# Re Rail

**IN THE MATTER OF:**

**THE BY-LAWS OF THE INVESTMENT DEALERS ASSOCIATION OF CANADA**

**AND**

**STÉPHANE RAIL**

2009 IIROC 2

Investment Industry Regulatory Organization of Canada
Appeal Panel

Heard: November 26, 2008.
Panel Decision: January 7, 2009
(49 paras.)

**Appeal Panel:**
Pierre A. Michaud, O.C., Q.C., Chair
Daniel Leclair
Roger Casgrain, CFA

**Appearances:**
Ms. Diane Bouchard, Counsel for the Respondent (IIROC)
Mr. Sébastien Caron (Heenan Blaikie), for the Appellant (Rail)

## DECISION

***UNOFFICIAL ENGLISH TRANSLATION***

1. Citing as his authority Association By-law 20.50 and following, Stéphane Rail (« Rail ») is appealing the guilty verdict rendered by the Hearing Panel on June 25, 2008 on counts 1a), 2 and 3.

2. The Respondent alleged that Rail committed eight violations of the rules of the Investment Industry Regulatory Organization of Canada ("IIROC"). Rail entered a guilty plea on three of the counts, namely counts 4, 5 and 6 of the Notice of Hearing.

3. In its decision of June 25, 2008, the Hearing Panel dismissed two of the counts contained in the Notice of Hearing, namely counts 1b) and 7, found Rail culpable of Counts 1 a), 2 and 3, the decision being a majority decision regarding counts 1a) and 2, with Danielle Le May dissenting on both counts. The decision regarding count 3 was unanimous.

4. The counts which are the subject of this appeal are as follows :

> "1. During the year 2000, while employed as a Registered Representative of TD Securities Inc. (hereinafter, TD), the Respondent engaged in conduct unbecoming or detrimental to the public interest, when he engaged in outside business activities without the consent and without the knowledge of his firm, as follows:

a) by introducing one of his clients, HC, to another of his clients, LV, with the aim of facilitating the obtaining of a loan for LV, knowing that his firm had already determined that this loan was too risky and that such behaviour was not consistent with his responsibilities as a registered representative;

2. In the year 2000, the Respondent, while employed with TD as a registered representative, made inappropriate use of personal and confidential information regarding two clients, HC and LV, by introducing them to one another in order to facilitate a financing project to benefit LV, thereby engaging in conduct unbecoming and detrimental to the public interest, contrary to Association By-law 29.1;

3. On or about September 18, 2000, while employed with TD as a registered representative, the Respondent failed to use due diligence to make sure that the cheque made by P. Inc.,

dated September 14, 2000, in the amount of $333,000 and payable to COC, was properly invested in the account belonging to COC, thereby engaging in conduct unbecoming and detrimental to the public interest, contrary to Association By-law 29.1;"

5. In his appeal factum, Rail defines the issues in dispute, as follows:

[TRANSLATION]

"Regarding count 1 a), the Appeal Panel will have to determine:

i) whether the Hearing Panel erred in concluding that the transaction in question was made without the knowledge and without the consent of TD and in adding new notions to the wording of the count;

ii) if the Hearing Panel erred in the interpretation of what constitutes an "outside business activity";

iii) if the Hearing Panel erred in concluding that the loan was made to benefit LV;

"Regarding count 2, the Appeal Panel will have to determine:

i) if the Hearing Panel erred in adding new notions to the wording of the count;

ii) if the Hearing Panel erred in concluding that Rail committed a violation other than that mentioned in the count;

"Regarding count 3, the Appeal Panel will have to determine:

i) if the Hearing Panel erred in concluding that the cheque was not deposited according to the clients' wishes, in the absence of any evidence to that effect;

ii) if the Hearing Panel erred in accepting illegal evidence that disregards the administration of justice;"

**JURISDICTION OF THE APPEAL PANEL**

6. At the outset, Rail's counsel invoked the Appeal Panel's lack of jurisdiction, in view of the publication by the Respondent, on November 24, 2008, of a rule that put an end to the appeal process provided under By-law 20.50 and following.

7. In our opinion, the Appeal Panel has full jurisdiction to rule on Rail's appeal, as the measures published on November 24, 2008 only take effect as of that date. The amendment to the rule contains no retroactive measure, and publication of the rule therefore does not affect Rail's acquired rights to appeal the Hearing Panel's decision. The appeal was lodged on July 24, 2008.

8. The legal counsel of both parties acknowledge that the Respondent could not, through publication of this amendment to the rule, infringe Rail's acquired rights to appeal the decision and, consequently, the Appeal Panel declares itself competent to rule on the appeal.

**THE STANDARD FOR INTERVENTION**

9. Counsel for the Respondent has argued that as regards the mixed questions of law and fact and determining the appellant's culpability on the counts that are the subject of the appeal, the Appeal Panel must be guided by the standard of reasonableness.

10. She submits that in matters of the presentation of evidence and its appraisal, the Appeal Panel must demonstrate a high degree of deference. In support of this assertion, she states that the Hearing Panel is a jurisdiction specializing in disciplinary matters in the securities industry, that it has the powers necessary to its jurisdiction and is comprised of one member in good standing (active or retired) of the Barreau du Québec, and two peer members (active or retired) of the securities industry.

11. The Appeal Panel is comprised of one active member in good standing of the Barreau du Québec, one independent member of the Board of Directors, and one industry member of the Board of Directors. It is therefore just as specialized as the Hearing Panel.

12. By-law 20.54 defines the powers of the Appeal Panel as follows:

> "20.54 Powers of Appeal Panel
>
> (1) A hearing held under this Part shall be an appeal on the record, however, the Appeal Panel may receive new or additional evidence as it considers just.
>
> (2) The Appeal Panel may:
>
> (a) affirm any decision;
>
> (b) quash any decision;
>
> (c) vary any decision or penalty;
>
> (d) make any decision that could have been made by a Hearing Panel pursuant to By-law 20.33, By-law 20.34, By-law 20.45 and By-law 20.49;
>
> (e) extend or limit the decision's application and effect to any Districts of the Association;
>
> (f) order a new hearing; or
>
> (g) make any order or decision that is considered just."

13. The powers conferred by the above-cited provision are extensive and lead us to conclude that the standard for intervention is that of reasonableness. Given the repeal of the right to appeal decisions rendered since November 24, 2008, we do not think it would be useful to analyze at any great length the authorities cited on this question, the specific powers stipulated in the above-cited provision being quite different from those discussed in the cited decisions.

BACKGROUND

- Rail has been active in the securities industry for over twenty (20) years and has never been the object of any customer complaints or disciplinary sanctions other than those concerned in the present matter.
- At all material times, Rail was in the employ of TD Securities Inc. (TD), then known as TD Evergreen.
- Since May 2001, Rail has been employed with Canaccord Capital Corporation, as a registered representative and manager of the Québec City branch.

- The particulars of the case against Rail are the result of two events which occurred more than eight years ago.

**THE PARTICULARS**

14. COUNT 1A):

Rail is alleged to have committed the following violation:

> "1. During the year 2000, while employed as a Registered Representative of TD Securities Inc. (hereinafter, TD), the Respondent engaged in conduct unbecoming or detrimental to the public interest, when he engaged in outside business activities without the consent and without the knowledge of his firm, as follows:
>
> a) by introducing one of his clients, HC, to another of his clients, LV, with the aim of facilitating the obtaining of a loan for LV, knowing that his firm had already determined that this loan was too risky and that such behaviour was not consistent with his responsibilities as a registered representative;"

15. The material facts may be summarized as follows:

- LV, a client of Rail, contacted the latter in order to discuss obtaining a $3,000,000 loan from TD, to be secured by the securities held in his account with TD;
- TD rejected the loan application because of the excessive concentration of LV's securities.
- Rail contacted another of his clients, HC, who wanted to increase his investment income and that of his holding company. Rail informed him of the possibility of making a short-term loan to another of his clients (LV), which loan would be secured and would bear a high rate of interest.
- Rail actively participated in the preparation of the transaction, which was ultimately substantiated by a document on April 3, 2000, and the funds were paid out in the month of July 2000.

16. The Hearing Panel identified the following matters as requiring resolution:

> [TRANSLATION]
>
> "To decide on Rail's culpability regarding count 1a), it is necessary to determine whether Rail's participation in the financial transaction between HC and LV constitutes an outside business activity within the meaning of the IIROC rules, and whether this activity was carried on without the consent and without the knowledge of TD."

17. The majority decision is to the effect that this activity was carried on without the knowledge and without the consent of TD, because TD never consented in writing, received no fees or commission, and was only informed of the transaction after it was concluded. This activity was considered to be outside the normal purview of a registered representative within the meaning of the IIROC rules. The majority decision concludes that Rail's behaviour constitutes conduct unbecoming and detrimental to the public interest.

18. Danielle Le May, the dissenting member of the Hearing Panel, is of the opinion that Rail did not engage in an outside business activity without the knowledge and without the consent of his firm. In her opinion, the transaction in which Rail participated may have been an outside deal, but surely not an outside business activity. She maintains that the evidence does not allow the conclusion that this transaction was made without the knowledge and without the consent of TD.

19. Rail, like Ms. Le May, asserts that its was not a prohibited outside business activity, and that, in any case, the evidence in no way establishes that this activity was carried on without the knowledge and without the consent of TD.

**IS IT AN OUTSIDE BUSINESS ACTIVITY?**

20. Member Regulation Notice MR0434 defines a business activity as "[an activity] for which direct or indirect payment/compensation received for services or employment (i.e., "remuneration") is effected or expected." Rail argues that he received no direct or indirect compensation for the transaction in question.

21. The evidence showed that Rail played a determining role in the loan that one of his clients, HC, made to another of his clients, LV, which the latter secured by transferring all of the assets in his accounts. LV, one of Rail's and TD's largest clients, initially wanted to borrow $3 million on margin. TD would not approve this transaction.

22. After TD's refusal, Rail introduced his client, HC, to his other client, LV, with the aim of facilitating the obtaining of a loan for LV.

23. Although the evidence shows that Rail was not compensated for the role he played in this transaction, he was motivated by fear that his client LV would leave TD for a competitor, taking all the securities and assets with him. In order not to lose the client, he played an active role in obtaining the loan.

24. Rail actively participated in the preparation of the transaction, among other things, by drafting or helping to draft the related documents, notably the "loans secured by assets of LV" document, and the orders to transfer the loan amounts from HC's account to LV's account.

25. In our opinion, this is clearly an outside business activity that required TD's prior approval.

**WAS THE BUSINESS TRANSACTED WITHOUT THE KNOWLEDGE AND APPROVAL OF TD?**

26. It must be said that this transaction was not done without the knowledge of TD since the unchallenged evidence reveals that on April 5, 2000, Rail discussed it with the branch manager, Denis Bourdeau.

27. Moreover, a funds transfer request was later made between the Toronto office and the Québec City office. We cannot therefore conclude that the transaction was concealed as the wording of the Notice of Hearing and Particulars implies.

28. The Respondent's investigator had satisfied himself that TD had alleged, in its defence against a civil suit, that it had never approved this transaction. An allegation in a legal proceeding is certainly not proof of the alleged fact.

29. Christopher Climo, Compliance Officer at TD, testified that the latter had a policy which stated that before an employee could engage in an outside business activity, or outside employment, he had to inform the firm, the HR department, and obtain TD's authorization to engage in this activity.

30. Clearly, Rail did not have authorization before he began participating in the preparation of the loan that TD had refused. He obtained authorization after the fact, according to his own testimony, when he talked to his branch manager on April 5, 2000. However, the loan note having already been signed on April 3, the implication is that Rail had been working on the loan well before then.

31. We therefore conclude that the majority Hearing Panel was justified in finding Rail culpable on count 1a). This matter is not akin to the "mere inadvertence or negligence" referred to in the decision of the Hearing Panel in Re Dax Sukhraj, which Rail's counsel cites as an authority.

32. It is important to note that Rail in no way benefited from the role he played in this matter and the evidence reveals no elements of deception or dishonesty on his part. Concerned about helping one of his major clients, he neglected to obtain authorization before engaging in the aforesaid activity.

33. COUNT 2:

Rail is alleged to have committed the following violation:

> 2. In the year 2000, the Respondent, while employed with TD as a registered representative, made inappropriate use of personal and confidential information regarding two clients, HC and LV, by introducing them to one another in order to facilitate a financing project to benefit LV,

thereby engaging in conduct unbecoming and detrimental to the public interest, contrary to Association By-law 29.1;

34. The majority members of the Hearing Panel recognized that to decide on Rail's culpability on this count, it was necessary to determine whether Rail made inappropriate use of personal and confidential information regarding two clients, HC and LV.

35. The main points are outlined in paragraph 15 above.

36. The majority decision retains the following from the evidence:

> "29. The evidence revealed that:
>
> a) Rail held personal and privileged information regarding his client HC, including, inter alia, the high value of his portfolio and the fact that he was seeking high-yield investments and had a tolerance for risk;
>
> b) Rail also held personal and privileged information regarding LV. This information included the fact that he was seeking a large loan and that TD had refused him this loan on the basis of an excessive concentration of his securities;
>
> c) Rail acted as an intermediary between HC and LV in the matter of the loan transaction described in Count 1 a) and mentioned to LV that he had another client who might be able to grant him the loan refused by TD."

37. The obligation to respect the confidentiality of information obtained in the course of a registered representative's activities is stated in Standard E of the Conduct and Practices Handbook, and reads as follows:

> [TRANSLATION]
>
> "Standard E - Confidentiality
>
> Any information concerning a client's transactions and accounts must be considered confidential and may only be disclosed with the client's permission, and for purposes of monitoring, or compliance with an order from a competent authority.
>
> - Client Information: A registrant must keep confidential his clients' identity and their personal financial position. The registrant must not discuss this information with anyone who does not work for the firm, and must also ensure that client lists and other confidential documents are put away at all times to prevent a visitor from perusing them or taking them.
> - Use of Confidential Information: Information on a client's personal and financial status and transactions must remain confidential; these details shall in no case be used for trading in personal accounts, capital accounts or the accounts of other clients. Not only must the registrant avoid trading on his own account based on the information at his disposal regarding outstanding orders, but he must refrain from basing his recommendations to other clients on this information or transmitting it to other parties.
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> Example A:
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> Investment Advisor Pénélope Gendron has a client who is a technical analyst. She notices that his investments have done extremely well, so she calls up several of her clients to tell them about these successes. The clients then decide to adopt the analyst's strategies."

38. Rail has testified that he had obtained the authorization of each of his two clients to reveal their respective identities. His testimony has not been contradicted. It would have been easy for the Respondent to call either of Rail's clients to give evidence on this question, which he did not do.

39. The allegation is that Rail made inappropriate use of personal and confidential information. Rail was following specific instructions from HC and LV. The circumstances are very different from those described in Example A above. In the matter before us, the Handbook standard may not have been followed to the letter, but it cannot be construed as conduct unbecoming or detrimental to the public interest. The analysis of the Hearing Panel in Re Dax Sukhraj, published last December 3, seems relevant to us:

> "As was said in Re Doering, [2007] I.D.A.C.D. No. 27, "not every violation necessarily results in culpability under terms of ... By-law [29.1]." Or, as described in Re Bahcheli, [2004] I.D.A.C.D. No. 12, "a charge of 'conduct unbecoming' involves a prosecution which clearly engages the professional reputation and possibly the livelihood of the Respondent. Implicit in the charge is a degree of moral turpitude or, at the very least, bad faith on the part of the Respondent.
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> "Other cases have even gone further. In Re Gareau, [2005] I.D.A.C.D. No. 25, a majority of the panel held that By-law 29.1 is "primarily intended to focus upon quasi-criminal and unethical conduct, rather than negligent conduct," and in Re Ng, [2007] I.D.A. C.D. No. 47, the panel noted that a person's conduct, to fall within the terms of the By-law, "must amount to something more than mere inadvertence or negligence." Finally, in Re Octagon Capital Corp., [2007] I.D.A.C.D. No. 16, it was held that "breach of a duty of care is negligence, but it does not follow that mere negligence constitutes a disciplinary offence," but "aggravated negligence or negligent conduct which leads to conduct unbecoming can, in fact, lead to a disciplinary offence."
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> "We agree with the proposition put in Octagon that mere negligence is insufficient to find "conduct unbecoming," but that "aggravated negligence," imprecise though the term is, may be sufficient to do so."

40. Count 2 alleges that Rail introduced his two clients to each other in order to benefit one of them. This has not been proved and, in our opinion, Rail should have been acquitted of this count.

41. COUNT 3:

> Rail is alleged to have committed the following violation:
>
> 3. On or about September 18, 2000, while employed with TD as a registered representative, the Respondent failed to use due diligence to make sure that a cheque made by P. Inc., dated September 14, 2000, in the amount of $333,000 and payable to COC, was properly invested in the account belonging to COC, thereby engaging in conduct unbecoming and detrimental to the public interest, contrary to Association By-law 29.1;

42. Rail was found culpable on this count in a unanimous decision by the Hearing Panel members.

43. Rail argues that the evidence shows that the cheque made by TD was deposited in the account of a third party. TD's internal policy at the time made no provision for what a representative should do when the client wishes to deposit a cheque in the account of a third party.

44. Rail and his assistant, Ms. Pouliot, both testified that it was possible to make such a deposit to the account of a third party in accordance with the customs and practices of TD, but only if the cheque was endorsed or with the written authorization of the person to whom the cheque is payable. They explained that it would have been impossible for them to deposit a cheque to the account of a third party without the prior written authorization of the person to whom the cheque was payable.

45. Proof of written authorization was never deposited to the file, by either party. However, it was Rail's responsibility to prove this. His testimony shows that he was content to ask his assistant to do what was necessary. It was his responsibility.

46. Here are some relevant excerpts from his testimony:

R. Mr. V, at the time, told me that he wanted the money sent to Mr. HC, and the procedure was, simply, to say to me: 'So, have the money transferred to Mr. HC.' Then, I asked my assistants to do what was necessary to have the money deposited to Mr. HC's account, rather than to CO's account.

[…]

Q. Can you clarify for us what personal knowledge you had of what you just told us? What did you, personally, see or hear?

R. Well, I don't have a very accurate knowledge of the administrative side, [except] for this. For myself, I talked with Mr. V. Mr. V. said: 'I want the money transferred to Mr. C.' So, I gave those instructions to my assistants and they took the administrative steps to satisfy the client's request. I don't…

Q. But, did… You referred to two possible options.

R. Yes.

Q. Did you ask your assistants to choose one of the two options or did you leave it open?

R. I left it open. That is to say, they had… I told them what the objective was, namely that it was Mr. C. who would be receiving the money, according to LV's instructions.

[…]

Q. Right. But, in the meanwhile, were you personally involved?

R. I had no other involvement, I did not… I didn't look after the paperwork. Is that what you are asking?

Q. Alright. Yes.

R. O.K. I didn't touch the paperwork connected with the… with that transaction.

[…]

Q. … But, you don't know whether the letter exists, is that accurate?

R. Actually, it wasn't me who wrote the letter.

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Q. Do you know, yes or no, if the letter exists? Did you ever see the letter?

R. I did not see the letter.

Q. Did you check whether the letter existed? Did you ask your assistants any questions?

R. I asked my assistants to see if the letter existed.

Q. You asked your assistants questions?

R. Well, lately, we had… because of all the procedures, there.

Q. Lately. But I'm talking about, at the time.

R. No, I did not go through the process.

Q. You never asked any questions. So you don't know if a letter of authorization was signed by Mr. V.?

R. Well, I mean, usually, there would normally be one.

Q. Usually. But I'm talking about… Now we're talking facts. We're talking facts, so it's concrete. Was there a letter or wasn't there? Did you see it?

R. Well, my understanding is that there is one.

Q. Your understanding is that there is a letter, but you never saw it?

R. Correct, I did not see it.

Q. So, you are unable to testify as to whether or not there is a letter?

R. I am unable to confirm that I have seen that letter.

[…]

47. It is very important that precise formalities be observed when depositing a cheque in the account of a third party, as occurred here, and it was incumbent on Rail to ensure that everything was being done according to TD's customs and practices. Clearly, Rail failed to exercise due diligence to ensure that the cheque was indeed deposited to the client's account.

48. In our opinion, the Hearing Panel was justified in finding Rail unanimously guilty on this count.

**CONCLUSIONS**

49. Rail's appeal is allowed in part, with a decision of not guilty on count 2. The guilty verdicts on counts 1 a) and 3 are upheld.

MONTRÉAL, this 7th day of January 2009.

Pierre A. Michaud, O.C., Q.C., Chair
Daniel Leclair
Roger Casgrain, CFA