

Re Mackie Research & McCarthy

IN THE MATTER OF:

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

and

Mackie Research Capital Corporation

and

Patrick McCarthy

2019 IIROC 29

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

Heard: October 3, 2019 in Toronto, Ontario

Decision: October 3, 2019

Reasons for Decision: November 15, 2019

Hearing Panel:

Joan Smart, Chair, Dave Persaud and Guenther Kleberg

Appearance:

Charles Corlett, Enforcement Counsel

Doug McLeod, for Mackie Research Capital Corporation and Patrick McCarthy

Patrick McCarthy and Patrick Walsh

REASONS FOR DECISION

I. INTRODUCTION

¶ 1 Proceedings were commenced by the Investment Industry Regulatory Organization of Canada (“IIROC”) against Mackie Research Capital Corporation (“MRCC”) and Patrick McCarthy (“McCarthy”) (together “the Respondents”) by a Notice of Application for Settlement Hearing. The issue before the Hearing Panel at the hearing on October 3, 2019 was whether to accept or reject a settlement agreement between IIROC and the Respondents (the “Settlement Agreement”). After reviewing the Settlement Agreement and hearing the submissions of the parties, the Hearing Panel decided to accept the Settlement Agreement. These are our reasons for that decision.

II. RESPONDENTS’ ADMITTED VIOLATIONS

¶ 2 The Respondents admitted to the following violations of IIROC’s Rules:

- a) McCarthy – In July 2014, McCarthy failed to comply with MRCC’s policies and procedures for

the receipt and containment of confidential information and failed to address that he was in possession of confidential information regarding a proposed financing, contrary to Dealer Member Rule 29.1; and

- b) MRCC – In July 2014, MRCC failed to establish and enforce adequate policies and procedures for the receipt and containment of confidential information regarding a proposed financing, contrary to Dealer Member Rule 38.1

III. AGREED FACTS

¶ 3 Set out below is a summary of the pertinent facts that the Respondents agreed to for the purposes of the Settlement Agreement. A copy of the Settlement Agreement is attached to these Reasons for Decision.

McCarthy's Role at MRCC

¶ 4 MRCC is a full-service investment firm and Dealer Member.

¶ 5 McCarthy joined MRCC in June 2014. During the relevant period, McCarthy worked at MRCC as an institutional sales trader. His role included sales and marketing of issuers to institutional clients.

¶ 6 McCarthy was not a member of MRCC's corporate finance group and would not, in the ordinary course of his duties, work on corporate finance transactions for MRCC's clients.

The Issuer XYZ

¶ 7 MRCC had led a financing for XYZ in 2013 and had a right of first refusal to lead future financings for XYZ that was to expire in December 2014.

¶ 8 XYZ was on MRCC's Focus List. MRCC sales and trading teams were encouraged to focus their efforts in promoting issuers on the Focus List. The list reflected market intelligence comprised of publicly available information.

¶ 9 By June 2014, it was generally known in the marketplace that XYZ was seeking to expand its investor base, improve liquidity, and potentially require a financing to fund announced growth initiatives.

McCarthy's Marketing Efforts Regarding XYZ

¶ 10 Upon commencement of his employment with MRCC, McCarthy worked with management of XYZ to facilitate introductions to institutional investors as part of his ordinary course marketing activities. He concluded that XYZ was undervalued, was relatively unknown and would require additional capital to facilitate its planned expansion.

¶ 11 McCarthy arranged a meeting between XYZ and members of MRCC's corporate finance group that was held on July 2, 2014. McCarthy did not attend the meeting.

¶ 12 McCarthy continued his activities relating to XYZ throughout July 2014, which included presenting XYZ to potential investors and facilitating secondary market trading.

MRCC's Corporate Finance Proposals to XYZ

¶ 13 Following the July 2, 2014 meeting, MRCC's corporate finance group proposed a \$7.5 million bought deal offering to XYZ. The proposal was rejected, but discussions between XYZ and MRCC corporate finance continued. McCarthy was not a party to those discussions or to discussions within MRCC's corporate finance group.

¶ 14 On July 15, 2014, MRCC corporate finance notified the compliance department of the addition of XYZ to the Watch List for a proposed financing. McCarthy was not added to the Watch List and was not notified of

the addition.

¶ 15 Later that day, MRCC presented a further \$5 million bought deal at \$9.50 per share to XYZ. That proposal and two subsequent proposals made on July 21 and July 24, 2014, were rejected.

¶ 16 On July 30, 2014, XYZ accepted a bought deal proposal from MRCC, resulting in a press release on July 31, 2014 announcing that MRCC would co-lead a \$5 million prospectus offering at \$9.50 per share. The offering was later upsized to \$6.5 million.

McCarthy's Exposure to Confidential Information Regarding Potential XYZ Financing

¶ 17 During July 2014, in the course of his parallel marketing and institutional trading activities, McCarthy became aware that MRCC and XYZ were engaged in discussions about a potential prospectus offering.

¶ 18 In mid-July 2014, to assist him in his marketing activities and to estimate the enterprise value of XYZ, McCarthy asked a junior MRCC analyst in corporate finance to help him analyze XYZ's prospects. On July 18, 2014, the analyst prepared a financial analysis which included among its assumptions that XYZ would require a future potential financing of \$5 million at \$9.50 per share. The share price of illiquid XYZ was then fluctuating with a bid-ask spread ranging from \$8.50 to \$10.00 per share.

¶ 19 While it was not alleged that the subject financial analysis contained disclosure of the specific terms of the final deal, the inclusion of specific deal terms in the analysis at a time when McCarthy knew that XYZ and MRCC were in discussions ought to have prompted McCarthy to take precautionary steps.

¶ 20 In a July 21, 2014 e-mail exchange between McCarthy and XYZ management, which was in the ordinary course of McCarthy's duties and concerned a marketing presentation, XYZ management stated:

"Happy to, however, I have to wait until any issues surrounding a potential financing are sorted out. I have been told by legal counsel not to do a single presentation as that would be considered pre-marketing...hopefully this will clear today or tomorrow."

¶ 21 As of July 21, 2014, McCarthy should have been aware he was in receipt of confidential information as the statement from XYZ management that XYZ's legal counsel had advised against pre-marketing was, in the context, information that XYZ was anticipating a prospectus offering.

¶ 22 After receipt of the information described above, McCarthy did not take precautionary steps such as consulting with MRCC's compliance department on permissible activities and safeguarding the information.

MRCC's Policies and Procedures

¶ 23 During the relevant period, MRCC's policies and procedures required MRCC employees who knew or believed they were exposed to confidential information relating to a public company to advise compliance immediately. Compliance would then determine the steps to be taken to protect the employee and the confidential information. That could result in the employee being placed "over the wall".

¶ 24 In failing to adequately consider whether he had been exposed to confidential information relating to a public company, McCarthy contravened MRCC's policies.

¶ 25 During the relevant period, MRCC's policies and procedures on the receipt and containment of confidential information operated largely on the basis of a Watch List. When MRCC was in receipt of confidential information regarding a financing, the corporate finance lead was to compile a list of the individuals working on the transaction and communicate that to compliance. The activities of anyone "brought over the wall" would be restricted until the information was no longer confidential.

¶ 26 McCarthy was not brought "over the wall" in respect of XYZ.

MRCC's Failure to Supervise

¶ 27 When McCarthy was hired in June 2014, MRCC failed to adequately consider that McCarthy's sales and marketing activities, which included fostering relationships between issuers and corporate finance, might expose him to confidential information and require safeguards. MRCC also did not adequately consider how it should apply its policies and procedures to supervise McCarthy.

¶ 28 Senior representatives of MRCC ought to have known, based on communications with McCarthy during the relevant period, that he had access to information about a potential financing of XYZ and ought to have taken precautionary steps, including potentially placing McCarthy on the Watch List.

¶ 29 As a result of failing to implement sufficiently robust controls, MRCC was unable to appropriately monitor activities outside of corporate finance with respect to XYZ and ensure that confidential information concerning the pending XYZ offering was contained.

Improvements Made by MRCC

¶ 30 Following the events described above, MRCC made improvements to its compliance policies and procedures regarding the receipt and containment of confidential information and provided clearer guidance regarding the identification of market sensitive confidential information.

¶ 31 Policy amendments made in October 2014 contemplate circumstances such as those involving McCarthy and XYZ by expressly capturing individuals outside of corporate finance who may need to be brought "over the wall" and have their activities restricted and monitored.

IV. ANALYSIS

Role of the Hearing Panel

¶ 32 According to Rule 8215 (5) of IIROC's Consolidated Enforcement, Examination and Approval Rules, a Hearing Panel may either accept or reject a settlement agreement.

¶ 33 As was noted in the case of *Re Milewski* [1999] I.D.A.C.D. No.17 at page 9:

"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 agreement 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."

¶ 34 Our task is not to decide what penalty we would have imposed in the case, but rather to determine whether the agreed penalty falls within an appropriate range of appropriateness, taking into account the conduct in issue, the protection of the public and the integrity of the capital markets.

McCarthy

¶ 35 Dealer Member Rule 29.1 provided that each employee of a Dealer Member shall observe high standards of ethics and conduct in the transaction of their business.

¶ 36 McCarthy's breach of Rule 29.1 arose when he continued his marketing and trading activities with respect to XYZ without sufficiently considering whether he had been exposed to confidential information regarding a potential financing and whether he needed to take proactive steps such as contacting MRCC's compliance department and restricting his institutional activities. Those failures were also contrary to MRCC's policies under which McCarthy should have informed MRCC compliance that he was in possession of confidential information.

¶ 37 The Settlement Agreement refers to the information that McCarthy possessed about XYZ as confidential information and does not reflect any finding as to whether or not the information was material. As was noted in National Policy 51-201 on Disclosure Standards, in making a determination on materiality, one must take into account a number of factors that can not be captured in a bright line test. However, it lists the public sale of securities as an example of information that may be material.

¶ 38 We do not believe it is critical to our decision with respect to the Settlement Agreement that a determination be made as to materiality of the subject information about XYZ. The information about a potential \$5 million public financing for a company whose shares were trading in the \$8.50 to \$10 range was such that McCarthy ought to have considered the nature of the information, including whether it was material, and taken appropriate steps.

¶ 39 As admitted by McCarthy, he failed to comply with MRCC's policies and procedures for the receipt and containment of confidential information and failed to address that he was in possession of confidential information regarding a proposed financing, contrary to Dealer Member Rule 29.1.

MRCC

¶ 40 Dealer Member Rule 38.1 requires that Dealer Members establish and maintain a system to supervise the activities of each employee that is reasonably designed to achieve compliance with the Rules of IIROC and all other laws, regulations and policies applicable to the Dealer Member's securities business.

¶ 41 MRCC had some policies and procedures in place at the relevant time which were intended to address the receipt and containment of confidential information.

¶ 42 However, as admitted by MRCC, the firm failed to:

- a) upon hiring McCarthy, sufficiently consider how he could potentially be exposed to confidential information about proposed offerings when marketing public issuers;
- b) establish or enforce sufficiently robust written policies and procedures and safeguards; and
- c) place McCarthy on the Watch List to allow compliance to adequately supervise his trading activities in XYZ.

¶ 43 MRCC failed to maintain an adequate system of controls that could reasonably ensure its policies and procedures were followed, resulting in the failure to prevent the subject contraventions.

¶ 44 As admitted by MRCC, in July 2014, MRCC failed to establish and enforce adequate policies and procedures for the receipt and containment of confidential information regarding a proposed financing, contrary to Dealer Member Rule 38.1.

Sanctions

¶ 45 The Respondents agreed to the following sanctions and costs:

- a) McCarthy
 - (i) a fine of \$100,000;
 - (ii) a suspension of approval for 1 month beginning October 14, 2019;
 - (iii) completion of the Partners, Directors and Senior Officers Course within 12 months of acceptance of the Settlement Agreement; and
 - (iv) costs of \$5000.
- b) MRCC

- (i) a fine of \$180,000; and
- (ii) costs of \$20,000.

¶ 46 IIROC's Sanction Guidelines set out a number of key factors to be considered by Hearing Panels in determining an appropriate sanction and are reflective of factors that have been considered by Hearing Panels in past cases. The factors set out in those Guidelines that are relevant and that we have considered in this case include:

- a) whether the Respondent engaged in numerous acts and /or a pattern of misconduct;
- b) whether the Respondent engaged in the misconduct over an extended period of time;
- c) whether the misconduct was intentional, wilfully blind or reckless with respect to regulatory requirements;
- d) whether the Respondent attempted to conceal his or her misconduct;
- e) the extent to which the Respondent obtained or attempted to obtain a financial benefit from the misconduct;
- f) the extent of harm to clients or other market participants;
- g) the extent of harm to market integrity or the reputation of the marketplace, or both;
- h) the respondent's relevant disciplinary history; and
- i) whether the Respondent voluntarily employed subsequent corrective measures to revise procedures to avoid recurrence of the misconduct.

¶ 47 In our view, the Respondents' contraventions in this case were serious and the sanctions must reflect that. It is critical to the integrity of the capital markets that confidential information about issuer transactions be appropriately safeguarded within Dealer Members.

¶ 48 IIROC counsel expressed the view that the sanctions should exceed the \$265,000 in revenue received by MRCC in respect of the XYZ transaction. While the Respondents agreed to the sanctions, their counsel emphasized that this was not a case where the fine should be seen as disgorgement of ill-gotten gains. We agree with both of those positions.

¶ 49 We believe the sanction must also be such that it will encourage other capital market participants to adopt and follow policies and procedures that are adequate for their securities-related business, particularly in respect of protecting confidential information.

¶ 50 In determining the sanction for McCarthy, we considered the fact that he was an experienced capital markets participant who was subject to a high standard of conduct and ought to have been aware of the need to safeguard confidential information about issuer transactions and followed his firm's policies and procedures in that regard.

¶ 51 We also considered the fact that McCarthy had previously entered into a settlement agreement with the Ontario Securities Commission (the "OSC") and been sanctioned in 2004 for facilitating a transaction in the secondary market, in which shares of an issuer were sold by persons with knowledge of a material fact which had not generally been disclosed, to persons who had no knowledge of that fact, while the issuer was on his firm's Restricted List.¹ However, a number of years have passed between that and the current case, during which time no other regulatory actions have been taken against McCarthy.

¹ *Re Paradigm, McCarthy and Rahim*, 2004 OSC 11

- ¶ 52 The Hearing Panel considered several significant mitigating factors in this case, including that:
- a) the case involved only one issuer transaction;
 - b) the subject events took place over a short period of time;
 - c) there was no allegation of intentional misconduct by either Respondent;
 - d) there was no deliberate attempt by McCarthy to acquire the confidential information;
 - e) there was no evidence that McCarthy had misused the confidential information for his personal benefit;
 - f) there was no evidence of client harm;
 - g) MRCC took proactive steps to improve its policies and procedures relating to confidential information;
 - h) the Respondents, by entering into the Settlement Agreement and attending the hearing, demonstrated that they accepted responsibility for their failures; and
 - i) the Respondents, by entering into the Settlement Agreement, saved IIROC the time and expense of a contested hearing on the merits.

¶ 53 IIROC counsel referred us to several previous IIROC and OSC cases that involved issues relating to confidential or material non-public information. As the facts differed significantly from the facts in this case, they provided limited precedential value. However, we noted that the proposed sanctions in the case at hand tended to be higher.

¶ 54 In our view, the seriousness of the contraventions, as well as the mitigants, are reasonably reflected in the size of the fines, and the suspension for McCarthy which, while short, will have an impact on him. Also, the requirement that he take additional training will serve to remind him of his compliance obligations.

¶ 55 In this case, we were particularly reluctant to interfere with the Settlement Agreement, given that we believed it was the product of extensive negotiation and compromise between the parties represented by experienced counsel who would have given serious consideration to the issues. The Settlement Agreement led to a much more expeditious resolution of the matter than a contested hearing where we expect the issues would have been vigorously contested. As a result, there was considerable benefit to the regulatory process in accepting the Settlement Agreement.

¶ 56 We found that the agreed sanctions in the Settlement Agreement fell within a reasonable range of appropriateness, having regard to the conduct at issue, the protection of the public and the integrity of the capital markets. We also believe they will serve as both a specific and a general deterrent. Accordingly, we decided to accept the Settlement Agreement.

Dated at Toronto this 15 day of November, 2019.

Joan Smart

Dave Persaud

Guenther Kleberg

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 Mackie Research Capital Corporation (“MRCC”) and Patrick McCarthy (“McCarthy”) (together, 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. In July 2014, MRCC was engaged in discussions with XYZ Corporation (“XYZ”) regarding a proposed financing. The public announcement for this financing was made on July 31, 2014.
5. In late July, while engaged in marketing XYZ, McCarthy was exposed to confidential information regarding a potential prospectus offering, which both he and MRCC failed to recognize and properly address.
6. Following receipt of this confidential information, McCarthy continued his marketing activities up to and following the public announcement of the deal. In doing so, McCarthy failed to sufficiently consider whether he had been exposed to confidential information regarding a potential financing, and whether he needed to take proactive steps in response, such as consulting with MRCC’s compliance department and restricting his institutional trading activities.
7. For its part, upon hiring McCarthy in June 2014, MRCC failed to sufficiently consider how McCarthy could potentially become exposed to confidential information about proposed offerings when marketing public issuers, including through communications with other MRCC personnel, such as corporate finance staff. MRCC did not establish or enforce sufficiently robust written policies and procedures and safeguards. MRCC failed to place McCarthy on the Watch List in a timely manner to allow compliance personnel to adequately supervise his trading activities in XYZ.
8. Subsequent to these events and prior to IIROC’s investigation, MRCC made improvements to its policies and procedures concerning the receipt and containment of confidential information regarding potential financings.

Background

9. MRCC is a full-service investment firm and Dealer Member with its head office located in Toronto.
10. McCarthy joined MRCC in June 2014, shortly before the events at issue. During the period of the events at issue, McCarthy worked at MRCC as an Institutional Sales Trader. McCarthy’s role included sales and marketing of issuers to institutional accounts.
11. While McCarthy’s role at MRCC could encompass the sale of private placements to investor clients, McCarthy was not a member of MRCC’s banking group and would not, in the ordinary course of his duties, work on offerings or other corporate finance transactions for MRCC’s clients.

The Issuer

12. MRCC had previously led a financing for XYZ in November 2013 and had an active right of first refusal to lead future financings that was to expire in December 2014.
13. XYZ was on MRCC's Focus List. The Focus List was maintained by a committee comprised of members of MRCC's banking and institutional sales and trading teams. The Focus List was distributed to the sales and trading teams who were encouraged to focus their respective efforts in promoting issuers that appeared on the list. The list reflected market intelligence comprised of publicly available information and did not contain or constitute confidential information.
14. By June 2014, it was generally known within the marketplace that XYZ was seeking to expand its investor base, improve liquidity, and potentially require a financing to fund announced and committed growth initiatives.

McCarthy's Marketing Efforts

15. Upon commencement of his employment with MRCC in June 2014, McCarthy worked with management of XYZ to facilitate introductions to institutional investors. McCarthy concluded that XYZ was undervalued, relatively unknown, and would require additional capital to facilitate its planned expansion. McCarthy presented this favourable assessment of XYZ to institutional clients and arranged one-on-one institutional meetings with management as part of his ordinary-course marketing activities.
16. These marketing efforts contributed to significant investor demand, including, in late June 2014, attracting the attention of a substantial institutional investor who wanted to establish a large position in XYZ.
17. McCarthy and XYZ worked together and independently to locate sellers in the marketplace to satisfy the demand but were stymied by the stock's illiquidity. In response to the growing demand and lack of corresponding shares on offer, McCarthy and XYZ management discussed the possibility of arranging a private placement offering.
18. As a result, McCarthy arranged a meeting between XYZ and members of MRCC's corporate finance group that was held on July 2, 2014. McCarthy did not attend this meeting.
19. McCarthy continued his marketing activities throughout July 2014. This included presenting XYZ to potential investors and facilitating secondary market trading.
20. In order to assist him in his marketing activities, and to estimate the enterprise value of XYZ, in mid-July 2014, McCarthy asked a junior MRCC analyst in corporate finance to help him analyze XYZ's prospects. On July 18, 2014, the analyst prepared a financial analysis which included amongst its assumptions that XYZ would require a future potential financing of \$5 million at \$9.50 per share. The share price of the illiquid XYZ was at this time fluctuating with a bid-ask spread ranging from \$8.50 to \$10.00 per share.

MRCC Corporate Finance Proposals to XYZ

21. Following the July 2, 2014 meeting, instead of pursuing a private placement, MRCC's corporate finance group proposed a \$7.5 million "bought deal" offering to XYZ. The proposal was rejected, but discussions between XYZ and MRCC corporate finance continued. McCarthy was not party to discussions between the corporate finance group and XYZ and was not party to discussions held within MRCC's corporate finance group.
22. On July 15, 2014, MRCC corporate finance staff notified the compliance department of XYZ's addition to the Watch List for a proposed financing. McCarthy was not added to the Watch List and was not notified of XYZ's addition to the list.

23. Later that day, MRCC presented a further \$5 million bought deal at \$9.50 per share to XYZ. This proposal was rejected, as were two subsequent revised proposals made on July 21, 2014 and July 24, 2014. Throughout this time, discussions between the parties regarding the terms of the potential offering continued.
24. On July 30, 2014, XYZ accepted a bought deal proposal from MRCC resulting in a press release on July 31, 2014 announcing that MRCC would co-lead a \$5 million prospectus offering at \$9.50 per share. The size of the offering was later upsized to \$6.5 million.

McCarthy's Exposure to Confidential Information Regarding a Potential Financing

25. During the July events described above, in the course of his parallel marketing and institutional trading activities, McCarthy became aware that MRCC and XYZ were engaged in discussions that had advanced beyond a private placement and had moved toward a prospectus offering.
26. McCarthy's awareness is reflected in part by the assumptions in the financial analysis he received from the MRCC analyst on July 18, 2014. While it is not alleged that the financial analysis contained disclosure of the specific terms of the July 31, 2014 offering per se, the inclusion of an assumption with specific deal terms within the analysis, at a time when McCarthy knew MRCC corporate finance was in discussions with the issuer, should have prompted McCarthy to take precautionary steps regarding the potential receipt of confidential information.
27. McCarthy's specific awareness of an impending offering is reflected in a July 21, 2014 email exchange with XYZ management. While McCarthy's email to management on that date had been in the ordinary course of his duties and concerned a marketing presentation, as part of XYZ management's response to McCarthy, XYZ management stated:

"Happy to, however I have to wait until any issues surrounding a potential financing are sorted out. I have been told by legal counsel not to do a single presentation as that would be considered pre-marketing...hopefully this will clear today or tomorrow."
28. The statement from XYZ management that XYZ's legal counsel had advised against pre-marketing was, in the context, information that XYZ was anticipating a prospectus offering.
29. Accordingly, by July 18, 2014, McCarthy should have been aware that he was potentially in receipt of confidential information, and by July 21, 2014, appreciated that he was in receipt of confidential information that a prospectus offering was being considered by XYZ. McCarthy should have taken precautionary measures such as consulting with MRCC's compliance department on permissible activities, and thus failed to take adequate steps to determine if the information he was exposed to was in fact confidential and safeguard this information appropriately.
30. McCarthy failed to address whether he needed to restrict or limit his institutional marketing and institutional trading activity. As a result, McCarthy's conduct fell below the standards expected of an experienced participant in the capital markets.

MRCC Policies and Procedures and the Watch List

31. During the Relevant Period, MRCC policies and procedures contained a self-reporting obligation for employees exposed to confidential information. This "self-determination" test required MRCC employees who knew or believed they were exposed to confidential information relating to a public company to advise compliance immediately. Compliance would then determine the steps to be taken to protect the employee and the confidential information. This could result in the employee being placed

“over the wall”. In failing to adequately consider whether he had been exposed to confidential information, McCarthy was in contravention of MRCC’s policies in this regard.

32. During the Relevant Period, MRCC’s policies and procedures on the receipt and containment of confidential information operated in large part on the basis of a Watch List. The Watch List was used to identify issuers “for which persons in possession of confidential/non-public information are restricted from trading.”
33. During the time of the events discussed above, responsibility for the Watch List lay with the senior MRCC corporate finance personnel in charge of a given financing. When MRCC was in receipt of confidential information, the corporate finance lead was to compile a list of the individuals working on the transaction and communicate that list to compliance. The activities of anyone brought “over the wall” as a result would be restricted until the information learned was no longer confidential. Compliance enforced the policy through monitoring trading activity, amongst other steps.
34. McCarthy was not a member of MRCC’s corporate finance group and, as noted above, in the case of XYZ, was not brought over the wall by corporate finance.
35. In October 2014, this policy was substantively amended to contemplate circumstances such as those involving McCarthy and XYZ, by expanding the policy to expressly capture individuals outside of corporate finance:

“When an employee outside of Corporate Finance is brought “over the wall”, this information must be communicated to the compliance department to ensure that the Watch List is properly monitored. An example of this would be an Institutional representative is brought over the wall intentionally, to bring expertise to the table. This person will have the full understanding that he/she will be put under restrictions (i.e. no research, no solicitation to clients, etc.) until the potential deal is complete.”

Failure to Supervise by MRCC

36. At the time McCarthy was hired in June 2014, MRCC failed to adequately consider that McCarthy’s contemplated sales and marketing activities, which included fostering the relationship between issuers and investment banking, might expose McCarthy to confidential information and require precautionary safeguards. MRCC did not adequately consider how it should apply and enforce its policies and procedures to supervise McCarthy and how it should review and assess his activities.
37. Senior representatives of MRCC ought to have known, based on communications with McCarthy during the period in question, that McCarthy had access to information concerning a potential financing of XYZ and followed-up accordingly. MRCC ought to have considered precautionary steps, including potentially placing McCarthy on the Watch List.
38. As a result of its failure to enact and enforce sufficiently robust controls, MRCC was unable to appropriately monitor and review activities occurring outside of investment banking with respect to XYZ and thus failed to ensure that confidential information concerning the pending XYZ offering was contained. By failing to appreciate the nature of McCarthy’s role in regard to XYZ, MRCC failed to maintain an adequate system of controls that could reasonably ensure its policies and procedures were followed, resulting in the failure to prevent the contraventions set out herein.

Improvements Made by MRCC

39. Following these events, improvements were made to MRCC compliance policies and investment banking

activities regarding the receipt and containment of information. MRCC revised its policies and supervisory processes and has provided clearer guidance regarding the identification of market sensitive confidential information. The MRCC Policies and Procedures Manual was revised to set out more practical and detailed protocols to address the receipt and containment of confidential information protocols by all employees.

40. As discussed above, in October 2014, the MRCC Watch List policy was substantively revised to contemplate the curtailing of activities of employees that are brought over the wall.
41. The accuracy and integrity of the Watch List is maintained through an email communication review for all issuers placed on the Watch List to determine whether the issuer was placed on the Watch List within an appropriate timeframe, and whether an individual outside of corporate finance should be identified as being “over the wall”. In conjunction with the email communication review, all trading in the issuer is reviewed.
42. Furthermore, MRCC’s policies and procedures have also been amended to include a separate “Wallcrosser List”, wherein the compliance department monitors the activity of individuals outside of corporate finance exposed to confidential information.

Additional Factors

43. The events discussed above occurred over a short period of time and there was no evidence of harm to any clients.
44. MRCC’s gross corporate finance revenue for the XYZ offering was \$265,000 of which \$42,400 was allocated to Institutional Sales and Trading.
45. While MRCC and McCarthy fully accept responsibility for their failures to appreciate and appropriately react to confidential information, it is not alleged that they engaged in intentional misconduct.
46. By settling, the Respondents have saved the need for a lengthy and costly hearing. It has also indicated the parties’ acceptance of their responsibilities.

PART IV – CONTRAVENTIONS

47. By engaging in the conduct described above, the Respondents committed the following contraventions of IIROC’s Rules:

MRCC

- (i) In July 2014, MRCC failed to establish and enforce adequate policies and procedures for the receipt and containment of confidential information regarding a proposed financing, contrary to Dealer Member Rule 38.1.

Patrick McCarthy

- (ii) In July 2014, McCarthy failed to comply with MRCC’s policies and procedures for the receipt and containment of confidential information and failed to address that he was in possession of confidential information regarding a proposed financing, contrary to Dealer Member Rule 29.1.

PART V – TERMS OF SETTLEMENT

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

MRCC

- a) a fine of \$180,000; and

b) costs of \$20,000.

Patrick McCarthy

a) a fine of \$100,000;

b) a suspension of approval for 1 month beginning October 14, 2019;

c) completion of the Partners, Directors and Seniors Officer Course within 12 months of acceptance of this Settlement Agreement; and

d) costs of \$5,000.

49. 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

50. 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.

51. 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

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

53. 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.

54. 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.

55. 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.

56. 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.

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

58. 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.

59. If this Settlement Agreement is accepted, the Respondents agree that neither they nor anyone on their

behalf will make a public statement inconsistent with this Settlement Agreement.

60. 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

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

DATED this "3rd" day of September, 2019.

"Witness" _____

Witness

"P.G. Walsh" _____

Mackie Research Capital Corporation

PER: "P.G. WALSH, CHAIRMAN & CEO"

"I HAVE AUTHORITY TO BIND THE CORPORATION"

"Witness" _____

Witness

"Patrick McCarthy" _____

Patrick McCarthy

DATED this "5th" day of September, 2019.

"April Engelberg" _____

Witness

"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 3rd day of October, 2019 by the following Hearing Panel:

Per: "Joan Smart" _____

Panel Chair

Per: "Dave Persaud" _____

Panel Member

Per: "Guenther Kleberg" _____

Panel Member

Copyright © 2019 Investment Industry Regulatory Organization of Canada. All Rights Reserved