69. 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.
70. 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.
71. The terms of this Settlement Agreement are confidential unless and until this Settlement Agreement has been accepted by the Hearing Panel.
72. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel and IIROC will post a full 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.
73. If this Settlement Agreement is accepted, the Respondent agrees that neither it nor anyone on its behalf, will make a public statement inconsistent with this Settlement Agreement.
74. 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**

75. This Settlement Agreement may be signed in one or more counterparts which together will constitute a binding agreement.
76. A fax or electronic copy of any signature will be treated as an original signature.

**DATED** this “19” day of June, 2017.

“Witness” \_\_\_\_\_

Witness

“Scotia Capital Inc.” \_\_\_\_\_

Scotia Capital Inc.

“Rob Delfrate” \_\_\_\_\_

Witness

“Elissa Sinha” \_\_\_\_\_

Elissa Sinha

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

The Settlement Agreement is hereby accepted this “5” day of “July”, 2017 by the following Hearing Panel:

Per: “John L McDougall, Q.C.” \_\_\_\_\_

Panel Chair

Per: “Daniel Iggers” \_\_\_\_\_

Panel Member

Per: “Richard E. Austin” \_\_\_\_\_

Panel Member