INVESTMENT DEALERS ASSOCIATION

IN THE MATTER OF:

THE BY-LAWS OF THE INVESTMENT DEALERS ASSOCIATION OF CANADA

AND

JOHN PHILLIP WATTS

PANEL: The Honourable J. Armand DesRoches, Chair
R.T. (Mike) Hammer, Member
Roland Coffill, Member

COUNSEL: Tamara Brooks, Enforcement Counsel, and
Milton Chan, Student at Law, for the Investment Dealers Association

Kevin Kiley for the Respondent John Phillip Watts

HEARING: May 6, 2008

DECISION AND REASONS

1. By Notice dated April 23, 2008, the Investment Dealers Association of Canada ("the Association") informed the public and John Phillip Watts ("the Respondent") that a hearing was to be held before a Hearing Panel appointed pursuant to By-law 20 of the Association for the presentation, review and consideration of a Settlement Agreement entered into on April 15, 2008 between the Association and the Respondent.

2. The hearing was held in Charlottetown, PEI, on May 6, 2008. During the hearing the Panel received and considered the Settlement Agreement, oral submissions of counsel as well as a Settlement Hearing Book prepared by the Association which contained the relevant By-laws, regulations and guidelines, and applicable previous decisions of Hearing Panels regarding sanctions.

3. At the conclusion of the hearing, the Panel announced its decision to accept the Settlement Agreement. The Settlement Agreement will be published by the Association in due course.

4. In the Settlement Agreement the Respondent admits to the following contraventions of the Association By-laws, regulations, rulings or policies:

> *a) Between November 2006 and April 2007, the Respondent, at all material times a Registered Representative employed by Berkshire Securities Inc., a Member of the Association, engaged in business conduct or practice which is detrimental to the public interest where, he issued correspondence and/or literature which contains unjustified promise of specific results, and/or opinion or forecast of future events which is not clearly labelled as such, without the knowledge or approval of his Member Firm, contrary to Association By-Law 29.1 and 29.7;*
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> *b) Between January and February 2007, the Respondent, at all materials times a Registered Representative employed by Berkshire Securities Inc., a Member of the Association, engaged in business conduct or practice which is detrimental to the public interest by failing to act in accordance with the internal policies of his member firm by directing his clients to sign blank New Account Application forms (NAAFs) in contravention of Association By-law 29.1.*

5. With respect to the first contravention, the facts reveal that from November 2006 to April 2007 the Respondent corresponded with a number of his clients through e-mails in which he presented very optimistic predictions for the performance of the stock of a certain Toronto based public company. On numerous occasions these e-mails contained specific projections of the company's stock price for a 12 to 36 month time range. This correspondence did not identify all material assumptions made in arriving at the projections, were not clearly labelled as opinion or forecast of future events, and failed to fairly present the potential risks to the clients.

6. These actions of the Respondent were in contravention of the Association's By-law No. 29, and specifically 29.7(1) which provides, in part:

> *29.7(1) No Member shall issue to the public … correspondence … which:*
>
> *(c) uses unrepresentative statistics to suggest unwarranted or exaggerated conclusions, or fails to identify the material assumptions made in arriving at these conclusions;*
> *(d) contains any opinion or forecast of future events which is not clearly labelled as such;*
> *(e) fails to fairly present the potential risks to the client:*

7. Also between November 2006 and April 2007, the Respondent authored and distributed various sales literature promoting the same Toronto based public company. Prior to April 10, 2007, the Respondent distributed this sales literature without the knowledge or authorization of his member firm, of which he was the Charlottetown Branch Manager. He acknowledged he was fully aware of his firm's policies in this respect. Having requested approval for distribution to this clients of a new research report concerning the company in question on April 10, 2007, he was instructed on April 11, 2007 not to disseminate the report.

8. These actions of the Respondent constituted a contravention of the Association's By-law No. 29.7 which establishes the high standards of ethics and conduct expected of its members. In particular, By-law 29.1 provides in part, that members:

> *ii) shall not engage in any business conduct or practice which is unbecoming or detrimental to the public interest.*

9. The facts surrounding the second contravention reveal that on two occasions in January, 2007, the Respondent provided instructions to his clients to sign blank New Account Application Forms. This action was contrary to his firm's Compliance Manual which required the appropriate due diligence in opening a new client account. Specifically the Manual required that prior to the first account being opened for a client, a fully completed, signed and dated New Account Application Form must be obtained.

10. This action not only contravened the firm's Compliance Manual, but also the Association's By-law 29.7 as being conduct that is detrimental to the public interest.

11. The Association and the Respondent agreed to the following sanctions:

(a) A fine in the amount of

a. $7,500.00 with respect to Count 1;
b. $2,500.00 with respect to Count 2

(b) Successful completion of the Conduct and Practices Handbook examination within 6 months from the effective date of the Settlement Agreement.

(c) The Respondent shall pay a portion of the Association's costs of this proceeding in the amount of $10,000.00.

12. While counsel for the Association maintained that the actions of the Respondent constituted serious breaches of the By-laws, he acknowledged the violations could not be said to be at the high end of the seriousness spectrum. He also advised the Panel that in reaching the Agreement with the Respondent, the Association had taken into account the following aggravating and mitigating factors:

Aggravating factors:

(a) the distribution of correspondence and literature occurred over a six month period;

(b) the Respondent was Branch manager at the material time; and

(c) the importance of complying with rules in a self-regulatory environment.

Mitigating factors:

(a) there is no evidence that any client suffered harm as a result of the Respondent's actions;

(b) there is no evidence to suggest the advice given by the Respondent was not suitable;

(c) the Respondent has no previous recorded violations;

(d) the Respondent co-operated fully in the investigation and ultimate resolution of the matter;

(e) as a direct result of his actions the Respondent's employment was terminated; and

(f) the Respondent has been under strict supervision since the termination of his previous employment and his employment by another firm.

13. Counsel for the Respondent agreed with the above submissions, and also requested the Panel to consider that at no time did any of the Respondent's clients complain to his firm or to the Association about the matters giving rise to the contraventions. He pointed out that the majority of the Respondent's clients at the time were "high net worth, sophisticated investors", and that, after the Respondent's employment had been terminated, these clients had transferred their accounts to the Respondent's new firm. Furthermore, as stated in the Settlement Agreement, the Association acknowledges that the account holdings were suitable for the stated investment objectives of the Respondent's clients, and the risk factors of these accounts.

14. While the Panel was invited to consider a number of previous decisions on the matter of sanctions, the most relevant and persuasive statement relating to the Panel's decision is found in *Milewski* (Re), [1999] 1.D.A.C.D. No. 17 in which a Panel of the Ontario District Council stated:

> *Although a settlement agreement must be accepted by a District Council before it can become effective, the standards for acceptance are not identical to those applied by a District Council making a penalty determination after a contested hearing. In a contested hearing, the District Council attempts to determine the correct penalty. A District Council considering a settlement agreement will tend not to alter a penalty that it considers to be within a reasonable range, taking into account the settlement process and the fact that the parties have agreed. It will not reject a settlement unless it views the penalty as clearly falling outside a reasonable range of appropriateness. Put another way, the District Council will reflect the public interest benefits of the settlement process in its consideration of specific settlements.*

15. The Panel is of the opinion that this passage accurately describes the appropriate test to be applied in deciding whether to accept or reject a Settlement Agreement.

16. For all of the above reasons the Panel has decided the Settlement Agreement, including the terms of settlement, reasonably addresses the purpose of disciplinary sanctions taking into account both the aggravating and mitigating factors. Consequently, the Panel has accepted the Settlement Agreement.

Dated the 12th day of May, 2008.

Executed on original by:

"J. Armand DesRoches"

J. Armand DesRoches – Chair

"R.T. (Mike) Hammer"

R.T. (Mike) Hammer – Member

"Roland Coffill"

Roland Coffill - Member