

Re Blackmont Capital Inc & Duke

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

Blackmont Capital Inc.

And

Dean Shannon Duke

2010 IIROC 57

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

Heard: November 2, 2010 in Vancouver BC
Decision: December 20, 2010
(71 paras.)

Hearing Panel:

John Rogers, Chair, Brian Field and Bob Sutherland

Appearance:

Barbara Lohmann, Enforcement Counsel for IIROC
Nigel M. Campbell, Blake, Cassels & Graydon LLP, for the Respondent, Blackmont Capital Inc.
Ronald N. Pelletier, Harper Grey LLP, for the Respondent, Dean Shannon Duke

DECISION ON PENALTY

Decision on Liability

¶ 1 Following a four day hearing, the Respondents, Blackmont Capital Inc. (“Blackmont”) and Dean Shannon Duke (“Duke”), (collectively the “Respondents”), were found to be liable for the allegations made against them by the Enforcement Division of IIROC (“IIROC Staff”) (See *Re: Blackmont Capital Inc. & Duke* [2010] IIROC No. 40) (“Decision on Liability”). This hearing was held to determine what penalties, if any, should be assessed against the Respondents.

¶ 2 In the Decision on Liability, the Hearing Panel found that:

1. The Respondents acted contrary to Rules 29.1 and 29.6 of the IIROC Dealer Member Rules (the “Rules”) by participating in an arrangement which involved the payment of commissions to a third

party which placed orders in the accounts of seven clients without disclosing the details and the existence of the arrangement to these clients (“Count 1”);

2. The Respondents acted contrary to Rule 200.1(i)(3) by effecting trades in the accounts of their clients based upon the instructions of a third party without the existence of a duly executed trading authorization enabling them to take trading instructions from such third party (“Count 2”); and
3. Blackmont acted contrary to the *Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations* (“PCMLTF Regulations”) in not having on hand documentation required by these regulations with respect to certain client accounts (“Count 3”).

Submission of IIROC Staff on Penalty

¶ 3 IIROC Staff submits that an appropriate sanction in this matter for all of Count 1, Count 2 and Count 3 is the assessment of a fine in the amount of \$1,590,166.40 against Blackmont and the assessment of a fine in the amount of \$129,126.98 against Mr. Duke. In addition, IIROC Staff submits that Mr. Duke should be prohibited from approval in all capacities of registration for a period of one year, and that as a condition of any re-approval in any capacity he must have successfully completed IIROC’s *Conduct and Practices Handbook* examination.

¶ 4 The Decision on Liability detailed a commission arrangement (the “Commission Arrangement”) involving the Respondents, a Mr. Carlos Civelli (“Civelli”), Mr. Civelli’s company, Clarion Finanz AG (“Clarion”), and an investment management corporation by the name of Professional Trading Services S.A. (“PTS”). Under the Commission Arrangement, Clarion acted as an “external asset manager” for seven European banks (the “Banks”) and in that capacity oversaw the operation of trading accounts (the “Accounts”) establish with Blackmont, for which Accounts Mr. Duke was the responsible RR. Although the Accounts were in the name of the Banks, the beneficial owners of the securities traded through the Accounts were customers of the Banks. There was no evidence that these beneficial owners were known to the Respondents. It was the lack of written consent from the Banks to the Respondents with respect to the Commission Arrangement which was the genesis of the Respondents’ liability contained within Count 1.

¶ 5 The Commission Arrangement included an agreement that of the gross commissions generated by orders placed by Clarion in respect of the Accounts, 50% would be paid to Blackmont, 20% would be paid to Mr. Duke and 30% would be paid to PTS. Over the four year period during which the Commission Arrangement was in operation, of the approximately \$2.8 million in gross commissions generated by the Accounts, Blackmont received \$1,440,160.40, Mr. Duke received \$742,126.98, and PTS was paid \$697,739.42.

¶ 6 IIROC Staff’s rationale behind the amount of the fines proposed as appropriate penalties to be assessed against the Respondents for all three Counts is that such fines should include an amount equal to the portions of the commissions received by the Respondents under the Commission Arrangement, constituting in effect a disgorgement of these commissions. It is the amount of these commissions received by the Respondents together with an additional fine of \$150,000 for Blackmont and an additional fine of \$55,000 for Mr. Duke which constitutes the fines being recommended by IIROC Staff.

Submission of The Respondents on Penalty

¶ 7 Blackmont submits that a penalty amounting to fines totaling \$220,000 would constitute an appropriate penalty. This cumulative amount is comprised of the sum of \$175,000 for Count 1, the sum of \$20,000 for Count 2, and the sum of \$25,000 for Count 3. The \$175,000 fine for Count 1 is calculated by assessing a fine in the amount of \$25,000 for each of the seven Accounts involved in the Commission Arrangement.

¶ 8 Mr. Duke submits that he should not be fined for the finding of liability under Count 1, but that he should be reprimanded, and that he be fined the sum of \$5,000 for the finding of liability under Count 2.

Decision on Penalty

¶ 9 For Counts 1, 2 and 3, the Hearing Panel imposes on Blackmont a fine in the amount of \$732,500.

¶ 10 For Counts 1 and 2, the Hearing Panel:

- (a) imposes on Mr. Duke a fine in the amount of \$265,000;
- (b) orders that as Mr. Duke is no longer working in the investment industry, that he be prohibited from approval in any capacity in the investment industry for a period of six months commencing on January 1, 2011 and terminating on June 30, 2011; and
- (c) orders that if Mr. Duke applies for readmission to the industry following June 30, 2011, a term of his re-approval include a six month period of strict supervision and the requirement that he must have first successfully completed IIROC's *Conduct and Practices Handbook* examination.

Reasons

¶ 11 Rule 20.34(2) authorizes a Hearing Panel upon finding a Dealer Member liable for a breach of the Rules to impose the following penalties:

- (a) a reprimand;
- (b) a fine not exceeding the greater of:
 - (i) \$5,000,000 per contravention; and
 - (ii) an amount equal to three times the profit made or loss avoided by the Dealer Member by reason of the contravention;
- (c) suspension of the rights and privileges of the Dealer Member (and such suspension may include a direction to the Dealer Member to cease dealing with the public) for any period of time and upon any conditions or terms;
- (d) terms and conditions of continued Membership;
- (e) termination of the rights and privileges of Membership;
- (f) expulsion of the Dealer Member from membership in the Corporation; or
- (g) any other fit remedy or penalty.

¶ 12 Rule 20.33 (2) gives similar authority to a Hearing Panel to impose the following penalties upon an Approved Person:

- (a) a reprimand;
- (b) a fine not exceeding the greater of:
 - (I) \$1,000,000 per contravention; and
 - (ii) an amount equal to three times the profit made or loss avoided by such Approved Person by reason of the contravention.
- (c) suspension of approval for any period of time and upon any conditions or terms;
- (d) terms and conditions of continued approval;
- (e) prohibition of approval in any capacity for any period of time;
- (f) termination of the rights and privileges of approval;
- (g) revocation of approval;
- (h) a permanent bar from approval with the Corporation; or
- (i) any other fit remedy or penalty.

¶ 13 It is to be noted that neither Rule 20.33 nor Rule 20.34 authorizes the Hearing Panel to order either a Dealer Member or an Approved Person to disgorge commissions earned by the offending party from actions carried out by that party which were subsequently found to be in breach of the Rules.

Disgorgement as a Factor in Determining the Penalty

¶ 14 The Ontario District Council addressed the question of disgorgement as a factor in determining a penalty in *Re: Mcrea* [2000] I.D.C.D. No. 1, and later in *Re: Mills* [2001] I.D.A.C.D. No. 7, where at paragraph 58 the Ontario District Council observed:

Although paragraph 20.10 (*currently Rule 20.33*) of the Association's By-laws does not specifically authorize a penalty requiring disgorgement of profits, it does contemplate their relevance by authorizing a maximum fine based on treble the pecuniary benefit obtained from a violation. In determining the amount of a fine, the District Council may take into account the profit obtained by a respondent as a result of a violation of the Association's By-laws or other rules.

¶ 15 In *Dimitrios Boulieris v. Staff of the IDA* OSC, 2004 LNONOSC 56 February 3, 2004, the Ontario Securities Commission, on an appeal by the IDA from a decision of the Ontario District Council, considered whether or not disgorgement of commissions received by the respondent should be considered in assessing a penalty against the respondent and observed at paragraph 50:

Where a registrant has wilfully facilitated a market manipulation, he should face severe consequences, including removal from the marketplace for an appropriate period and disgorgement of moneys received as a consequence of his conduct. Otherwise, confidence in the capital markets will suffer and the market will be at risk of further disreputable conduct, and harm from the registrant.

¶ 16 The Ontario Securities Commission allowed the appeal and imposed a fine calculated as being three times the commissions earned by Mr. Boulieris from the securities trading which was found to constitute the market manipulation. The Commission's decision was subsequently upheld by the Divisional Court of the Ontario Superior Court of Justice.

¶ 17 For the assistance of the Hearing Panel, IIROC Staff counsel provided references to decisions of courts in the United States where the question of disgorgement was considered and orders of disgorgement of profits made against respondents found liable for committing securities fraud. The general tenor of these cases was to the effect that the primary purpose of the equitable remedy of disgorgement is to ensure that those guilty of securities fraud do not profit from their ill-gotten gains.

¶ 18 From the matters referred to above, it is quite clear that in determining the amount of fines which should be imposed upon the Respondents, we should consider the amount of commissions earned by the Respondents under the Commission Arrangement and that we should decide whether to include in the amounts of the fines we determine to be appropriate an amount equal to that which would constitute disgorgement of the commissions earned by the Respondents under the Commission Arrangement.

Specific and General Deterrence

¶ 19 In *Re: Derivative Services Inc.*, [2002] I.D.A.C.D. No. 26 the District Council identified the protection of the investing public and IIROC's membership, together with the preservation of the integrity of the securities markets and IIROC's regulatory processes as being the main goals for the imposition of sanctions by a Hearing Panel upon a finding of liability for a breach of the Rules.

¶ 20 In *Mills* the Ontario District Council further refined these goals by addressing the issue of sanctions in terms of specific and general deterrence. In an often cited passage from this decision, the Ontario District Council observed at pg.3:

Industry expectations and understandings are particularly relevant to general deterrence. If a penalty is less than industry understandings would lead its members to expect for the conduct under consideration, it may undermine the goals of the Association's disciplinary process; similarly, excessive penalties may reduce respect for the process and concomitantly diminish its deterrent effect. Thus the responsibility of the District Council in a penalty hearing is to determine a penalty appropriate to the conduct and respondent before it, reflecting that its primary purpose is prevention, rather than punishment. An appropriate penalty will achieve both specific and general deterrence. The primary focus of the

District Council, however, is the respondent; the appropriateness of the penalty relates most directly to the nature of the respondent's violation, the circumstances in which it was committed and other aggravating and mitigating factors relevant to the respondent's conduct and its consequences, like those identified in the TSE Guidelines. Such considerations may lead the District Council to conclude that a respondent should be prohibited from participation in the securities industry or that a lesser penalty is sufficient to prevent repetition of the misconduct. The emphasis is thus on specific deterrence on the assumption that general deterrence will follow from an appropriate decision; cf., e.g., *In the Matter of CCI Capital Canada Ltd.*, (1999) 22 O.S.C.B. 6289 (October 8) at 6291. Although the seriousness of a respondent's conduct may incline a District Council toward increasing a penalty in order to enhance its general deterrent effect, any temptation to treat general deterrence as providing an independent basis for an additional penalty should be resisted.

¶ 21 These observations highlight that our primary goal in determining an appropriate penalty is one of prevention and not punishment; and that in attempting to achieve this goal, we should be mindful of the difference between seeking specific deterrence to ensure that the Respondents are not tempted to again in the future breach the Rules, and the appropriate general deterrence message that we wish to send to the industry as a whole. The Ontario District Council cautions us that in making this determination, we must also be mindful of not increasing a penalty over what otherwise might be considered appropriate in order to achieve specific deterrence for the purpose of accomplishing a general deterrence goal. In other words and to expand upon the sentiments of Messrs. Gilbert and Sullivan in *The Mikado*, not only "to make the punishment fit the crime", but to make the punishment fit the crime *and* the perpetrator of the crime, as well.

Specific Deterrence with Respect to Blackmont

¶ 22 Blackmont's counsel advised us at the Hearing that in May 2007, CI Financial Corp ("CI Financial") purchased Blackmont. He further advised us that in October 2009, CI Financial sold Blackmont to Macquarie Private Wealth ("Macquarie").

¶ 23 The purpose for this advice was twofold. Firstly, to make the point that CI Financial would be responsible for any monetary penalty awarded against Blackmont; and secondly, to confirm that Blackmont's current owner, Macquarie, has a strong culture of compliance together with robust education and enforcement policies which are regularly audited through an internal compliance function.

¶ 24 The fact that we have been advised that CI Financial will be responsible for any monetary award against Blackmont is irrelevant. And, while we are gratified to be advised that Macquarie takes its compliance responsibilities seriously, this is the least of what we would expect from an IIROC Dealer Member.

¶ 25 However, what is of interest to us is his advice that the CI Financial acquisition of Blackmont occurred in May 2007. It was following this acquisition that steps were taken to remedy the lack of the necessary written consents with respect to the Commission Arrangement as disclosed by the staff audit of the IDA its 2007 Sales Compliance Review. As was set out in the Decision on Liability, when Mr. Civelli refused to cooperate with this remedial action, the Commission Arrangement was terminated in November 2007. This termination of what was a profitable arrangement for Blackmont very much suggests that under CI Financial's ownership, which has now become Macquarie's ownership, a similar breach of the Rules to those reflected in Counts 1, 2, and 3 is unlikely to again occur. This indicates to us that a strong element of specific deterrence is not required in the determination of an appropriate penalty against Blackmont.

Specific Deterrence with Respect to Mr. Duke

¶ 26 However, such would not appear to be the case with Mr. Duke. Unlike Blackmont which has no history of disciplinary sanctions against it, the Decision on Liability highlights the fact that this is the third time that Mr. Duke has been disciplined for a failure to perform his role as a gatekeeper in the securities markets. It would appear that in determining an appropriate penalty for Mr. Duke, an element of specific deterrence should be included to ensure that if in the future Mr. Duke chooses to become employed in the securities industry, he will better appreciate his obligation to understand and uphold the Rules and will not repeat the conduct that has

led to his current and previous disciplinary sanctions.

Disciplinary Sanction Guidelines

¶ 27 The IIROC Dealer Member Disciplinary Sanction Guidelines, published in March, 2009, (the “Guidelines”) have two guidelines useful in assisting us to determine appropriate sanctions against the Respondents.

1.5 of the Guidelines

¶ 28 Section 1.5 of the Guidelines is entitled “*Securities Act* breach or breach of any related Provincial or Federal Legislation – Dealer Member Rule 29.1”. Our finding on Count 1 was that the Respondents were liable for breaching Rule 29.6 and Section 53 of the Securities Rules made pursuant to the *Securities Act* of British Columbia (“Section 53”). Our finding on Count 3 was that Blackmont had breached the Federal PCMLTF Regulations with respect to four of the Accounts. Therefore, a consideration of this section of the Guidelines is applicable to our determination of an appropriate penalty under Count 1 and Count 3.

¶ 29 Section 1.5 of the Guidelines lists the following six considerations for us to take into account in our deliberations:

1. Seriousness of legislative breach;
2. Clients knowledge;
3. Loss to clients;
4. Respondents’ intent;
5. Whether the Respondents were unjustly enriched and obtained/attempted to obtain a financial benefit; and
6. Whether the Respondents concealed/attempted to conceal their conduct from the Dealer Member firm or the Corporation.

¶ 30 The recommended sanctions under this section are:

- A minimum fine of \$10,000 for an Approved Person and of \$25,000 for a Dealer Member;
- Possible suspension for 3 months to 10 years, or possible ban if conduct is egregious;
- Re-write the CPH; and
- Fine should include the amount of any financial benefit to the Respondents.

¶ 31 In the introduction to the above considerations and recommended sanctions, Section 1.5 of the Guidelines cautions that the conduct dealt with by this section “may cover a very wide range of offences and various principles and penalties may be appropriate”.

¶ 32 To deal with these listed considerations in light of the evidence before us:

- (i) Seriousness of legislative breach: The Commission Arrangement although not in any manner constituting fraudulent activity does constitute a clear breach of Section 53 and Rule 29.6 in that the requisite written consents of the Banks were not on file. Nor does this oversight appear to have been an inadvertent breach of the Rules and Section 53. As was noted in the Decision on Liability, when steps were taken to have this matter remedied, Mr. Civelli balked and the Commission Arrangement came to an end. We consider these breaches of Section 53 and of Rule 29.6 to be very serious.

However, we do not find the breach of the PCMLTF Regulations to carry the same element of *gravitas*. The deficiency in the complete documentation required by the PCMLTF Regulations was found only with respect to four of the seven Accounts. This was a deficiency in documentation, with absolutely no allegation whatsoever of money laundering or terrorist financing transactions, the activity the PCMLTF Regulations were enacted to prevent.

- (ii) Clients knowledge: Although it was clear that the records of Blackmont did not contain the requisite written consents to the Commission Arrangement, what was less clear was whether or not the Banks knew of the Commission Arrangement.
- (iii) Loss to clients: There was no loss to clients.
- (iv) Respondents' intent: The evidence before us is that until it was acquired by CI Financial, Blackmont's intention was one of benign neglect, choosing not to deal with the lack of the necessary written consents for the Commission Arrangement or the complete documentation required by the PCMLTF Regulations. However, this was not the case for Mr. Duke. With respect to the Commission Arrangement, it was quite clear that Mr. Duke was concerned about the necessary paperwork being extant and certainly toward the end of the four year period during which the Commission Arrangement was in effect, Mr. Duke was actively attempting to secure the necessary documentation to comply with Rule 29.6 and Section 53.
- (v) Unjust Enrichment or Attaining Financial Benefit: There was no evidence of unjust enrichment. Rather, the evidence is that normal commissions were paid by the Banks; the trading in the Accounts was performed in accordance with the instructions of the Banks' agent, Clarion; and that the Banks had no complaints with the trading done under the Commission Arrangement.
- (vi) Attempted concealment: There was no evidence of any attempt to conceal the Accounts, the trading activity on the Accounts, or the Commission Arrangement from the IDA. Indeed, following the 2007 Sales Compliance Review by IDA Staff which brought to light the Commission Arrangement, the Respondents have fully cooperated with IIROC Staff and provided complete disclosure of all elements of the Commission Arrangement and the requisite PCMLTF Regulations documentation.

3.9 of the Guidelines

¶ 33 Section 3.9 of the Guidelines is entitled "Unauthorized Third Party Instructions – Dealer Member Rule 200.1(i)(3)". Our finding on Count 2 was that the Respondents were liable for breaching Rule 200.1(i)(3) with respect to four of the Accounts. As with Section 1.5 of the Guidelines, consideration of this section of the Guidelines is applicable to our determination of an appropriate penalty for our finding on Count 2.

¶ 34 Section 3.9 of the Guidelines lists the following five considerations for us to take into account:

1. Number of unauthorized instructions acted upon by the Registrants;
2. Whether client provided verbal authority;
3. Underlying reason for accepting unauthorized instructions;
4. Nature of instructions and its impact upon the account; and
5. Magnitude of client losses.

¶ 35 The recommended sanctions under this section are:

- A minimum fine of \$5,000;
- Re-write of CPH;
- Period of close or strict supervision; and
- Period of suspension (in most egregious cases involving elements of deception and misrepresentation to client).

¶ 36 To deal with these listed considerations in light of the evidence before us:

- (i) Number of unauthorized instructions acted upon by Registrants: The earning of gross commissions amounting to \$2.8 million for all of the seven Accounts suggests that there must have been a fair amount of trading in the four Accounts in question over the period during which the Commission Arrangement

was in place.

- (ii) Whether client provided verbal authority: It is clear from the evidence before us that verbal authority was provided by Clarion as the Banks' agent for almost all of the trading on all of the Accounts.
- (iii) Underlying reason for accepting unauthorized instructions: It is not clear from the evidence before us that the instructions were unauthorized. What is clear is that the documentation for the Accounts in the possession of Blackmont did not include the requisite written authorizations.
- (iv) Nature of instructions and its impact upon the account: The trading instructions for the Accounts were given mainly by Clarion and there was no evidence before us that these instructions had any adverse impact upon the Accounts.
- (v) Magnitude of client losses. There was no evidence before us of any losses suffered by the Banks.

Penalty Determination

Count 1

¶ 37 Determining an appropriate penalty to impose on the Respondents for the liability we have found against them in Count 1 has proven to be a challenging task. As outlined above, we have determined that with respect to Blackmont, specific deterrence should not be a factor although the same can not be said for Mr. Duke.

¶ 38 When it comes to general deterrence, we must consider the amount of the commission revenue earned by the Respondents over the four year period during which the Commission Arrangement was in place. The purpose for this is to ensure that for the breach of the Rules for which the Respondents were found liable on Count 1, the penalty assessed by us against the Respondents is considered more than merely a cost of doing business with respect to the commission revenue generated by them from the Commission Arrangement.

¶ 39 This concern would be satisfied if the concept of disgorgement is one of the elements for the amount of fines which we consider appropriate to impose against the Respondents. Section 1.5 of the Guidelines encourages us in this direction by recommending that an appropriate fine "should include the amount of any financial benefit to the Respondents".

¶ 40 This provision of Section 1.5 of the Guidelines and the concept of a perpetrator not being permitted to become unjustly enriched from wrongdoing supports the submission of IIROC Staff that the amount of the fines imposed upon the Respondents for Count 1 should amount to at least the amount of commissions earned by them as a result of the Commission Arrangement.

¶ 41 However, Section 1.5 also cautions that its provisions cover a very wide range of offences. Indeed, the failure by Blackmont to comply with the PCMLTF Regulations as included in Count 3 comes within the purview of Section 1.5. Outside of this cautionary context, it could be argued that the liability for the breach of the Rules found against Blackmont in Count 3 could require the disgorgement of the commissions earned by Blackmont as a result of the Commission Arrangement. But surely the principal of general deterrence and the sanction recommending the disgorgement of financial benefit contained in Section 1.5 does not justify a fine amounting to in excess of a million dollars for the breach of the Rules detailed in Count 3.

¶ 42 In determining the appropriate amount of fines to be imposed upon the Respondents, we are mindful of the fact that in the trading on the Accounts there was no finding of fraud, nor was there any attempt by the Respondents to conceal any aspect of the Commission Arrangement. There was no finding of any client loss. Nor was there a finding that the Respondents were unjustly enriched by having the Banks pay commissions greater than the normal commissions they would have had to pay if the Commission Arrangement had not been in place. Indeed, there was no finding of any client complaint, even though the Banks received regular statements for the Accounts during the time the Respondents were operating under the Commission Arrangement.

¶ 43 In our Decision on Liability, we questioned whether or not the customers of the Banks who were the beneficial owners of the securities traded in the Accounts had any knowledge of the Commission Arrangement.

If these customers were unaware of the payments made to PTS, it might be suggested that there was an element of fraud associated with these payments. However, the matter before us does not involve the question of the identity of these beneficial owners nor any allegation of fraud with respect to the PTS payments. Nor were the Respondents found liable for breaches of Rules relating to any of the aspects of the “know your client” rule.

¶ 44 The Commission Arrangement *per se* was not illegal. Under the Rules and under the law of British Columbia, it was perfectly legal for the Respondents to make the payments to PTS under the Commission Arrangement, provided that the Respondents had first secured the written consent of the Banks to such payments. It was not the existence of the Commission Arrangement which constituted a breach of the Rules, rather it was the failure of the Respondents to secure the Banks' written consent. Unlike the finding in *Boulieris*, the Respondents were not found liable for wilful market manipulation nor were they found liable for securities fraud. Rather, the Respondents were found liable for not having secured the requisite written consent disclosing the Commission Arrangement.

¶ 45 We are very mindful of the words of the Ontario District Council in *Mills* as above set out that in attempting to meet our concern about general deterrence we resist the temptation toward increasing a penalty in order to enhance its general deterrent effect. For this reason, and because the action, or better, the lack of action for which the Respondents have been found liable under Count 1 does not involve issues of fraud or market manipulation, we have determined that disgorgement should not be considered as an appropriate measurement in determining the amount of the fines to be imposed upon the Respondents.

¶ 46 Section 1.5 of the Guidelines recommends that a minimum fine in the amount of \$25,000 for a Member Dealer and \$10,000 for an Approved Person be considered for matters to which Section 1.5 relates. A minimum fine is not appropriate for the Respondents' breach of the Rules under Count 1. Rather to reflect the gravity with which we consider the Respondents' action we believe that a fine in the amount of three and one half times the recommended minimum sanction is appropriate.

¶ 47 Applying this benchmark to the minimum fines of \$25,000 for a Member Dealer and \$10,000 for an Approved Person as set out by Section 1.5 of the Guidelines, we determine that for each of the Accounts, a fine in the amount of \$87,500 is an appropriate fine for Blackmont and a fine in the amount of \$35,000 is an appropriate fine for Mr. Duke. As there are seven Accounts, we have determined the total amount of the fine for Blackmont for Count 1 to be \$612,500, and for Mr. Duke for Count 1 to be of \$245,000.

Count 2

¶ 48 Appropriate penalties for Count 2 cause us less concern. It is quite clear that all parties to the Commission Arrangement were fully aware of what was happening with respect to the trading in the Accounts. If there was not written authorization for this trading activity, there was certainly verbal authority. The Banks as the holders of the Accounts were sophisticated international financial institutions who received regular statements on the Accounts. There was no evidence of losses from this trading in the Accounts or of any complaint registered by any of the Banks with respect to this trading.

¶ 49 We therefore believe that the minimum fine of \$5,000 recommended under Section 3.9 of the Guidelines for both a Member Dealer and an Approved Person is an appropriate amount. As there were four of the Accounts for which the Respondents were found liable for breaching the Rules, we find that a fine of \$20,000 for each of the Respondents is an appropriate fine with respect to Count 2.

Count 3

¶ 50 As was noted above, the breach of the PCMLTF Regulations applied to the requisite documentation with respect to four out of the seven Accounts. There was no loss or harm to the Banks as a result of this documentary deficiency, there was no attempt to conceal this deficiency, nor did this deficiency result in any enrichment to Blackmont. Most importantly, there was no suggestion whatsoever that the trading in the Accounts ran afoul of the purpose or intent of the PCMLTF Regulations.

¶ 51 As with Count 2, we believe that the minimum fine of \$25,000 recommended under Section 1.5 of the

Guidelines for a Member Dealer is an appropriate amount. As Blackmont was found liable for breaching the Rules with respect to four Accounts, we have determined that a fine of \$100,000 is an appropriate penalty.

Repeat Offender

¶ 52 In his submissions, counsel for Mr. Duke highlighted the fact that over the course of the four years during which Commission Arrangement was in place, Mr. Duke sought his employer's assistance to secure the requisite written consent from the Banks for the Commission Arrangement. We agree with this observation and accept Mr. Duke's efforts as very much a mitigating factor in Mr. Duke's favour.

¶ 53 However, this is Mr. Duke's third disciplinary matter. Therefore, in addition to the fines imposed upon him, we believe additional sanctions are necessary. We do not find that a reprimand as recommended by Mr. Duke's counsel meets this requirement of additional sanctions.

¶ 54 We believe that the sanctions as above outlined including a six month suspension, the requirement of a period of strict supervision should Mr. Duke chose to reenter the industry, and the requirement that prior to reentering the industry he must have first successfully completed IIROC's *Conduct and Practices Handbook* examination will all act as specific deterrents to encourage Mr. Duke to abide by the Rules in his future employment in the investment industry.

¶ 55 We should note that without the aforementioned mitigating factor, the length of both the suspension and strict supervision requirements we would have imposed upon Mr. Duke would have been much longer.

Costs

¶ 56 Rule 20.49 of the Rules provides a Hearing Panel with the ability to award costs against a respondent where, as is the case here, there has been a finding of liability. Subsection (1) of this Rule states:

20.49 Assessment of Costs

(1) In addition to imposing any of the penalties set out in Rule 20.33, Rule 20.34 or Rule 20.45, the Hearing Panel may assess and order any Corporation Staff investigation and prosecution costs determined to be appropriate and reasonable in the circumstances.

¶ 57 IIROC Staff filed with the Hearing Panel a Bill of Costs detailing investigation and prosecution expenses relating to Count 1, Count 2 and Count 3 amounting to \$64,539.43 and submits that pursuant to Rule 20.49 an order for costs should be made jointly and severally against the Respondents in the amount of \$50,000 as being appropriate and reasonable in the circumstances for the matter at hand.

¶ 58 The Respondents submit that there should be no award for costs against them under Rule 20.49.

¶ 59 Hearing Panels have for some time been grappling with the issue of what criteria to apply in exercising the power to award costs granted to them by Rule 20.49. (See for example *Re: Jeske* [2004] I.D.A.C.D. No.40; *Re: Credifinance Securities Ltd.* [2006] I.D.A.C. D. No. 30; *Re: McLellan* [2007] I.D.A.C. No. 14; *Re Octagon Capital Corp.* [2007] I.D.A.C.D. No. 16; *Re:Ng* [2007] I.D.A.C.D.;*Re: Golden Capital Securities Ltd.* [2008] IIROC No.1; *Re: Van Hee* [2009] IIROC No. 34; *Re:Steinhoff* [2010] IIROC No. 42; and *Re:Trites* [2010] IIROC No. 48.

¶ 60 As was observed by the Hearing Panel in *Steinhoff* as it was struggling to establish touchstones upon which to base its determination as to the amount of costs which it might consider "appropriate and reasonable in the circumstances":

¶ 44 ... No guidance is obtainable from Member Rule 20.49. The fact is that that conclusion [the amount of costs that is appropriate and reasonable in the circumstances] is little more than an act of magic, virtually impossible to explain. As a practical matter, the costs "regime" is neither more nor less than an invitation to the members of the panel to appeal to their private instincts about propriety and reason.

and

¶ 46 There is, we feel bound to say, something highly unsatisfactory about Member Rule 20.49 (1). It creates

enormous uncertainty and unpredictability and great potential for unfairness, not only to respondents but to IIROC itself.

¶ 61 We agree with the Hearing Panel in *Steinhoff* and add our voices to those of other Hearing Panels to encourage IIROC to review the provisions of Rule 20.49 for the purpose of providing direction to Hearing Panels as to the criteria upon which an award of costs should be based.

¶ 62 However, there still remains before us the application by IIROC Staff for an award of costs against the Respondents in the matter at hand.

¶ 63 In *Credifinance Securities Ltd.* at paragraph 56, the Hearing Panel observed:

In recent years, there has been a trend to the awarding of quite substantial costs in these cases. We think that care should be exercised so that the fear of attracting an award of very large costs does not have the effect of inhibiting a Member, or an approved person, from advancing a defence which it thinks is meritorious. It is also worth keeping in mind, when thinking about costs, that a successful respondent cannot get its costs from the IDA. Since the power to award costs is one-sided, we think that a conservative approach to costs is not unwarranted.

¶ 64 The Hearing Panel in *Credifinance Securities Ltd.* identified two cautions with which we agree – the awarding of costs is one sided in that only IIROC is able to secure costs, and cost awards should not be an inhibitor to effectively prevent a Dealer Member or an Approved Person from mounting a defence. As well, although Rule 20.49(1) states that an award of costs is in addition to any fines that may be assessed as penalties under Rules 20.33, 20.34, or 20.35, it little matters to a respondent whether a financial obligation is imposed in the form of a fine or an award of costs, the respondent is still liable to pay the money no matter under what heading it has been awarded.

¶ 65 It is noted that Rule 20.49(1) is permissive rather than mandatory. This Rule provides that a Hearing Panel *may* assess and order costs against a respondent. This approach suggests that two decisions must be made by a Hearing Panel in the making of an award for costs. The first decision is whether or not an award is “appropriate and reasonable in the circumstances” and, if an award is merited, what should be the amount of the award. In other words, a Hearing Panel must first determine whether or not it believes that a particular respondent should be liable to have an award of costs made against that respondent, and, if such liability is found, the quantum of the costs to be awarded. We suggest that the majority of the decisions cited above of Hearing Panels bemoaning the difficulties with the provisions of Rule 20.49(1) speak to the lack of direction with respect to determining this quantum of costs.

¶ 66 Viewed in this manner, and keeping in mind that an award of costs can not be made against IIROC, a Hearing Panel should not base its decision as to whether or not a respondent should be liable for costs solely upon the respondent's lack of success in the matter before it. Rather, this decision should constitute a reflection of the Hearing Panel's view of how the respondent approached the entire disciplinary process. If the respondent takes pains to thwart the disciplinary process and the disciplinary proceeding to which the respondent is a party, thereby resulting in additional costs to IIROC, it is entirely appropriate for a Hearing Panel to determine that an award of costs should be made against this respondent. However, if the respondent actively participates in the disciplinary process, albeit with an active and vigorous defence which subsequently is determined not to succeed, the Hearing Panel should be open to determine that an award of costs is not appropriate in the circumstances.

¶ 67 The matter before us is an example of the latter situation. In this matter, the Respondents have launched a vigorous defence against the allegations made against them by IIROC Staff. Contrary to their defence, we have largely found against the Respondents. However, at no time was there ever any suggestion that the Respondents were not fully cooperative with IIROC Staff and with the disciplinary process. The Respondents responded to all the allegations against them, retained counsel at their expense, which counsel together with IIROC Staff counsel were of great assistance to the Hearing Panel, and the Respondents attended all five days of this Hearing. There is no doubt that the Respondents fully participated in the disciplinary hearing process.

¶ 68 In addition, we found in the Decision on Liability that IIROC Staff have not established some of the allegations made against the Respondents in Count 2 and against Blackmont in Count 3. If, as determined by *Jeske*, an award of costs against the Respondents is to be a function of the actual costs incurred by IIROC Staff in the prosecution of the matter against the Respondents, how is a Hearing Panel to account for the situation, such as the matter at hand, where the Respondents have been found not to be liable to the full extent of the allegations made by IIROC Staff against them? An allocation of costs among Count 1, 2, and 3 would be an exercise in futility.

¶ 69 We do not find that the Respondents in any manner abused the IIROC disciplinary process and we have determined that an award of costs should not be made against them.

¶ 70 On an additional note. In its submissions, IIROC Staff proposes that we should make an award of costs against the Respondents in a manner so that the Respondent are made jointly and severally liable for its payment. As above set out, an award of costs is to be based upon the actual costs incurred by IIROC Staff in pursuing the disciplinary process. In the matter at hand, the allegations in Counts 1, 2 and 3 were made against Blackmont, while Mr. Duke was involved only with the allegations contained in Counts 1 and 2. Although there is no evidence before us as to what costs were incurred by IIROC Staff with respect to each of the Counts and the allegations contained therein, we believe that as Mr. Duke was not included in Count 3, that it would be grossly unfair to him to impose upon him joint and several liability for any award of costs we might have made.

Decision on Costs

¶ 71 For the reasons above set out, we make no order of costs against the Respondents.

Dated at Vancouver, British Columbia this 20th day of December, 2010.

John Rogers, Chair

Brian Field

Bob Sutherland

Copyright © 2010 Investment Industry Regulatory Organization of Canada. All Rights Reserved.