

# Re Gottfred

IN THE MATTER OF:

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

**and**

**Kenneth John Gottfred (Respondent)**

2016 IIROC 22

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

Heard: April 20, 2016

Decision: June 2, 2016

**Hearing Panel:**

Joseph A. Bernardo, Chair, John Van Koll, and Mark Redcliffe

**Appearances:**

Paul Smith, Enforcement Counsel

The Respondent was neither present nor represented by counsel.

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## DECISION ON THE MERITS AND PENALTY

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### Overview

¶ 1 On March 14, 2016, the Investment Industry Regulatory Organization of Canada (IIROC) issued a Notice of Hearing that set April 20, 2016 as the date for the hearing in Vancouver. The Notice of Hearing contained allegations against Kenneth John Gottfred that:

1. From January 2011 to April 2014, he executed discretionary transactions in client accounts contrary to IIROC Dealer Member Rule 1300.4.
2. From August 2011 to April 2014, he acted contrary to IIROC Dealer Member Rule 1300.1(q) by recommending that clients use margin when it was not suitable for them.
3. Since April 2015, he had failed to cooperate with an IIROC investigation into his conduct contrary to IIROC Dealer Member Rule 19.5.

¶ 2 At the commencement of these proceedings, Enforcement Counsel informed the Hearing Panel that the Respondent had declined to serve a Response as required by Rule 7.1 of the Rules of Practice and Procedure and, furthermore, had advised the Staff he had no intention of attending the hearing. The Panel consented to IIROC's request that the hearing proceed in the Respondent's absence under Rules 7.2 and 13.5.

¶ 3 After considering the record and Counsel's submissions, the Panel found that the Respondent had violated IIROC's Dealer Member Rules as alleged in the Notice of Hearing. The Panel then directed IIROC to make submissions on penalty and, upon receiving them, reserved its decision on sanctions.

¶ 4 These are the reasons for our findings and sanction decision.

## Hearing in Respondent's Absence

¶ 5 Rules 7.2 and 13.5 confer on Hearing Panels discretion to make findings of fact and determine sanctions in the absence of a respondent, and to do so without the necessity of receiving and weighing evidence. Given the nature of this discretion, the provisions deserve to be reviewed in full.

Rule 7.2 states that:

*If a Respondent served with a Notice of Hearing fails to serve a Response in accordance with Rule 7.1:*

- (a) *the Organization may proceed with the hearing of the matter as set out in the Notice of Hearing without further notice to and in the absence of the Respondent; and*
- (b) *the Hearing Panel may, accept as proven the facts and violations alleged by the Organization in the Notice of Hearing, and may impose penalties and costs pursuant to Dealer Member Rules 20.33, 20.34 and 20.49.*

Rule 13.5 states that:

*Where a Respondent, having been served with a Notice of Hearing, fails to attend a disciplinary hearing, the Hearing Panel may proceed in the absence of the Respondent and may accept as proven the facts and violations alleged by the Organization in the Notice of Hearing.*

*Upon making a finding of the violations as alleged in the Notice of Hearing, the Hearing Panel may immediately hear submissions of the Organization regarding an appropriate penalty and may impose such penalty, as it deems appropriate, pursuant to Dealer Member Rule 20.33 and 20.34.*

¶ 6 The purpose of these Rules is unambiguous: it is to assist Hearing Panels when they are confronted with respondents who, by their own conduct, unmistakably disclose to IIROC that they do not intend to engage its discipline process. The remedy contemplated by Rules 7.2 and 13.5 is to dispense with hearing practices that in the normal course would otherwise be understood as fundamental to procedural fairness.

¶ 7 As another Hearing Panel observed recently, procedural rights in IIROC hearings must be understood as operating in a context in which the public interest requires the timely and efficient resolution of outstanding allegations of misconduct: *Dirani (Re)*, 2016 IIROC 13, at paras. 4 and 5. When a respondent declines to answer allegations made against it, it is therefore both rational and proportionate to confer on the decision-maker discretion to forgo the testing of evidence and consider the allegations in the respondent's absence.

¶ 8 All regulatory discretion must be exercised reasonably. It follows that a decision to depart significantly from usual practices should attract particular care. The following principles should apply:

1. Before exercising its discretion under Rules 7.2 or 13.5, a Hearing Panel must be satisfied that the respondent had proper notice of the allegations and of the potential adverse consequences of failing to engage the disciplinary process.
2. What may be called the deeming aspect of Rules 7.2 and 13.5 is limited. A Hearing Panel may deem as proven only those facts and violations alleged in the Notice of Hearing, which is to say only those of which the respondent had prior notice and declined to address. If IIROC elects to supplement its case by tendering evidence, it must be assessed for relevance, credibility and reliability in the usual fashion. Moreover, the Panel must consider whether the evidence changes the character of the case alleged against the respondent in the Notice of Hearing and, if so, whether it would be unfair to accept the evidence into the record without prior notice to the respondent.
3. Finally, while Rules 7.2 and 13.5 may expedite the finding of fact, the onus still remains on IIROC to establish its case on the civil standard of a balance of probabilities: *Armstrong (Re)*, 2015 IIROC 34, at para. 5. In order for a Panel to accept an alleged violation in a Notice of

Hearing as proven, it must be satisfied that the underlying allegations of fact are sufficient to *prima facie* establish the legal elements of the misconduct.

### **Notice to the respondent**

¶ 9 At the hearing, Counsel tendered the Affidavit of Senior Investigator Michael Smith sworn on April 20, 2016 (Affidavit), which the Panel accepted and received into the record.

¶ 10 The Affidavit attests that:

1. On March 17, 2016, Mr. Smith sent the Respondent an email, attached to which was a copy of the Notice of Hearing. In the email, Mr. Smith provided the time, date, and place of the hearing, was explicit in describing it as a “disciplinary hearing”, and asked the Respondent to acknowledge receipt and confirm whether he planned to attend.
2. The Respondent answered Mr. Smith within minutes by way of an e-mail reply. He thanked Mr. Smith for the Notice and stated “I will not be attending this meeting.”
3. On March 21, 2016, the Notice of Hearing was served on the Respondent by registered mail delivery to his last known address as recorded in IIROC’s registration records.

¶ 11 The Affidavit was sworn in proper form, and nothing in its contents or in the record generally raises any question whatsoever about the accuracy or reliability of the matters attested to within the Affidavit.

¶ 12 On the evidence provided by the Affidavit, it is plain that the Notice of Hearing was served on the Respondent in accordance with Rule 5.2(b) of IIROC’s Rules of Practice and Procedure.

¶ 13 The Affidavit also establishes that the Respondent by virtue of his March 17, 2016 email exchange with Mr. Smith had both personal possession of a copy of the Notice of Hearing and personal knowledge of the hearing particulars.

¶ 14 The Notice of Hearing informed the Respondent of IIROC’s case against him. It also explicitly notified the Respondent that failing to serve a Response or attend the hearing could result in the allegations against him being accepted as proven and penalties and costs being ordered against him, all in his absence. In our view, there can be no doubt that the Respondent had full notice of the potential adverse consequences of his failing to engage IIROC’s disciplinary process.

¶ 15 The Affidavit also supplemented IIROC’s case by providing certain evidence relevant to how IIROC conducted its investigation. This evidence does not change the character of IIROC’s case against the Respondent as set out in the Notice of Hearing. Accordingly, we accepted the supplemental evidence into the record without notice to the Respondent.

### **Findings**

¶ 16 Unless otherwise indicated, the following findings are derived from the allegations of fact contained in the Notice of Hearing. Any findings derived from the Affidavit are identified as such.

#### *Background*

¶ 17 The Respondent became a registered representative in 1991 and was employed by a Dealer Member firm in Manitoba from 1992 to 1995.

¶ 18 He subsequently moved to Kelowna, British Columbia, where he was employed from 1995 to 2002 as a mutual fund representative by a bank.

¶ 19 In 2002, the Respondent began employment with Raymond James in Kelowna as a registered representative, a position he held continuously until he resigned in February 2015. He has not been registered with a Dealer Member firm since that time.

¶ 20 Two customers of the Kelowna bank that employed the Respondent held an investment portfolio at the

bank with a total value of approximately \$615,000, comprised primarily of income oriented mutual funds (the “Clients”). In 2002, after the Respondent moved to Raymond James, the Clients opened accounts at that firm for which he was the registered representative. At 58 and 57 years old, respectively, they were both retired and conservative investors with no prior experience investing through a Dealer Member firm. The Clients transferred their entire portfolio to Raymond James within a year of opening their accounts.

¶ 21 Included as exhibits to the Affidavit are extracts from an interview of the Clients conducted by Mr. Smith. These establish that:

1. The Clients were a married couple.
2. The Respondent had been their investment advisor at the bank, where their investments were primarily in Guaranteed Investment Certificates and mutual funds.
3. The Clients had never invested in individual stocks prior to opening accounts at Raymond James.

#### *Unauthorized discretionary trading*

¶ 22 The Respondent suggested to the Clients that they should allow him to execute transactions without first contacting them. The Clients agreed to this arrangement. They subsequently did not speak to the Respondent “each time” a security was bought or sold.

¶ 23 In the extracts of Mr. Smith’s interview of the Clients attached to the Affidavit, the Clients indicate that subsequent to accepting his suggestion that he exercise his own discretion in executing trades on their behalf, the Respondent occasionally still consulted with them prior to executing a trade. From this, we interpret the use of the phrase “each time” in the Notice of Hearing to mean the Respondent did not consult the Clients “every time” he executed a trade on their behalf.

¶ 24 The Notice of Hearing does not specify the date when the Respondent suggested to the Clients that he should execute transactions on their behalf without consulting them, stating only that it was “[w]ithin a few years of opening the accounts”. The extracts of Mr. Smith’s interview of the Clients attached to the Affidavit indicate that to the best of their recollection the Respondent made the suggestion in 2004 or 2005. Although the Respondent commenced executing discretionary transactions in the early years of the accounts, the relevant count in the Notice of Hearing limits the violation period to the last three years of the accounts, stating that the misconduct took place between January 2011 and April 2014.

¶ 25 The particulars in the Notice of Hearing do not specify how many transactions the Respondent executed on his own initiative. They state only that between 2011 and 2014 approximately 274 transactions were carried out in the Clients’ accounts, and that the Respondent did not obtain specific instructions regarding “many” of them.

¶ 26 Rule 1300.4 prohibits a registered representative from exercising discretionary authority over a customer account unless:

- (a) the Dealer Member has designated a Supervisor or Supervisors to be responsible for discretionary accounts;
- (b) the customer has given prior written authorization in compliance with Rule 1300.5;
- (c) a Supervisor designated under subsection (a) has approved the account as a discretionary account and recorded that approval;
- (d) the registered representative authorized to effect discretionary trades for the account has actively dealt in, advised on or performed analysis for a period of two years with respect to all types of products which are to be traded on a discretionary basis; and
- (e) the account is maintained at the Dealer Member of the registered representative.

¶ 27 The Client accounts were maintained at the Respondent's Dealer Member employer and we are prepared to take notice that Raymond James in the normal course designates personnel to supervise and be responsible for discretionary accounts. There is no indication in the record, however, that the Respondent had obtained any kind of written authorization from the Clients to engage in discretionary trading or that Raymond James had approved their accounts for such trading or that the Respondent had an in depth understanding of the products he traded at his own discretion.

¶ 28 The allegations of fact in the Notice of Hearing regarding the circumstances of the unauthorized discretionary trading are minimal, but they are sufficient to make out the elements of the violation. We accept them as proven and find that between January 2011 and April 2014 the Respondent violated Dealer Member Rule 1300.4.

#### *Unsuitable margin trading*

¶ 29 The Clients made regular monthly withdrawals from their accounts, which over time reduced the overall value of their joint portfolio.

¶ 30 By May 2009, the total value of the portfolio had been reduced to approximately \$350,000, of which \$300,000 was held in joint cash accounts. At this time, the Respondent recommended to the Clients that they convert these accounts to a joint margin account, advising them that it would enable them to take better advantage of buying opportunities. The Clients followed the Respondent's recommendation and opened a margin account.

¶ 31 The Notice of Hearing states that the new client application form for the account recorded the risk tolerance of the Clients as "100% High" and their investment knowledge as "Good", while their net liquid assets were recorded as \$500,000. The Notice of Hearing does not explain the \$150,000 discrepancy between the \$350,000 in capital it alleges the Clients had available for investment and the \$500,000 amount represented in the new client application form.

¶ 32 The Notice of Hearing states that the Respondent did not discuss the risks of margin trading to the Clients or that they would be required to pay interest on outstanding cash balances owed in respect monies borrowed against the equity held in the account. The extracts of Mr. Smith's interview of the Clients attached to the Affidavit are not so definitive.

¶ 33 They indicate that the Clients did not have a strong understanding of how a margin account functions. Nonetheless, the Clients acknowledged having had at least one conversation with the Respondent in which the fact that margin trading involved borrowing money was discussed. The Clients disclosed that they were surprised not by the margin account sustaining interest charges, but rather by their total amount.

¶ 34 The Clients held the margin account from May 2009 to April 2014. During this period, the account was charged approximately \$19,900 in interest and \$49,300 in commission expenses and, overall, sustained a net loss of approximately \$36,000.

¶ 35 Dealer Member Rule 1300.1(q) imposes a duty of diligence on registered representatives to ensure when recommending a securities transaction to a client that the recommendation is suitable for the client

*...based on factors including the client's current financial situation, investment knowledge, investment objectives and time horizon, risk tolerance and the account or accounts' current investment portfolio composition and risk level.*

The Notice of Hearing does not directly address these factors.

¶ 36 It is clear enough that the investment knowledge of the Clients was limited when they first opened their accounts at Raymond James. The margin account, however, was opened after some seven years, during which they had been active market participants. It cannot be inferred from that fact alone that the Clients had become better informed investors over time, but the Notice of Hearing creates some uncertainty about the point by citing

without comment the new client application form's representation of their investment knowledge as "Good".

¶ 37 Similarly, the Notice of Hearing does not provide facts that allow for an objective determination of the suitability of margin trading for the Clients in light of their risk tolerance. Instead, it cites without comment or contradiction the new client application form's representation of their risk tolerance as "100% High". The Clients disavowed that in their interview, but it remains unclear what their actual risk tolerance was at the time.

¶ 38 As for the nature of the account's portfolio and its risk level, the Notice of Hearing provides no guidance. A margin account is not synonymous with 100% risk of loss. The level of risk involved in margin trading is, among other things, a function of the proportion and cost of debt the investor incurs relative to the value and volatility of the equity in the account. In the event, the Clients' margin account lost money, but there is no indication that it ever became necessary at any point to liquidate equity to cover the account's debt positions. The cost of leveraging appears to have been limited to interest charges, which, while considerable at \$19,900, were substantially less than the \$49,300 paid in commissions. The interest charges are, in any event, identified for the account's entire operating period, which began in May 2009, whereas the Notice of Hearing limits the violation period from August 2011 to April 2014. In short, it is not possible to determine from the record either the level of actual investment risk to which the Clients were exposed by the margin trading or what actual interest charges they incurred from it.

¶ 39 The only basis for assessing the suitability of margin trading for the Clients is their financial situation and time horizon, insofar as they can be inferred from certain of the allegations of fact.

¶ 40 The Clients opened their accounts at Raymond James in 2002. Within a year, they had transferred into those accounts the entirety of their investment portfolio of approximately \$615,000. They then proceeded to make regular monthly withdrawals from the accounts. By May 2009, the total amount of withdrawals (together with any trading losses and commission expenses to that date) had been sufficient to reduce the value of their portfolio by \$265,000 to approximately \$350,000.

¶ 41 The record does not disclose the purpose of the withdrawals. It is evident, however, the Clients were in a financial situation that imposed steady pressure on their investment principal. Moreover, at the time the margin account was opened the Clients, both retirees, were each 64 years old.

¶ 42 There is no analysis under which margin trading is suitable for investors in a situation that requires them to continually draw on capital and whose age constrains their investment time horizon. When net liquid assets are in steadily declining balance and the recovery time for any losses is by definition limited, then an investor's central investment objective must be capital preservation and no amount of leverage risk is appropriate.

¶ 43 The Notice of Hearing contains few allegations of fact that address the suitability of margin trading for the Clients and they are far from clearly articulated. Certain basic facts regarding the Clients' financial situation and time horizon, however, are clear and we accept them as proven. On that basis, we find that the Respondent from August 2011 to April 2014 the Respondent acted contrary to Dealer Member Rule 1300.1(q).

#### *Failure to cooperate*

¶ 44 The allegations of fact in the Notice of Hearing that particularize the Respondent's refusal to cooperate with IIROC's investigation are unambiguous. The Affidavit gives additional relevant details about IIROC's overtures to the Respondent.

¶ 45 In October 2014, IIROC gave the Respondent written notice that it had commenced an investigation into his conduct relating to allegations of unsuitable investment and discretionary trading. Mr. Smith attests that this was by way of a letter he sent to the Respondent by registered mail.

¶ 46 On March 25, 2015, IIROC spoke with the Respondent by telephone to advise that he would be required to attend an investigative interview at its Vancouver office, to which the Respondent replied that he would not go to the interview. Mr. Smith attests that in this conversation he advised the Respondent that he could arrange to have the interview conducted in Kelowna. The Respondent stated it was also unlikely that he would attend

any interview in Kelowna. Mr. Smith told the Respondent that he would contact him at a later date.

¶ 47 On April 1, 2015, IIROC delivered a letter to the Respondent a letter advising him that arrangements had been made to interview him in Kelowna and offered a choice of dates for him to attend. Mr. Smith attests that prior to sending this letter he had reserved three alternate dates with a reporting service in Kelowna, that he sent the letter to the Respondent as an email attachment, that the letter advised that the Respondent was required to attend the interview under Rule 19.5, and that the letter informed the Respondent the interview could take place on his choice of the three different dates.

¶ 48 On April 2, 2015, the Respondent replied to Mr. Smith's email and stated he would "not be participating in this interview."

¶ 49 Mr. Smith attests that the email he sent to the Respondent on April 1, 2015 was encrypted and required the recipient to enter a password in order to see its content. It is evident from the Respondent's April 2, 2015 response that he had de-encrypted the email and was aware of the contents of the attached letter.

¶ 50 Mr. Smith attests that on April 6, 2015 he sent the Respondent another letter as an attachment to an encrypted email. Within an hour the Respondent sent a reply stating that he did not have time to look at encrypted messages and re-iterated that he was not prepared to be interviewed. Mr. Smith responded by sending the Respondent another email, this time unencrypted, that stated directly in its body that:

- If the Respondent refused to attend the interview he could be subject to a disciplinary proceeding for failure to cooperate with an IIROC investigation.
- Such a ban typically results in a permanent ban from registration with IIROC.
- He should reconsider his position.
- He had a choice of three dates to be interviewed in Kelowna.

¶ 51 The Respondent emailed a reply to Mr. Smith within the hour in which he stated that he would "not be re-entering the business ever" and that he "really (didn't) care" what actions IIROC Staff would take as a consequence.

¶ 52 Neither the Notice of Hearing nor the Affidavit discuss how the Respondent's failure to co-operate affected the investigation.

¶ 53 Registered representatives are subject to Rule 19.5, which requires all Approved Persons to attend and give information when IIROC requires them to do so. Although the Respondent has left the securities industry, Rule 20.7(1) provides that IIROC's jurisdiction over him continues for a period of five years from the date he ceased to be an Approved Person.

¶ 54 The allegations of fact in the Notice of Hearing that relate to the Respondent's failure to cooperate with IIROC's investigation speak for themselves. We accept them as proven and find that the Respondent violated Dealer Member Rule 19.5.

### **Sanction considerations**

¶ 55 Enforcement Counsel tendered a number of relatively recent sanction decisions as examples of how other Hearing Panels have determined penalties in instances of discretionary trading, unsuitable recommendation of margin trading, and failure to cooperate.

¶ 56 Counsel submitted that a respondent's failure to cooperate with an investigation by its nature is a grave form of misconduct that, absent mitigating circumstances, warrants a permanent bar from approval.

¶ 57 With respect to monetary penalties, Counsel submitted that for the violations of failing to cooperate and unauthorized discretionary trading fines of \$25,000 and \$20,000, respectively, were at the low end and it would

not be unreasonable to order the same amounts in the circumstances of the present case. With respect to recommending margin trading when it was not suitable for the Clients, Counsel pointed out that even isolated incidents tend to attract significant monetary penalties, whereas in the present case the misconduct took place over an extended period. In those circumstances, Counsel submitted a penalty of \$35,000 could be considered lenient.

¶ 58 Counsel submitted a claim for costs on behalf of IIROC in the amount of \$5000, and tendered a Bill of Costs in support.

¶ 59 The Sanction Guidelines identify the purposes and animating principles of IIROC's disciplinary process, as well as key factors to be considered in the determination of sanctions. While Hearing Panels as administrative tribunals are not bound to follow the Guidelines, they are distilled from the guidance provided by past decisions and administrative law generally. The Guidelines, being both relevant and acute, deserve close attention and consideration when determining sanctions.

¶ 60 IIROC's disciplinary process is directed at ensuring that the securities industry meets high standards of conduct and preserving market integrity. The fairness and efficiency of capital markets relies to great extent on a robust framework of proficiency, business and financial conduct rules. Enforcement of those rules, by confirming to member firms and their registered employees that they are of cardinal importance, both strengthens the industry and protects the investing public.

¶ 61 The Guidelines emphasize the forward looking purpose of the discipline process. The first sanctioning principle, in particular, is clear in stating that disciplinary sanctions are preventative in nature, serving to protect the investing public by creating incentives that reinforce the business standards and practices mandated by the Dealer Member Rules. Achieving this requires sanction outcomes that deliver both specific and general deterrence, such that both the respondent and other persons similarly situated in the industry are discouraged from engaging in future misconduct.

¶ 62 The Guidelines, following general administrative law, point out that the appropriateness of a sanction necessarily depends on the facts of a case, with the specific circumstances or details surrounding an episode of misconduct being of particular importance. The sanction decisions submitted by Counsel reflect this emphasis.

¶ 63 In *Beck (Re)* 2012 IIROC 41, the respondent failed to either serve a Response or attend the hearing. Accordingly, the Hearing Panel decided the matter on the strength of the facts set out in the Notice of Hearing. These identified 35 specific transactions the respondent had executed at his own discretion without proper authority during the client's absence, the circumstances surrounding her absence, and the net commission earnings derived from the misconduct. Considering these facts, the Panel ordered sanctions that included a fine of \$20,000 and disgorgement of commission profits.

¶ 64 In *Armstrong, supra*, the respondent after some initial responsiveness failed to cooperate with IIROC's investigation into his unauthorized discretionary trading, left the industry, and declined to attend the hearing into his misconduct. The case was decided on the facts in the Notice of Hearing, which were clear in identifying at least 18 unauthorized transactions and the commissions the respondent had earned from them. The sanctions sought by IIROC Staff, and ordered by the Hearing Panel, included a global fine of \$50,000 in respect of both the failure to cooperate and the underlying misconduct of unauthorized discretionary trading, and disgorgement of commission profits.

¶ 65 *Brodie (Re)* 2013 IIROC 39 and *Jones (Re)* 2014 IIROC 15 were both defended hearings where the misconduct included both unauthorized discretionary trading and unsuitable recommendations, with the latter in *Jones* involving margin trading. The decisions are of limited assistance, as their underlying facts were of a substantially different character from those at the matter at hand. Nonetheless, they are additional examples of sanction decisions that were responsive to the specific factual circumstances of the misconduct at issue.

¶ 66 We are limited in our ability to do this in the present case with respect to the unauthorized discretionary trading and unsuitable margin trading violations.

¶ 67 For example, the Guidelines identify as fundamental the sanction principle that respondents should not financially benefit as a result of their misconduct. IIROC did not ask that the Respondent be ordered to disgorge commission profits. Based on the information in the record, it would not have been feasible.

¶ 68 After May 2009, the margin account housed the bulk of the Clients' investment capital. It follows that the financial benefits the Respondent subsequently derived from unauthorized discretionary trading would have been substantially the same as those he obtained from the unsuitable recommendation of margin. The Notice of Hearing indicates that between May 2009 to April 2014 the Respondent earned \$49,300 in commissions from margin account transactions. However, it identifies the violation periods for the unauthorized discretionary trading and the unsuitable margin recommendation as being from January 2011 to April 2014 and August 2011 to April 2014, respectively. It is therefore clear that the Respondent derived benefit from his misconduct during the violation periods, but the information in the record is not sufficient to permit a determination of the amount.

¶ 69 Ensuring that wrongdoers are relieved of any financial benefits they have obtained from their misconduct is an essential aspect of both specific and general deterrence. Ascertaining the amount of improperly obtained benefits is also relevant to assessing the extent of harm caused to clients or other market participants, which the Guidelines identify as a key factor in the determination of sanctions. Another key factor is the number, size and character of the transactions involved in the misconduct. The total number of transactions in the margin account between 2011 and 2014 points to the frequency of unauthorized discretionary trade executions as relevant to sanctioning in this case, but we are limited in following the Notice of Hearing to finding that "many" transactions were improper, which in its indeterminacy is about the same as saying "some". Similarly, the extracts of Mr. Smith's interview of the Clients suggest a level of vulnerability, yet another key factor, but the record does not permit the drawing of firm conclusions.

¶ 70 It should not be construed from these observations that we are questioning or second-guessing how Staff investigated this case or exercised its prosecutorial discretion in setting out allegations of fact in the Notice of Hearing. Undertaking disciplinary actions is by its nature, as is all enforcement work, subject to competing priorities, limited resources and any manner of practical impediments; and we are mindful that this is a case in which the individual with the most relevant information refused to cooperate with the investigation. We refer to the scarcity of facts only because the intelligibility of our sanction determination requires it.

¶ 71 In determining sanctions, the extent to which we can address the unauthorized discretionary trading and unsuitable recommendation violations is limited because what can be said about them with any certainty is limited:

- With the knowledge but not informed consent of the Clients, the Respondent engaged in unauthorized discretionary trading for a period of a little over three years. We infer that the trading imposed economic harm on the Clients in the form of commission expenses, but are unable to quantify it. We infer from the fact that trading took place over an extended period that the Respondent's misconduct was deliberate and relied on a continuing lack of transparency with his employer.
- The Respondent recommended margin trading to the Clients when by any analysis it was unsuitable for them and implemented it for a period of over two and a half years. The Clients sustained harm in the form of interest charges, but it is not quantifiable on the information in the record.

¶ 72 The information relating to the Respondent's failure to cooperate with IIROC's investigation is another matter. It is abundantly clear that he wilfully refused to cooperate with IIROC's investigation, despite Mr. Smith's diligent efforts to persuade him otherwise and to caution him of the negative consequences of refusing to make himself available for questioning. The Respondent's response was an attitude of breezy indifference that bordered on the contemptuous.

¶ 73 One of the cases provided by Counsel, *Trites (Re)* 2010 IROC 48, is highly instructive in its analysis of the significance of an approved person's failure to cooperate with an IROC investigation.

¶ 74 In *Trites*, the respondent came under investigation for engaging in unauthorized discretionary trading, recommending unsuitable investments, and misrepresenting the risks of certain investments in respect of four different clients. He failed to cooperate with the investigation and resigned from the industry. IROC issued a Notice of Hearing that was limited to alleging a breach of Rule 19.5, whereupon the respondent's failure to attend the hearing the Hearing Panel, relying on affidavit evidence, found him to have violated. In its reasons, the Panel noted that the respondent had intentionally failed to attend an interview without offering any excuse or explanation and after IROC had made reasonable attempts to accommodate him. The Panel observed:

It is of vital importance to the system for regulating approved persons that approved persons cooperate with reasonable demands made on them during investigation of their conduct. This obligation does not end when an approved person ceases to be registered. (at para. 12)

¶ 75 The Panel did not consider the seriousness of the underlying allegations to be a relevant factor in sanctioning. On the contrary, in that regard the more relevant consideration was the inherent seriousness of failing to cooperate:

We do not consider that it is generally worse to fail to attend an interview in an investigation involving serious allegations than in an investigation involving less serious allegations. The gravamen of the misconduct is not respecting that, as a participant or former participant in a regulated industry, one must comply with the obligation to cooperate with the regulator's investigation, regardless of how one regards the allegations. (at para. 16)

¶ 76 Placing paramount value on the need to preserve the integrity of IROC's disciplinary process, the Panel in *Trites* ordered the respondent permanently barred from approval in any capacity and to pay a fine of \$25,000.

¶ 77 In *Armstrong, supra*, where as previously mentioned a global fine of \$50,000 was ordered in respect of both a failure to cooperate and an underlying unauthorized discretionary trading violation, the respondent was also permanently barred from approval.

## **Decision**

¶ 78 The Respondent does not have any prior disciplinary history. We observe, however, that common to each of the Respondent's violations is the deliberate nature of the misconduct.

¶ 79 Whatever the full scope and effect of the unauthorized discretionary trading and unsuitable margin recommendation on the Clients, the violations were committed over an extended period, which necessarily speaks to purposefulness. The violation of Rules 1300.4 and 1300.1(q) was not incidental to how the Respondent conceived and undertook his role as the Clients' registered representative, but integral to it. This signifies a fundamental failure in the Respondent's understanding of the purpose and value of standards of conduct. The same can be said of the Respondent's cavalier attitude towards IROC's investigation.

¶ 80 The intentional character of the Respondent's misconduct and his refusal to be held accountable for it in any way point to a need for sanctions that have the strongest element of specific deterrence. The sanctions must also communicate to the industry and the investing public that deep failures to meet standards of conduct will be met with commensurately firm disciplinary measures.

¶ 81 IROC says that the Respondent should be permanently barred from approval. We agree.

¶ 82 With respect to determining a monetary penalty, we are of the view that given the nature of the record in this case it is more appropriate to assess a global amount instead of cumulating separate amounts in respect of each violation. Taking into account the overall circumstances of the case, we consider a fine of \$50,000 would be appropriate.

¶ 83 IROC's claim of \$5000 for costs is reasonable, when it is assessed against the total of 90 hours

recorded in the Bill of Costs for investigation and prosecution.

¶ 84 Further to Dealer Member Rules 20.33(2) and 20.49, we order that the Respondent:

1. is permanently barred from approval with IIROC in any capacity;
2. pay a fine of \$50,000; and
3. pay costs in the amount \$5000.

Dated at Vancouver, British Columbia, this 2<sup>nd</sup> day June, 2016.

Joseph A. Bernardo, Chair

John Van Koll

Mark Redcliffe

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