

Re BBS Securities

IN THE MATTER OF:

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

and

BBS Securities Inc.

2018 IIROC 36

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

Heard: August 7, 2018 in Toronto

Decision: August 7, 2018

Written Reasons for Decision: October 15, 2018

Hearing Panel:

Julia Dublin, Chair, Peter Dymott and Ron Smith

Appearance:

Kathryn Andrews, Enforcement Counsel

Frank Scali, IIROC Investigator

Kevin Richard, Counsel for BBS Securities Inc.

REASONS FOR DECISION ON JOINT SETTLEMENT AGREEMENT

Background

¶ 1 A Settlement Hearing to approve a joint Settlement Agreement entered into between IIROC and the Respondent (copy attached) was held on August 7, 2018. The Hearing Panel received and considered oral submissions from IIROC counsel and the Respondent's counsel, as well as the IIROC Settlement Brief, containing the Settlement Agreement, extracts from IIROC Rules and disciplinary sanctions guidelines and selected IIROC hearing panel decisions.

¶ 2 The contravention agreed to by IIROC staff and the Respondent was:

Between April and July 2014, BBS Securities Inc. directed its Order-Execution Only division to solicit clients and potential clients to recommend share purchases, contrary to Dealer Member Rules 1300.1 and 3200.

¶ 3 Staff and the Respondent agreed to the following terms of settlement:

- (a) a fine in the amount of \$65,000; and
- (b) costs of \$3,000

Facts

¶ 4 The full facts are set out in the Settlement Agreement and additional facts were elicited at the hearing. The facts set out here are a summary of information contained in the Settlement Agreement and provided with

counsel consent at the hearing.

¶ 5 During the relevant period, April to July 2014, BBS Securities Inc. ("BBS") operated Virtual Brokers, an Order-Execution Only division approved by IIROC. Under IIROC Rules 1300.1 and 3200, trades by BBS clients in accounts held through Virtual Brokers were exempt from suitability determinations so long as Virtual Brokers did not recommend the trades.

¶ 6 In May 2014, BBS signed an engagement letter with White Knight Acquisitions III ("WK3") to act as agent in a best efforts prospectus offering by WK3, a Capital Pool Company ("CPC") governed by Policy 2.4 of the TSX Venture Exchange ("TSXV"). This Policy requires that, at the end of its initial public offering ("IPO") a CPC must have 200 shareholders, each beneficially owning at least 100 unrestricted shares excluding shares held by non-arm's length parties.

¶ 7 WK3 sought to raise a minimum of \$500,000 and a maximum of \$1,000,000 at \$0.20 per share. BBS and WK3 also signed an agency agreement on July 11, 2014. BBS has not acted as an agent for a CPC on any other occasion.

¶ 8 In June or early July, 2014, BBS became concerned it would not be able to attract enough arm's length investors in WK3 by the closing date to meet the TSXV's minimum shareholder requirement. To improve the numbers, BBS asked employees in the Virtual Broker division to advise clients and potential clients that if they acquired 1000 shares of WK3 they would receive a firm credit of \$200, in effect offering free shares of WK3. Some clients were advised that they thus risked no loss of any principal. Some employees did not explain that the resale of shares was subject to WK3 engaging in a successful Qualifying Transaction under TSXV rules. There was also a New Issue section on the Virtual Brokers website featuring WK3.

¶ 9 129 clients purchased exactly 1000 WK3 shares and received a \$200 credit or refund at a cost of \$25,000 to BBS.

¶ 10 117 clients purchased more than 1000 WK3 shares each. More than 20 of these were BBS employees, family members or companies related to the principals.

¶ 11 WK3 announced on July 18, 2014 that the IPO was completed with 2,930,500 common shares at \$0.20 per share, for gross proceeds of \$586,100. The Qualifying Transaction took place and WK3 shares were ultimately fully tradable on the TSXV.

¶ 12 As agent, BBS received 10% of the gross proceeds, i.e. \$58,610. BBS apparently did not benefit from any brokers' options.

¶ 13 On November 1, 2017, BBS became a wholly-owned subsidiary of CI Financial Corp. and continues to operate the Virtual Brokers division.

Application of IIROC Guidelines and Past Decisions to Present Circumstances

¶ 14 Counsel agreed that there are no precedent cases that clearly apply to these facts to suggest a reasonable range of sanctions.

¶ 15 The Panel considered the IIROC Sanction Guidelines brought to our attention by IIROC counsel, in particular factors of the number, size and character of the transactions at issue, frequency of acts, any pattern of misconduct, the period of misconduct, level of intention, previous disciplinary history and corrective measures. The Panel took into account how the factors applied to the circumstances of the Respondent.

Number, Size and Character of the Transactions at Issue

¶ 16 IIROC Staff and the Respondent submitted that BBS's promotion was not intended to avoid TSXV rules but to comply with them. For example, companies often give shares to employees as part of a CPC transaction.

¶ 17 The notion of giving away free shares to clients is not in itself contrary to the public interest or IIROC Rules. It can be a form of promotion used by full service dealer firms. However, the IIROC Rules did not

permit BBS to include any element of promoting the acquisition of securities to clients through its discount brokerage division, including supporting its corporate finance function by offering free securities of a specific company either through cold calls or on its website.

Frequency of Acts and Pattern of Misconduct

¶ 18 The WK3 offering was the only time BBS acted as agent on a CPC transaction and the only time it breached the Order-Execution Only Rules.

Previous Disciplinary History and Corrective Measures

¶ 19 BBS has no previous disciplinary history. There was no evidence of client harm. No clients were out of pocket. BBS is now a wholly owned subsidiary under the compliance umbrella of CI Financial Corp.

Agreed Sanctions

¶ 20 The Panel concluded that the agreed fine of \$65,000, being in the range of BBS's agency fee for the WK3 offering, was reasonable. The agreed sum of \$3000 for investigative costs was reasonable given the relative simplicity of the facts and the Respondent's cooperation.

Conclusion

¶ 21 Under Section 8215 of IIROC Rule 8200 "Enforcement Proceedings", at the conclusion of a settlement hearing, the hearing panel may either accept or reject the proposed settlement. This does not permit the hearing panel to vary any of the terms of a settlement agreement, even in favour of a respondent.

¶ 22 The Panel considered the IIROC disciplinary Sanction Guidelines and the oft-cited principle from *Re Milewski*, [1999] I.D.A.C.D. No.17:

"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."

¶ 23 The Panel accepted the joint Settlement Agreement. The Panel concluded that the sanctions provided for in the Agreement were reasonable to achieve the regulatory goals of both specific and general deterrence. The contraventions seem to have stemmed from a failure to fully understand the IIROC Order-Execution Only Rules rather than a deliberate attempt to flout them. The point should now be clear to both the Respondent and the industry at large.

Dated at Toronto, Ontario this 15th day of October, 2018.

Julia Dublin

Peter Dymott

Ron Smith

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 BBS Securities Inc. (the “Respondent” or “BBS”).

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. BBS Securities Inc. (“BBS”) is a Dealer Member which also operates an Order-Execution Only (“OEO”) division called Virtual Brokers. Between April and July 2014 (the “Relevant Period”), and contrary to the regulatory exemptions applicable to OEO firms, BBS directed Virtual Brokers to solicit orders from clients and potential clients to recommend the purchase of Whiteknight Acquisitions III’s (“WK3”) Initial Public Offering (the “IPO”).

OEO division of BBS

5. During the Relevant Period, Virtual Brokers was approved by IIROC as an OEO division of BBS. Virtual Brokers received approval to accept orders from customers without a suitability determination where no recommendation is provided by the firm, under Dealer Member Rules 1300.1 (t), 1300.1 (v), 1300.1 (w) and 3200.

The OEO Regulatory Framework

6. IIROC’s regulatory requirements, which set out the basic framework for OEO firms or divisions, are designed to ensure that an OEO division’s clients make their own investment decisions, without receiving any recommendations or suitability assessment from the OEO division. IIROC rules prohibit OEO divisions from providing any recommendations. As long as the OEO division does not provide recommendations to clients, IIROC rules exempt the OEO firm from suitability determination requirements.

Background

7. In early 2014, BBS was approached by WK3 to act as WK3’s agent in an upcoming IPO. WK3 was a Capital Pool Company (“CPC”). BBS had not previously acted as agent for a CPC nor have they since.
8. Policy 2.4 of the TSX Venture Exchange (the “TSXV”) applies to all CPCs. TSXV Policy 2.4 section 3.2 (1) indicates that upon completion of the IPO, the CPC must have *a minimum of 200 shareholders* with each shareholder beneficially holding *at least 1000 common shares* free of re-sale restrictions and *exclusive of any common shares held by non-arm’s length parties* to the CPC. (emphasis added)

Engagement letter and agency agreement

9. BBS and WK3 signed an engagement letter on May 5, 2014 in which WK3 retained BBS to act as agent in arranging a best efforts prospectus offering of common shares of WK3 at \$0.20 per share with an offering size of \$500,000 minimum and \$1 million maximum. BBS and WK3 also signed an agency agreement dated July 11, 2014.

The Promotion

10. On or about June or early July of 2014, BBS became concerned that it did not have enough arm’s length investors to ensure the success of WK3’s CPC and its proposed TSXV listing. In addition to individuals, companies and BBS employees who had purchased or who intended to purchase varying amounts of WK3 shares, BBS needed more arm’s length investors to ensure a successful closing of this transaction in order

to comply with TSXV Policy 2.4.

11. In June and July 2014, BBS asked certain employees of Virtual Brokers to carry out a promotion in which they would solicit existing and/or potential clients and tell them that if they expressed an interest to purchase 1000 shares of WK3, then they would receive a credit of \$200 which would cover the cost of the purchase. This conduct amounts to a recommendation, contrary to Dealer Member Rules 1300.1 and 3200.
12. The employees also were told to advise clients or potential clients that as the cost of the purchase would be credited to them, there was no risk of losing their money on this investment as they would not end up paying anything for the investment.
13. Certain Virtual Brokers employees did not explain at the time that the WK3 shares had to be held for a certain period of time or that the shares may never be able to be sold, depending on whether or not the subsequent qualifying transaction was successful.

Number of investors

14. There were a total of 246 investors for WK3 shares, including:
 - a. 129 participants who “purchased” exactly 1000 WK3 shares at a cost of \$200 each as part of the Promotion, based on the recommendation by the OEO division of BBS. The cost of these shares was refunded by BBS to almost all of these participants. At least two of these participants were BBS employees; and,
 - b. 117 individuals and corporations who purchased more than 1000 WK3 shares each. More than 20 of these investors were either BBS employees, family members or companies related to the principals.

Completion of WK3’s IPO

15. WK3 announced in a July 18, 2014 press release that the IPO was completed with 2,930,500 common shares at a price of \$0.20 per share, for gross proceeds of \$586,100. WK3 shares were admitted for trading on the Exchange on July 21, 2014, as a Tier 2 company. Ultimately the WK3 qualifying transaction took place after July 2014.

Amounts Paid to and by BBS

16. BBS as agent received a cash commission of 10% of the gross proceeds of the offering as well as options to purchase up to 293,500 common shares at \$.20 per share, exercisable within 24 months of listing on the TSXV.
17. Accordingly, BBS received some \$58,610 as 10% of the gross proceeds indicated above.
18. BBS spent \$25,000 pursuant to the Promotion for the 129 participants to purchase WK3 shares.

Other

19. The Respondent does not have a prior disciplinary history.
20. As indicated in an IIROC Notice, as of November 1, 2017, CI Financial Corp. indirectly acquired all of the outstanding securities of BBS. BBS continues to operate as does VB. BBS’ website indicates that it is a wholly owned subsidiary of CI Financial Corp.

PART IV – CONTRAVENTIONS

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

Contravention:

Between April and July 2014, BBS Securities Inc. directed its Order-Execution Only division to solicit

clients and potential clients to recommend share purchases, contrary to Dealer Member Rules 1300.1 and 3200.

PART V – TERMS OF SETTLEMENT

22. The Respondent agrees to the following sanctions and costs:
 - a) A fine in the amount of \$65,000; and,
 - b) Costs of \$3,000.
23. 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

24. 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 contravention in Part IV of this Settlement Agreement, subject to the provisions of the following paragraph.
25. 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

26. This Settlement Agreement is conditional on acceptance by the Hearing Panel.
27. 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.
28. 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.
29. 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.
30. 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.
31. The terms of this Settlement Agreement are confidential unless and until this Settlement Agreement has been accepted by the Hearing Panel.
32. 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.
33. 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.
34. 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

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

DATED this “25th” day of June, 2018.

“Deborah Carlyle”

Witness

“BBS Securities Inc.”

Respondent BBS Securities Inc.

“Ricki Newmarch”

Witness

“Kathryn Andrews”

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

The Settlement Agreement is hereby accepted this “7th” day of “August”, 2018 by the following Hearing Panel:

Per: “Julia Dublin”

Panel Chair

Per: “Ron Smith”

Panel Member

Per: “Peter Dymott”

Panel Member

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