Re Donnelly

IN THE MATTER OF:

THE DEALER MEMBER RULES OF THE INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

AND

THE BY-LAWS OF THE INVESTMENT DEALERS ASSOCIATION OF CANADA

AND

JOHN DONNELLY

2010 IIROC 32

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

Hearing: January 25, 2010, in Toronto Ontario
Decision: July 28, 2010
(20 paras.)

Hearing Panel:
Thomas J. Lockwood, Q.C. (chair), Sandy Grant, David W. Kerr

Appearances:
Natalija Popovic & Andrew Werbowski, Enforcement Counsel
Joel Wiesenfeld & John Fabello, Respondent's Counsel

DECISION AND REASONS

¶ 1 On January 27, 2009, the Investment Industry Regulatory Organization of Canada ("IIROC") issued a Notice of Hearing against the Respondent, John Donnelly ("Respondent").

¶ 2 The Respondent was personally served with the Notice of Hearing on February 18, 2009.

¶ 3 The first appearance before the Hearing Panel was on March 5, 2009, at which time it was agreed that a timetable would be proposed by the parties for the Hearing Panel's consideration.

¶ 4 The parties were able to agree upon a timetable for pre-Hearing matters but not for the Hearing commencement date.

¶ 5 The parties provided written submissions with respect to the Hearing commencement date. By Hearing Panel Decision, dated May 4, 2009, it was ordered that the Hearing was to commence on January 25, 2010, and continue on January 26 to 29, February 1 and 2, 2010, if necessary.

¶ 6 On January 21, 2010, the parties entered into a Settlement Agreement. On January 25, 2010, the Hearing Panel considered the provisions of the Settlement Agreement.

¶ 7 After hearing submissions, both as to the applicable law and as to why this particular Settlement Agreement met the appropriate criteria, the Hearing Panel retired to consider whether we were in a position to accept the Settlement Agreement on the basis of the material before us.

¶ 8 After consideration, the Hearing Panel unanimously accepted the Settlement Agreement and made an Order to this effect on January 25, 2010. At that time, we advised that we would provide written Reasons for our Decision. This constitutes those Reasons.

¶ 9 The Settlement Agreement is as follows:

> "I. INTRODUCTION
>
> 1. The Enforcement Department Staff ("Staff") of the Investment Industry Regulatory Organization of Canada ("IIROC") has conducted an investigation ("the Investigation") into the conduct of John Donnelly ("the Respondent").
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> 2. The Investigation was commenced by Enforcement Department Staff ("IDA Staff") of the Investment Dealers Association of Canada ("IDA") prior to May 30, 2008. On June 1, 2008, IIROC consolidated the regulatory and enforcement functions of the Investment Dealers Association of Canada and Market Regulation Services Inc. Pursuant to the *Administrative and Regulatory Services Agreement* between IDA and IIROC, effective June 1, 2008, the IDA has retained IIROC to provide services for IDA to carry out its regulatory functions.
>
> 3. The Investigation discloses matters for which the Respondent may be disciplined by a hearing panel appointed pursuant to IIROC Transitional Rule No. 1, Schedule C.1, Part C ("the Hearing Panel").
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> II. JOINT SETTLEMENT RECOMMENDATIONS
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> 4. For the purposes of this settlement, the Respondent consents to be subject to the jurisdiction of IIROC.
>
> 5. Staff and the Respondent consent and agree to the settlement of these matters by way of this settlement agreement ("the Settlement Agreement") in accordance with IIROC Dealer Member Rules 20.35 to 20.40, inclusive and Rule 15 of the Dealer Member Rules of Practice and Procedure.
>
> 6. The Settlement Agreement is subject to acceptance by the Hearing Panel.
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> 7. The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.
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> 8. The Settlement Agreement will be presented to the Hearing Panel at a hearing ("the Settlement Hearing") for approval. Following the conclusion of the Settlement Hearing, the Hearing Panel may either accept or reject the Settlement Agreement.
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> 9. If the Hearing Panel accepts the Settlement Agreement, the Respondent waives his right under IIROC rules and any applicable legislation to a disciplinary hearing, review or appeal.
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> 10. 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 in relation to the matters disclosed in the Investigation.
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> 11. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel.
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> 12. Staff and the Respondent agree that if the Hearing Panel accepts the Settlement Agreement, they, or anyone on their behalf, will not make any public statements

inconsistent with the Settlement Agreement.

13. Staff and the Respondent jointly recommend that the Hearing Panel accept the Settlement Agreement.

III. STATEMENT OF FACTS

14. Staff and the Respondent agree, solely for the purposes of this Settlement Agreement, with the facts set out in this Section III and acknowledge that the terms of the settlement contained in this Settlement Agreement are based upon those specific facts. Staff and the Respondent agree that this settlement agreement is without prejudice to the Respondent and Staff in any other proceedings of any kind, including but not limited to civil proceedings and proceedings brought by IIROC or a securities commission.

A. PARTIES

15. At all material times, the Respondent was employed as Branch Manager in the Toronto office of Blackmont Capital Inc., a Member of IIROC (Blackmont), formerly First Associates Inc. Upon taking the role as Branch Manager, the Respondent, of his own volition, drafted a new branch compliance manual and worked on other improvements to branch compliance.

16. At all material times, the Respondent was responsible for the supervision of PV and AP, who were registered representatives of Blackmont, and their client accounts.

B. ACCOUNT OPENING

17. The clients of PV and AP included over 60 clients who opened accounts from May 2004 to January 2005 (the "JR Client Accounts"). The Respondent was responsible for supervision over these accounts.

18. PV and AP represented on the New Client Account Forms (the "NCAFs") for the JR Client Accounts that they emanated from "cold call", "personal contact" and referrals from various sources, including "Jawad", "R & A Associates" and "Rathore & Associates".

19. PV and AP did not disclose to the Respondent that in fact all of the accounts were from the same referral source, who was JR (a non-registrant) and/or a company or companies controlled by JR, including PPSI.

20. PV and AP did not disclose to the Respondent that:

    (a) PPSI is an Ontario company controlled by JR and was incorporated in or about 2002. PPSI purports to provide credit counselling services relating to locked in pension and RRSP liquidation, as well as credit and collection consulting. PPSI is allegedly a member of a group of companies, also controlled by JR, called R & A and Associates.

    (b) JR is the sole director and operating mind of PPSI; at all material times he directed all PPSI staff. JR was formerly a registrant of the Mutual Fund Dealers Association (MFDA) but was barred from registration with that association in 2005 for failure to cooperate with an MFDA investigation. The MFDA investigation related to JR's undisclosed operation of PPSI between August and November 2002. JR has never been a registrant of IIROC or any predecessor thereto.

    (c) Throughout 2004 PPSI received numerous referrals of individuals, who were experiencing financial hardship, from various collection agencies across Canada. Many of these individuals were in turn referred by JR to, and became clients of,

PV and AP (the JR Clients) for the purpose of de-locking locked in registered accounts and investing in securities in which JR and others had undisclosed self-interest.

21. PV and AP opened accounts at Blackmont for the JR Clients. The majority of the NCAFs for the JR Client accounts submitted by PV and AP share the following characteristics:

- Low income
- Low net worth
- 100% high risk tolerance
- 100% medium-term trading strategy

As well, several NCAFs contained handwritten changes to the account documentation to increase risk tolerance and/or financial information.

22. Despite the majority of the NCAFs having incongruity of low income, low net worth clients having a 100% high risk tolerance and mid-term trading strategy, the Respondent made limited inquiries of PV or AP prior to approving the opening of the JR Client accounts.

23. In addition, despite a significant number of handwritten changes to the NCAFs, the Respondent only made limited inquiries of PV or AP about these changes.

24. During the material time, the Respondent, as the supervising branch manager, or his delegate, approved and signed off on at least 60 JR Client accounts.

25. Concurrent with discussions between the Respondent and back office, on or about October 4, 2004, the Respondent sent an e-mail to PV and AP to desist from taking any further referrals from PPSI for the purpose of de-locking locked in registered accounts.

26. The Respondent subsequently approved a further approximately 20 NCAFs for JR referral clients after October 4, 2004. By that time he and the firm had some information that there may have been a connection between PPSI and the referral sources listed by the RRs on the NCAFs.

C. GRAY WOLF

27. Between December 20, 2004 and January 13, 2005, 25 JR Clients purchased, in aggregate, approximately $400,000 worth of debentures of Gray Wolf Capital Corporation (Gray Wolf). Gray Wolf was a company with limited resources, no operating track record and few assets of any value. It had been listed for trading on the Canadian Trading and Quotations Systems Inc. (CNQ) two days previously.

28. On December 22, 2004 the Respondent queried the RRs in writing about Gray Wolf purchases, but only to ask whether the security was a private placement going into a registered account.

29. On December 23, 2004, Blackmont compliance staff alerted the Respondent to the Gray Wolf trade activity in certain JR Client accounts. In particular, compliance staff inquired about the purchase of Gray Wolf debentures for GF, a JR Client, which appeared to be inconsistent with his stated objectives and risk tolerance.

30. Despite the Respondent doing some due diligence with respect to Gray Wolf, and despite being prompted by Blackmont compliance regarding suitability concerns, the Respondent permitted other JR clients to purchase Gray Wolf through to January 13, 2005.

31. After January 13, 2005, the following took place:

- On January 14, 2005, Blackmont compliance staff suggested to the Respondent that he review AP's commission runs for December 20 and 21, 2004, for the JR Client accounts;
- On January 20, 2005 Blackmont compliance staff advised the Respondent that the NCAFs for four additional JR Client accounts, approved by the Respondent in 2005, indicated that they had been referred by JR or a JR associated company and directed the Respondent to ensure that these accounts were closed;
- On January 25, 2005 the Respondent made inquiries of AP in respect of the four additional JR Client accounts; and
- On January 26, 2005 Blackmont compliance staff followed up with the Respondent regarding AP's commission runs for December 20 and 21, 2004.

32. On or about February 3, 2005 a JR Client filed a written complaint with the British Columbia Securities Commission. In this complaint, the JR Client indicates that JR gave him instructions to buy Gray Wolf and that JR was, in fact, the operating mind for decisions in the account.

33. On February 4, 2005 the Respondent in concurrence with compliance sent an e-mail to AP, with a blind carbon copy to compliance, alerting him to the issues raised by JR Client complaint and questions he could expect from compliance at a meeting to be scheduled.

34. On February 16, 2005 Blackmont compliance staff, the Respondent, PV and AP attended a meeting to review the JR Client complaint. At this meeting, Blackmont compliance staff and the Respondent expressed concerns regarding the suitability of the Gray Wolf investments in the JR client accounts.

35. Following the February 16, 2005 meeting the JR Clients were contacted and asked if they wished to sell their Gray Wolf debentures. In the majority of cases, the JR Clients sold the Gray Wolf debentures with only a nominal loss.

IV. CONTRAVENTIONS

36. The Respondent admits to the following contravention of IIROC Rules, Guidelines, IDA By-Laws, Regulations or Policies:

Count 1: The Respondent, at all material times, Branch Manager of the Toronto branch of Blackmont Capital Inc. ("Blackmont"), a Member of the Association, failed to adequately supervise the client account management activities of the accounts by the Registered Representatives, PV and AP, employees of Blackmont, during the period June 2004 to March 2005, in contravention of Association Regulation 1300.2 and Policy No. 2 (now IIROC Rules 1300.2 and 2500).

37. The following mitigating and aggravating factors are relevant:

Mitigating

- The Respondent has no previous disciplinary history and was misled by PV and AP.

Aggravating

- Of the approximately 60 JR Clients, six had no income, 13 had annual income of less than $15,000, 29 had annual income of less than $25,000 and 12 had a net worth of less than $50,000.

V. TERMS OF SETTLEMENT

38. The Respondent agrees to the following terms of settlement:

- a suspension of registration approval for 45 days as Branch Manager or from acting in any compliance capacity with any Dealer Member of IIROC; and
- a fine in the sum of $50,000.

39. The Respondent agrees to pay costs to the Association in the sum of $8,500.00.

40. Unless otherwise stated, any monetary penalties and costs imposed upon the Respondent are payable immediately upon the effective date of the Settlement Agreement.

41. Unless otherwise stated, any suspensions, bars, expulsions, restrictions or other terms of the Settlement Agreement shall commence on the effective date of the Settlement Agreement.

AGREED TO by the Respondent at the City of Toronto, in the Province of Ontario, this 21st day of January, 2010.

"Witness signature "	"John Donnelly"
WITNESS	JOHN DONNELLY

AGREED TO by Staff at the City of Toronto, in the Province of Ontario, this 21st day of January, 2010.

"Kathryn Andrews"	"Andrew P. Werbowski"
WITNESS	ANDREW P. WERBOWSKI Enforcement Counsel on behalf of Staff of the Investment Industry Regulatory Organization of Canada"

FACTORS CONCERNING ACCEPTANCE OF A SETTLEMENT AGREEMENT

¶ 10 The settlement in principle, in this case, was reached just prior to the scheduled commencement of the Hearing on the Merits. The settlement was formalized in the Settlement Agreement. This Settlement Agreement was reached by the parties after significant discussion and negotiation. It represents what they feel, with their knowledge and experience, is an appropriate resolution. Under those circumstances, in our view, a Hearing Panel should not interfere lightly in this negotiated settlement so long as the penalties agreed upon are in the reasonable range of appropriateness given the admitted conduct of the Respondent.

¶ 11 In determining whether the Settlement Agreement should be accepted, we have considered a number of factors. These include the following:

(a) whether, in our view, the Settlement Agreement is reasonable and proportionate having regard to the conduct of the Respondent, as set out therein.

(b) whether, in our view, the Settlement Agreement addresses the issue of both specific and general deterrence.

(c) whether, in our view, the proposed settlement will prevent the type of conduct, which is described in the Settlement Agreement, from occurring again in the future.

(d) whether, in our view, the proposed penalty will protect investors.

(e) whether, in our view, the Settlement Agreement will foster confidence in the integrity of the Canadian Capital Markets.

(f) whether, in our view, the Settlement Agreement will foster confidence in the integrity of the Investment Industry Regulatory Organization of Canada.

(g) whether, in our view, the Settlement Agreement will foster confidence in the regulatory process itself

¶ 12 In determining whether the proposed penalty was appropriate, we followed the guidelines provided by past Hearing Panels and considered the following factors:

- the seriousness of the allegations proved against the Respondent;
- the Respondent's past conduct, including prior sanctions;
- the Respondent's experience in the capital markets;
- the level of the Respondent's activity in the capital markets;
- whether the Respondent recognizes the seriousness of the improper activity;
- the harm suffered by investors as a result of the Respondent's activities;
- the benefits received by the Respondent as a result of the improper activity; and
- previous Decisions made in similar circumstances.

¶ 13 We also considered the IIROC Dealer Member Disciplinary Sanction Guidelines. We note that these Guidelines are not mandatory, but simply suggest the types and ranges of penalties that might be appropriate to particular case types. Staff provided a series of useful extracts from the Guidelines relevant to the type of misconduct set out in the Settlement Agreement.

¶ 14 In cases that address a failure to supervise and a contravention of IIROC Rules 1300.2 and 2500, the Guidelines recommend a maximum fine of $25,000, as well as, in appropriate cases, a period of suspension or permanent bar from supervisory and/or compliance responsibilities. The proposed sanctions in the present case meet the minimum Guideline thresholds.

¶ 15 We were also provided with a number of precedent cases, including:

(a) Re: Racine [2006] I.D.A.C.D. No. 24;

(b) Re: Corrigan [2005] I.D.A.C.D. No. 7;

(c) Re: Dunn [2004] I.D.A.C.D. No. 52;

(d) Re: Morrison [2003] I.D.A.C.D. No. 13; and

(e) Re: Milewski [1999] I.D.A.C.D. No. 17.

¶ 16 A review of the facts of these cases and the sanctions imposed reveal that the proposed sanctions in the instant case are consistent with those imposed by previous Hearing Panels on previous occasions in similar or analogous circumstances.

¶ 17 We believe that the proposed penalties will deter future misconduct by the Respondent, deter others from engaging in similar misconduct, improve overall compliance by industry participants and foster confidence in the regulatory process.

¶ 18 We also noted the nature of the proceedings, the fact that they are public and the effect that this has had,

and will have, on the Respondent.

¶ 19 After careful consideration of all of the above factors, we unanimously concluded that the Settlement Agreement was reasonable and in the public interest and should be accepted by this Hearing Panel.

PENALTIES IMPOSED

¶ 20 In summary, the penalties which were imposed on the Respondent, are the following:

(a) a fine in the amount of $50,000;

(b) a suspension of registration approval for 45 days as Branch Manager or from acting in any compliance capacity with any Dealer Member of IIROC; and

(c) costs payable to IIROC in the amount of $8,500.

DATED as of the 28th day of July, 2010.

Thomas J. Lockwood, Q.C., Chair

Sandy Grant, Member

David W. Kerr, Member