



Mutual Fund Dealers Association of Canada
Association canadienne des courtiers de fonds mutuels

**IN THE MATTER OF A DISCIPLINARY HEARING
PURSUANT TO SECTIONS 20 AND 24 OF BY-LAW NO. 1 OF
THE MUTUAL FUND DEALERS ASSOCIATION OF CANADA**

Re: Peter Haralds Brauns

Heard: March 5-7, April 2-4, May 1, 2013 in Toronto, Ontario
Decision and Reasons (Misconduct): October 15, 2013

**DECISION and REASONS
(Misconduct)**

Hearing Panel of the Central Regional Council:

Mark J. Sandler)	Chair
Janet Himmeroder)	Industry Representative
Greg Juby)	Industry Representative

Appearances:

Shelly Feld)	Counsel, Mutual Fund Dealers Association of Canada
)	
)	
Peter Haralds Brauns)	In Person
)	

The Allegations

1. Peter Haralds Brauns (“the Respondent”) is a mutual funds salesperson. The Mutual Fund Dealers Association of Canada (“MFDA”) alleges that he violated its By-laws, Rules or Policies. The specific allegations are as follows:

Allegation #1: Commencing March 8, 2002, the Respondent continued to engage in personal financial dealings with clients VK, LJ and SE in relation to:

- (a) approximately \$650,000 that the Respondent received from client VK as loans to or investments in a company incorporated and controlled by the Respondent and an additional \$127,000 that the Respondent received from client VK as personal loans;
- (b) approximately \$10,000 that the Respondent borrowed from client LJ and failed to repay during LJ’s life; and
- (c) approximately \$150,000 that the Respondent obtained from client SE in July 2008 which he failed to repay prior to the commencement of the MFDA investigation into his conduct;

thereby giving rise to conflicts of interest between the interests of the Respondent and the interests of clients VK, LJ and SE which the Respondent failed to ensure were addressed by the exercise of responsible business judgment influenced only by the best interests of the clients, contrary to MFDA Rules 2.1.4 and 2.1.1.

Allegation #2: Between 2005 and December 2009, the Respondent conducted securities related business that was not carried on for the account and through the facilities of the Member by soliciting or otherwise facilitating the investment of approximately \$625,000 by LS, RF, JM and SE in a company incorporated and controlled by the Respondent and failing to repay approximately \$225,000 of that amount, contrary to MFDA Rules 1.1.1(a), 2.1.4 and 2.1.1.

Allegation #3: The Respondent failed to ensure that a conflict of interest between his

interests and those of clients LJ and VK was addressed by the exercise of responsible business judgment influenced only by the best interests of the clients when the Respondent accepted and acted upon general powers of attorney or other similar authorizations from clients LJ and VK:

(a) commencing on June 1, 2004, when the Respondent accepted an appointment as Estate Trustee with a will for the estate of client LJ; and

(b) commencing on January 6, 2007, when the Respondent accepted a general power of attorney or other similar authorization for client VK; and

(c) commencing on September 17, 2008, when the Respondent accepted an appointment as Estate Trustee with a will for the estate of client VK following the death of client VK;

contrary to MFDA Rules 2.1.4, 2.3.1(a), and 2.1.1(b) and (c).

The Applicable Rules and Commentary

2. All three allegations make reference to Rules 2.1.1 and 2.1.4. These Rules have been amended from time to time. However, at all relevant times, Rule 2.1.1 articulated the general standards of conduct that apply to an Approved Person, such as the duty to deal fairly, honestly and in good faith with clients, and to observe high standards of ethics and conduct in the transaction of business. At all relevant times, Rule 2.1.4 required, amongst other things, that Members and Approved Persons be aware of the possibility of conflicts of interest arising in connection with their business with clients. The version of the Rule made as of February 23, 2001 also required that:

(a)...[I]n the event that such a conflict or potential conflict of interest arises, the Member shall ensure that it is addressed by the exercise of responsible business judgment influenced only by the best interests of the client...

(b) Any conflict of interest that arises or can reasonably be expected to arise as referred to in Rule 2.1.4(a) shall be immediately disclosed in writing by the Member to the client prior to the Member, or any person acting on its behalf in connection with its business, conducting business for the client.

(c) Each Member shall develop and maintain written policies and procedures to ensure

compliance with Rules 2.1.4(a) and (b).

3. An October 3, 2005 MFDA Member Regulation Notice was intended to clarify the obligations of Members and Approved Persons regarding personal financial dealings with clients. It summarized both Rule 2.1.1 and 2.1.4. In relation to the latter Rule, it said, amongst other things:

Any such conflicts or potential conflicts of interest must be addressed by the exercise of responsible business judgment influenced only by the best interests of the client. Responsible business judgment requires the use of reasonable care and diligence as necessary in the circumstances to address the conflict or potential conflict in the best interests of the client. The appropriate course of action will depend on the nature of the conflict of interest and the client's circumstances. In situations involving a potentially significant conflict of interest, the exercise of reasonable business judgment may require a prohibition on the type of transaction giving rise to the conflict.

Specific Situations

a) Borrowing from Clients

Borrowing from a client by either the Member or Approved Persons raises a significant and direct conflict that in almost all cases will be impossible to resolve in favour of the client. While such activity is not explicitly prohibited under MFDA Rules, MFDA staff are unaware of any circumstances where Members or Approved Persons proposing to enter into any such arrangements would be able to demonstrate that the conflict has been properly dealt with.

Although MFDA Member Regulation Notices are not binding, they do provide guidance to the industry, and equally important, place Members and Approved Persons on notice respecting the issues which they must direct their attention to and appropriately address.

4. The version of Rule 2.1.4 made as of February 27, 2006 also required that:

(a)...Where an Approved Person becomes aware of any conflict of potential conflict of interest, the Approved Person shall immediately disclose such conflict or potential conflict of interest to the Member.

(b) In the event that such a conflict or potential conflict of interest arises, the Member and the Approved Person shall ensure that it is addressed by the exercise of responsible business judgment influenced only by the best interests of the client...

(c) Any conflict or potential conflict of interest that arises as referred to in Rule 2.1.4(a) shall be immediately disclosed in writing to the client by the Member, or by the Approved Person as the Member directs, prior to the Member or Approved Person

proceeding with the proposed transaction giving rise to the conflict or potential conflict of interest.

(d) Each Member shall develop and maintain written policies and procedures to ensure compliance with Rules 2.1.4(a), (b) and (c).

5. The MFDA Bulletin which accompanied the February 2006 amendments to Rule 2.1.4 stated that these amendments clarified that the requirements of the Rule were intended to apply to any conflicts of interest that arise between the interests of the Member or the Approved Person and the interests of the client regardless of whether they relate specifically to Member business. As well, the Bulletin stated that the amendments would also assist Members in meeting their obligations under the Rules by expressly requiring Approved Persons to report conflicts or potential conflicts to the Member. We agree though, in our view, this requirement was already implicit in the earlier version of Rule 2.1.4.

6. The second allegation against the Respondent also relies upon Rule 1.1.1(a). The Rule provided, at all relevant times, that “[n]o Member or Approved Person ... in respect of a Member shall directly or indirectly, engage in any securities related business (as defined in By-law 1.1) except in accordance with the following:

(a) all such securities related business is carried on for the account of the Member, through the facilities of the Member ...”

It is undisputed that certain qualifications on this Rule have no application here.

7. MFDA By-law No. 1 defines “securities related business” to mean any business or activity that constitutes trading or advising in securities for the purposes of applicable securities legislation in any jurisdiction in Canada. This includes securities sold pursuant to exemptions under applicable securities legislation.

8. The third allegation against the Respondent also relies upon Rule 2.3.1(a). There have been several versions of this Rule as well. Rule 2.3.1 made as of February 23, 2001 provided that “[n]o Member or Approved Person shall accept or act upon a general power of attorney or other similar authorization from a client in favour of the Member or Approved Person.” Rule 2.3.1(a), made as of December 11, 2008 is similarly worded. Rule 2.3.1(b) was added to exempt an

Approved Person whose client is his/her spouse, parent or child and where other preconditions have been met. It is undisputed that this exemption has no application here.

The Respondent's Registration History and Agreements to Comply

9. The Respondent has been registered in Ontario as a mutual fund salesperson since 1971. Since September 1999, he has been registered with Professional Investments (Kingston) Inc. ("PI Kingston"). He had served as a branch manager from 1971 to 1976.

10. PI Kingston has been a Member of the MFDA since March 8, 2002. That is why March 8, 2002 is the earliest date set out in the MFDA's allegations. It represents the date that the Respondent became an Approved Person, and thereby subject to the MFDA's jurisdiction. That being said, the events prior to March 8, 2002, relied upon by both parties, were often relevant to give context to or explain what happened after March 8, 2002.¹

11. As an Approved Person, the Respondent agreed in writing to be bound by, and comply with the MFDA Rules and to remain fully informed as to those Rules when amended. He also agreed in writing to conduct his affairs in accordance with the contents of the Policies and Procedures Manual of PI Kingston. Similarly, he signed a Standard Associate Agreement that reflected his agreement to comply with applicable securities legislation, provisions of the MFDA, and all Member policies and procedures.

12. At all relevant times, the Policies and Procedures of PI Kingston required the Respondent, amongst other things, to:

- (a) act honestly, in good faith and in the best interests of the client and to place the client's needs first in all areas in which a conflict may arise;
- (b) ...
- (c) ...
- (d) report any potential conflicts of duty to the Compliance Officer, such as outside employment;
- (e) avoid personal financial dealings with clients; and

¹ Staff submitted that hearing panels have taken different views of the use that can be made of conduct by an individual or firm that predates the assumption of jurisdiction over them by the MFDA. It is unnecessary to reconcile those views here. The allegations here are confined to post-jurisdictional conduct, although as we have said, the earlier conduct gives important context to what followed. We also accept that pre-jurisdictional conduct is relevant to penalty, if the allegations have been otherwise proven.

- (f) be aware of the possibility of conflicts of interest arising in connection with business conducted and ensure that any such conflict is handled by the exercise of responsible business judgment and governed by the best interests of the client.

13. The Policies and Procedures also prohibited Approved Persons from:

- (a) selling or engaging in a sales activity for any product that has not been approved by senior management and included on the approved product list, including any product that does not have a prospectus;
- (b) ...
- (c) accepting or acting upon a general power of attorney or other similar authorization from a client ...

14. As must be obvious, the Policies and Procedures of PI Kingston, at the relevant time, largely tracked a number of the obligations imposed on Approved Persons under the MFDA Rules.

The Burden of Proof

15. The MFDA bears the burden of demonstrating, on a balance of probabilities, that each of the allegations against the Respondent has been proven. Although the Supreme Court of Canada has rejected earlier jurisprudence that the burden of proof varies with the seriousness of the allegations and the consequences to the affected party, it remains true that evidence must always be sufficiently clear, cogent and convincing in order to satisfy the balance of probabilities test.² Any inability on our part to be satisfied on a balance of probabilities in relation to any allegation would require us to dismiss that allegation.

Our Approach to the Evidence

16. Under our Rules of Procedure, we are permitted to admit relevant evidence, such as certain kinds of hearsay evidence, which would be inadmissible in civil proceedings.³ We often exercised our discretion to receive such evidence. However, where the veracity of that evidence was challenged, particularly by the Respondent, we carefully considered whether the evidence was shown to be reliable and whether the Respondent had a meaningful opportunity to test that

² *F.H. v. McDougall*, 2008 SCC 53.

³ We are not bound by the technical or legal rules of evidence: s. 1.6(1) of the MFDA Rules of Procedure.

evidence. These considerations were relevant to the weight to be given to the evidence.

17. In our reasons, we refer to some, but not all of the evidence. However, we have considered all of the evidence tendered by both parties, consisting of *viva voce* testimony, and exhibits, including the prior statement made by the Respondent to the MFDA which he relied upon in support of his defence. We also considered the submissions, oral and written, of both parties, and the Response and Amended Response filed by the Respondent.

18. In our reasons, we generally refer to clients and other affected parties by initials. Inclusion of their full names is unnecessary to explain what we have decided and why. The use of initials provides some limited measure of privacy to those affected, particularly former clients.

19. One of the Respondent's former clients was VK. She is now deceased. One of her nieces, WR, and another niece's husband, GL, testified at the hearing. They are also involved in a related civil action against the Respondent. Significant parts of their testimony involved hearsay and even double hearsay. Some of it amounted to little more than speculation as to what VK might have thought or done. Sometimes they expressed opinions, particularly as to the Respondent's motivations. This was particularly true for WR. She described the Respondent in strong pejorative terms. Without reflecting on these witnesses, we have placed no reliance on evidence which merely constituted the witnesses' opinions, was speculative or which had limited relevance to the precise regulatory issues that we had to decide. Of course, we were entitled to consider whether the existing civil action impacted upon or tainted the credibility or reliability of any witness who testified at the hearing.

20. We gave significant latitude to the Respondent in the conduct of the hearing and when he testified. This was a reflection of the fact that he was self-represented and had little familiarity with the hearing process. That being said, he was articulate and fully capable of putting forward his position on the issues.

21. As already noted, we recognized that some of the evidence had limited relevance to the regulatory issues we had to decide. For example, we found it unnecessary to resolve, at least at this stage, some of the competing characterizations of the Respondent's conduct. Our focus was on whether the MFDA had proven misconduct as alleged. Although there still remained

credibility and reliability issues, some of which we address below, what we found striking was the extent to which the parties agreed on the most significant underlying facts once the proverbial “dust settled.” Indeed, a number of our findings are based on what the Respondent admitted.

Disposition

22. For the reasons which follow, we are satisfied that the MFDA has proven, on a balance of probabilities, each of the allegations against the Respondent.

The Client VK

The Evidence Respecting Allegation #1: Conflict of Interest

23. VK was born in 1912. She had a grade 8 education. She served in the Women’s Auxiliary Corps of the Canadian Armed Forces during World War II and thereafter served as a civil servant for much of her life. She retired in the 1970s. She was a widower. Around 1990, she sold her house and moved into a retirement home. She remained there for the rest of her life, except for the last months spent in hospital. She died on May 26, 2008, at the age of 96.

24. VK was somewhat frugal, and led a modest lifestyle. For the most part, her expenses were fixed. She was able to accumulate significant savings, largely invested in mutual funds. The Respondent had been her advisor well before he joined PI Kingston. She followed him to PI Kingston, and continued on as a client of the firm until her death.

25. VK had no children. On occasion, she asked for advice from one of her brothers, but generally, was a very private person who rarely discussed her financial affairs with others. The Respondent was the exception. He and VK had a longstanding relationship. VK trusted him, and relied on his judgment to inform her investment decisions. She regarded him as a friend and confidant, not just her advisor.

26. VK was not a sophisticated investor. Indeed, her background and education suggest the contrary. A Know-Your-Client form dated May 15, 2008 (when VK was 96, 11 days from her

death) reflected a risk tolerance of 5 out of 9 with “fair” investment knowledge.⁴

27. According to the Respondent, by 1983, all of VK’s RRSPs had been converted to annuities. The annuities alone gave her a fixed income of \$7,572 a year for the rest of her life. The Respondent testified that he had encouraged her to put money aside on a regular basis. He was troubled by the fact that the real estate lawyer who handled the sale of her house had put her into unsecured second mortgages. He ultimately convinced her that this was unwise. (We found it difficult to reconcile this evidence with the Respondent’s willingness to allow VK to make large unsecured and risky investments in the hotel project which he initiated.)

28. The Respondent testified that his job as VK’s financial advisor was to take care of her as well as his employer as a mutual fund dealer. He said that he produced very simple financial records for her that focused on her holdings. Her annual income was well in excess of \$45,000 a year. That was generated by Old Age Security, Canada Pension Plan, a government military pension, and the life annuities. He testified that by 1990, her total estate value was \$459,000 which consisted of Laurentian mutual funds (which he had placed her in) of \$203,000, \$70,000 in mortgages, loans to family members and \$70,000 in bank accounts. She also held an old mutual fund worth \$58,000 left to her by her husband, \$13,000 in Canada Savings Bonds, some corporate bonds and a GIC. She recognized that she should not move money around; it should be allowed to grow.

29. The Respondent had a dream – to build a hotel in Riga, Latvia as the Soviet Union’s grip on the country crumbled. He shared his vision with VK who appreciated the attention she received from him. He thought that he could personally raise about \$1 million and that he had enough people who would also be interested in supporting such a venture.

30. According to the Respondent, in 1992 or 1993, he realized that he did not have enough money to complete the project. He told VK that the numbers were becoming too big. She said, “Would you take me as a partner?” At that time, she had about \$450,000 in mutual funds. He told her that he might need \$2 million to complete the project. She purportedly said that he could have all of her mutual funds. He told her to talk to her family since they were her future beneficiaries. Her brother Frank apparently told her she was crazy. However, according to the

⁴ The MFDA has challenged the legitimacy of documentation prepared or signed in May 2008. That issue is addressed later in these reasons.

Respondent, she wanted so badly to be part of something, and had always been taken for granted. So she said she wanted to do this. The Respondent testified that he insisted that they do it through a company. She said that she did not want her interest diluted by another partner. Cesis Holdings Inc. (“Cesis”) was created by Janis Apse, a lawyer. According to the Respondent, Mr. Apse suggested that the Respondent leave the room at one point, and asked VK if she was sure she knew what she was doing. He indicated that she could lose all her money. She told him that she didn’t care; she trusted the Respondent.

31. At this point in the narrative, it should be noted that the Respondent described his conversations with VK throughout their “partnership” in the hotel venture. According to him, he discussed in detail with VK each of the investment decisions that affected her. These included: how much she would invest at various times, the interest rates that would flow from her investments, why the interest was not being paid to her as contemplated, why interest was being paid to other investors at the same time, and at different rates, why the interest rates on loans he made to Cesis were recorded at different interest rates, why some investments were made by VK to Cesis, and some to the Respondent personally, why the indebtedness to her was converted to shares in Cesis, and so on. However, there is little or no independent support for much of what the Respondent described as having been discussed with VK and agreed upon.

32. VK kept a binder pertaining to her investments in the hotel. It was discovered by GL when sorting her belongings. It contained the promissory notes which she received, and rough reckonings of what she was owed, sometimes in the Respondent’s handwriting and sometimes in hers. The figures contained in the binder are not always reconcilable, and have given rise to some dispute now over the total amount that VK invested in the hotel project. The binder also shows her obvious pride in the project, containing amongst other things, news clippings about the opening of the hotel and the speech given by the Respondent which credited her support for the project’s success.

33. On August 13, 1993, the Respondent incorporated Cesis, an Ontario company. It was to hold 75% of the shares of a Latvian company carrying on with the construction and operation of the hotel. The balance of the shares in the Latvian company was to be held by the Respondent’s cousin who leased the land on which the hotel was to be built to Cesis. The Respondent was the President and sole officer and director of Cesis.

34. The Respondent testified that the share distribution at the beginning was 60/40 in his favour, reflecting his contemplated commitment to fund \$1 million.⁵ He said that accountants suggested that the company be set up with minimal capital and that the shareholders loan money to the company. He did not think that he had contributed much more than \$10,000 or \$20,000 before he realized that he would not have enough money for the project. So he rolled his position (which did not involve much up front capital) into Cesis.

35. Once Cesis was incorporated, the Respondent obtained the first investment in Cesis from his client VK. It was for \$170,000 and was evidenced by a promissory note from Cesis dated August 17, 1993. The Respondent signed the note as President. It made reference to an interest-free loan which could only be extended with VK's approval. According to the Respondent, he contributed \$8,099 at the same time. This amount was reflected in the Cesis bank statements.

36. Following VK's initial investment of \$170,000, the Respondent obtained additional monies from his client as loans to or investments in Cesis. Subject to the Respondent's disagreement as to the total amount invested by VK (which is discussed below), it would appear from the existing promissory notes that VK placed about \$620,000 in Cesis as set out below:

Date	Document	Amount
August 17, 1993	Promissory Note (Interest Free)	\$170,000
September 9, 1994 (renewed Sept 9, 1996)	Promissory Note (Annual interest of 10%) One year due date. Unpaid interest to be compounded.	\$250,000 (Renewal Amount \$275,000 Representing the original principal plus one year's interest)
February 27, 1996	Promissory Note (Annual interest of 10%) Five year due date. Unpaid interest to be compounded.	\$190,000
October 29, 1996	Promissory Note (Annual interest of 10%) One year due date. Unpaid interest to be compounded.	\$10,000
	Total	\$620,000⁶

⁵ The precise distribution, according to a document introduced by the Respondent was 47/52 in his favour.

⁶ This does not include the \$25,000 added to the \$250,000 note when renewed since it does not represent funds actually advanced by VK.

37. A December 17, 1993 shareholders agreement signed by the Respondent provided that, in the event that he predeceased VK, all shares owned by him in Cesis were to be sold to her for their book value the day before he died. The Respondent testified that this agreement was prompted by VK's inquiry as to what would happen if he died. She did not want to lose control over the company. There was no corollary agreement in the event that VK predeceased the Respondent.

38. Between 1996 and 1999, the Respondent also obtained personal loans from VK. Again, subject to the Respondent's disagreement discussed below, it would appear from the existing promissory notes that these personal loans totaled \$127,000 as set out below:

<u>Date</u>	<u>Document</u>	<u>Amount</u>
June 3, 1996*	Promissory Note (Annual interest of 10%) One year term. Unpaid interest to be compounded.	\$26,000
February 26, 1997	Handwritten Demand Promissory Note	\$20,000
July 25, 1997	Promissory Note (Annual interest of 10%) One year term. Unpaid interest to be compounded.	\$10,000
June 11, 1998	Promissory Note (Annual interest of 10%)	30,000
December 22, 1999*	Promissory Note (Annual interest 0%)	\$41,000
	Total	\$127,000

39. The three notes that are not accompanied by an asterisk immediately above were not enclosed or referred to by the Respondent in a letter dated August 17, 2010 providing information requested by the MFDA to PI Kingston. The Respondent's letter purported to enclose all notes pertaining to VK. The omitted notes were found in VK's binder.

40. The disagreement over the total amount invested by VK stems from the February 27, 2006 promissory note for \$190,000. In early 2006, VK received a cheque from the bank for \$121,583.33; she redeemed her mutual funds in the American Equity Fund for \$189,284.91; and \$122,298.94 was deposited into the Cesis account. The contemporaneous promissory note

showed a loan of \$190,000.

41. The Respondent testified that at this point, he had exhausted all avenues of financing, including his personal resources and those of his wife. He and VK agreed that she would pledge her American Equity mutual funds as collateral security for a loan from the Laurentian Bank to the Respondent for the hotel. Mr. Apse confirmed in writing that he had explained VK's exposure as a guarantor to her.⁷ However, according to the Respondent, he and VK recognized that it made no sense to pay interest on a bank loan when VK could simply invest the monies directly into the hotel project. So that is what transpired. The bank loan was immediately retired. They agreed that a promissory note would be issued for \$190,000, even though the full amount had not been advanced at that time. Accordingly, various subsequent advances by VK were already captured by the \$190,000 promissory note. Some of the subsequent promissory notes were therefore issued in error.

42. The Respondent's account does not make sense. He was unable to provide a credible explanation for:

- (a) why a promissory note evidencing a debt for \$190,000 was prepared, if the indebtedness at that time was only \$122,298.94;
- (b) why subsequent promissory notes were issued for sums which were purportedly already covered by the \$190,000 promissory note;
- (c) why subsequent promissory notes were issued by the Respondent personally, if the subsequent advances were truly tied to the \$190,000 promissory note to Cesis; and
- (d) why there is no correlation between \$67,711.06 (the difference between \$190,000 and the funded \$122,298.94) and any combination of subsequent advances.

The Respondent's testimony also did not accord with his earlier account to the MFDA or any of his or VK's handwritten notes.

⁷ On January 13, 1995, Janis Apse, an Ottawa lawyer, wrote to the Laurentian Bank confirming that he was consulted by VK as to the liability she would incur as a guarantor on a loan from the bank to the Respondent. She was being asked to pledge \$142,000 in assets (share certificates in the Laurentian American Growth Fund) as collateral security for the loan. The Respondent testified that the transaction never closed in this way, and that by 1996, when the mutual funds were redeemed, their value had increased to just under \$190,000, which is in accord with the documentation.

43. The Respondent maintained that VK did not have access to the total funds which the MFDA alleges that she advanced, and that the Cesis bank records do not support the MFDA's position. However, the difference between what the MFDA alleges that VK advanced, and what the Respondent concedes is not so large as to support that position, especially when the MFDA's position is that some of the indebtedness possibly represented notional compensation to VK for costs incurred when she was compelled to liquidate her mutual funds prematurely. As well, the Respondent conceded that not all advances for the hotel went through the Cesis bank account, undermining any reliance on the account deposits as an accurate reflection of the total monies loaned.

44. An alternative explanation for what transpired makes more sense. VK redeemed the mutual funds for \$189,284.91, which was \$715.09 short of \$190,000. She had to pay capital gains taxes, redemption fees, and possibly penalties to retire the bank loan. As a result, the full \$189,284.91 was not advanced to Cesis. However, she would not have incurred these costs had she retained these mutual funds as collateral security. Accordingly, the Respondent agreed to give her credit for the full \$189,284.91. VK deposited \$122,298.94 into the Cesis account, \$715.09 more than the cheque she obtained from the bank. This was done to justify the \$190,000 promissory note, rather than a note for only \$189,284.91.

45. All that being said, it is our view that the precise amount of the indebtedness to VK need not be determined for the purpose of these proceedings. What is troubling here is that the very best explanation that the Respondent can provide for what transpired is that he was not ensuring that an accurate and complete record of what VK had loaned him and Cesis was kept. It is impossible for him to assert that only her best interests were being advanced throughout when the most fundamental aspect of her financial involvement (what she was owed) and the varying interest rates that did or did not apply to her individual advances were so poorly documented.

46. What is undisputed is that the vast majority of the funds advanced by VK were generated by the redemption of her mutual funds. This was at a time when the Respondent owed an obligation to his employer as a mutual fund dealer and to the client.

47. An agreement dated June 1996 between VK and the Respondent provided that the value of the Cesis shares, which was \$1.00 when issued, would be \$100.00, the value to be established

at either time of sale or upon the death of either party. The Respondent testified that this referred only to the Class A shares that had been distributed when Cesis was incorporated. The agreement also stated that any promissory notes which would normally become due at the time of death would be paid back to either estate over a ten year period, with an annual interest rate of 10%. This came a few weeks before the opening of the hotel in Riga on July 12, 1996, which VK attended.

48. A resolution dated August 12, 2000 of the board of directors of Cesis provided that 217,000 class B non-voting shares be issued to the Respondent, that a further 839,797 class B non-voting shares be issued to the Respondent, and that 635,000 class B non-voting shares be issued to VK, each share for the consideration of \$1.00. The Respondent signed as director and they both signed as shareholders. A shareholders resolution dated September 18, 2000 confirmed that all outstanding notes payable by Cesis to VK were to be converted to 635,000 class B non-voting shares. It appears that \$635,000 in debt owed by Cesis to VK was thereby being converted into Class B non-voting common shares of Cesis.

49. An August 2, 2000 unsigned resolution of the voting shareholders of Cesis confirmed that 100,000 class B shares of Cesis were being transferred from the Respondent to VK, and that the transfer of shares was a conversion of all outstanding notes payable by the Respondent to VK. An August 12, 2000 transfer of shares reflected the same transaction. Then, a transfer of shares dated September 18, 2000 indicated that the Respondent was transferring 376,582 class B non-voting shares of Cesis to VK in consideration for all outstanding notes payable by the Respondent to VK.

50. Although there were multiple forms of some of these documents, some bearing different dates and some being drafts rather than signed documents, the bottom line here is obvious. The debt owed by both Cesis and the Respondent to VK, and some unascertained calculation of accumulated interest on the outstanding promissory notes, was being converted to Class B non-voting shares of Cesis, each purportedly valued at \$1.00.

51. The Respondent testified that by late 1999 and 2000, he was panicking. The hotel was not making money, but VK's entitlement to interest was accumulating. In the event of her death, he would be faced with demands for money. He proposed, and VK agreed, that the debt owing to

VK be converted to shares in the company. The Respondent said that they should be talking to the beneficiaries to explain the situation. She suggested that he speak with GL and his wife, VK's niece. So he met with them and explained the conversion of the debt to shares. He said that they did not really understand what was said. GL also described a meeting that he and his wife attended with the Respondent and their limited understanding of what was said. In fairness to GL and PL, it would have been difficult for most people to understand precisely what was or was not happening at that point. The Respondent claimed that there was confusion over exactly what had been advanced by VK, and there were rough calculations of outstanding interest. He said that he effectively transferred far more shares to VK than she would otherwise have been entitled to. The Respondent did not care. In the result, VK held 1,111,582 shares of Cesis and he held 580,715.

52. Not surprisingly, it was the MFDA's position that this share conversion essentially relieved the Respondent and Cesis of any indebtedness to VK through providing her with non-voting shares of dubious value. Accordingly, the Respondent was doing VK no favour by "over-transferring" shares to her.

53. On February 23, 2001, the Respondent obtained an additional \$30,000 from VK said to be invested in common shares of Cesis to cover deficits being incurred by the hotel. This was confirmed by the Respondent in later correspondence dated November 5, 2001.

54. The Respondent testified that in 2004, they faced another dilemma. They were paying his cousin skyrocketing rent for the land. She insisted on being paid US\$500,000 if they wanted to purchase the land; otherwise, the lease would be terminated and the hotel would have to be moved. So the Respondent contacted LS, who was a wealthy 85 year old who owned a lot of land in Latvia. According to the Respondent, LS contributed about \$250,000 to enable them to purchase the land in 2004. This meant that Cesis fully owned the Latvian company which now owned the land. The Respondent claimed that the land was appraised in 2005 for 3.8 million dollars.

55. VK passed away on May 26, 2008. Cesis had made no payments to VK prior to that. One interest payment for \$25,000 was notionally made through an increase in the \$250,000 note to \$275,000 when it was renewed. Nor had the Respondent made any payments to VK.

56. The Respondent testified that a “global collapse” took place in October 2008. As a result, the cash flow from the hotel plummeted. The Respondent had lost all his capital, and remained liable for existing debts. VK did not die with any debts. He assumed them. He testified that he “relinquished his shares” because of all the conflicts that prevented him from being both the financial manager and continuing to hold the shares of the company. He later clarified that he sold his shares in Cesis for a total of \$100. In cross-examination, he admitted that, in reality, he had sold the shares in a non-arm’s length transaction to his son. He remains involved, in some capacity that is unclear, in the hotel project.

57. The Respondent was co-executor and trustee of VK’s estate, together with her niece’s husband, GL. The evidence bearing on this role and the events that followed VK’s death is better summarized when we address the third allegation. At this point in the narrative, it suffices to note that a third party, JM, with whom the Respondent dealt, agreed to purchase all of the shares held by VK’s estate in Cesis for \$25,000. This followed a meeting involving the beneficiaries, several people they consulted, and the Respondent in Arnprior. (There were conflicting accounts of precisely what was said at the meeting which we find unnecessary to address. The Respondent did not dispute one aspect of WR’s evidence about this meeting, namely that he had talked about “schmoozing an 85-year-old man” to enable him or Cesis to purchase his cousin’s land.⁸) The beneficiaries and the people they consulted subsequently raised questions about the investment advice given to VK, the relationship between her and the Respondent, the potential conflict of interest on his part, and what had happened to VK’s funds. They were dissatisfied with the \$25,000 offer obtained from JM by the Respondent, but appear to have accepted it both because they did not want to become partners in the hotel business (and assume any further indebtedness) and because the \$25,000 would enable them to hire a lawyer to pursue a lawsuit against the Respondent and his employer PI Kingston. That lawsuit was later commenced. It was dismissed against PI Kingston, though there is no evidence before us as to what, if any settlement, accompanied that disposition. It is irrelevant to us in any event. The lawsuit against the Respondent remains outstanding.

Findings Respecting Allegation #1

⁸ The evidence was unclear on whether he had indicated that the land was already purchased or that he was seeking to purchase it. It is more likely that the Respondent said that this purchase had already taken place.

58. When the Respondent became VK's "partner" in the hotel project, and caused VK to loan him and Cesis well over \$500,000, he was in a blatant conflict of interest. He had a personal and financial interest in VK investing significant unsecured sums of money in his hotel project and in doing so on favourable terms to him and to Cesis. The conflict of interest was exacerbated by his obligation to his employer as a mutual fund dealer, since he was advising VK to divest herself of her mutual fund portfolio in favour of investments in the hotel.⁹ This conflict of interest was so profound that he could not conceivably exercise responsible business judgment influenced only by VK's best interests. This was the classic situation in which the conflict could only be resolved by an absolute prohibition on obtaining monies from VK, whether their relationship is described as a partnership or as one of lender-borrower, while he was her mutual fund advisor.¹⁰

59. As we stated at the outset of these reasons, the allegations against the Respondent are only proven if he engaged in misconduct after he became an Approved Person subject to the jurisdiction of the MFDA on March 8, 2002. We are satisfied that his misconduct continued after the MFDA assumed jurisdiction over his activities. There was no need for the MFDA to prove that VK invested additional monies in the hotel after March 8, 2002. The Respondent continued to serve as VK's mutual fund advisor. He continued to engage in personal financial dealings with her. Decisions continued to be made that affected the value of and risk associated with her shares. Similarly, decisions continued to be made as to whether dividends or other forms of remuneration or compensation would flow to VK.

60. The MFDA and some of VK's beneficiaries have portrayed the Respondent as a predator who exercised undue influence on a vulnerable, elderly client. The Respondent has portrayed himself as someone who gave VK a purpose in life, and was well motivated throughout. Even the most generous interpretation of the Respondent's relationship with VK, if accepted, could not erase the conflict of interest that existed or the fact that the Respondent did not ensure that he exercised responsible business judgment influenced only by the best interests of VK. We are reinforced in that view by the unsatisfactory recording of precisely what was owed to VK, and

⁹ In cross-examination, the Respondent was asked whether it was appropriate for him, as a mutual fund advisor, based on what he had explained was his duty to bring funds in to his Member, to advise a client to redeem funds held with the mutual fund dealer to invest in an outside enterprise with him. His answer was telling: "The dilemma of being in any kind of a business and doing anything else always puts a person into, you know, how many hats do you wear? And as you point out and as we acknowledge that (sic) there arise the potential for conflict of interest between what we do in one situation and what would we do in another situation ..."

¹⁰ See *Arnold Tonnies*, [2005] MFDA Prairie Regional Council, File No. 200503, dated June 27, 2005 at pp. 13-14 considering MFDA Rule 2.1.4(a), as it then read.

the many purported changes in the interest arrangements with VK and how they compared to interest allocated to the Respondent or paid to other investors. We reject the Respondent's position that all of this was fully explained to VK – in part, because the Respondent was unable to credibly explain much of it to us. Nor did the infrequent interventions by the lawyer for Cesis constitute independent legal advice respecting much of what transpired between the Respondent and VK. VK's vulnerability, based on her age, limited education and lack of sophistication in financial affairs, construction projects, and the hospitality industry – particularly in Latvia – meant that the Respondent fell far short in ensuring that only her best interests were being advanced. Simply put, the existing conflict of interest got in the way.

61. In so concluding, there can be no distinction drawn between loans to the Respondent personally and loans made to Cesis. As the hearing panel stated in *Conrad Arthur Nunweiler*¹¹, at paragraph 17:

Where an Approved Person borrows money from a client, or arranges investments by clients in companies in which the Approved Person has a personal interest, such conduct immediately raises a significant actual conflict of interest, a conflict that in most if not all cases will be impossible to resolve in favour of the client. It is patently obvious that facilitating investments by a client in your company, or borrowing money from a client is not the exercise of responsible business judgment in the best interests of clients.

Evidence Respecting Allegation #3: Accepting Appointment as Estate Trustee and Power of Attorney for VK

62. On September 4, 1993, at the age of 81, VK made a will that appointed her brother FR and the Respondent as co-executors and estate trustees.

63. On August 27, 1999, she also appointed her brother FR as her attorney for personal care and the Respondent as her substitute attorney. On the same day, she signed a new will that again appointed her brother FR and the Respondent as co-executors and estate trustees. On June 9, 2004, she made another will with the same appointments.

64. On November 23, 2004, PI Kingston issued a “Compliance Notice re Personal Financial Dealings.” It was prompted, in part, by the complaint made by LM who was the Respondent's

¹¹ [2012] MFDA Pacific Regional Council, File No. 201030.

co-executor and trustee respecting the estate of LJ.¹² The Compliance Notice stated:

Prohibited activities include:

...

Acting as a **trustee or executor**, on a client account where you are the advisor of record. To clarify, while you are acting as either a trustee or an executor the client account(s) must be switched to another representative of the firm.¹³(Emphasis added.)

65. VK's brother FR died on September 21, 2005. Following his death, VK made a new will which again named the Respondent as co-executor and trustee, but now made GL the other executor and trustee.

66. On January 6, 2007, VK named the Respondent and GL as her attorneys for property. This empowered them to deal with VK's financial affairs. In his earlier statement to the MFDA, the Respondent denied that he had ever acted on this power of attorney. When he testified, he acknowledged that this was inaccurate. Indeed, the evidence was clear that he assumed the prime responsibility as VK's attorney for property, especially as VK became more incapacitated near the end of her life.

67. There was some troubling evidence that very shortly before VK died (when she was already 96 years old and incapacitated by illness), she purportedly prepared a Know-Your-Client form and transferred her account to Ms. Stacey, another advisor at PI Kingston and someone who had served as the Respondent's assistant in the past. Ms. Stacey had no relationship to speak of with VK. The Respondent was cross-examined on the legitimacy of this documentation. He acknowledged that VK was on a lot of medication in the final weeks and months of her life and was not thinking very clearly. He said that the "Know-Your-Client" form, although dated May 15, 2008, was signed earlier, but undated. The Respondent could not "confirm" that the document was created using VK's signature stamp. The stamp had been created because VK was unable to apply her signature to documents. His evidence included the following:

¹² Also referred to at paragraph 92 of our reasons.

¹³ According to Rule 2.3.1, it is prohibited to accept or act on a general power of attorney or similar authorization from a client even if the holder of the power of attorney ceases to be the Approved Person of record on the account unless the client is a spouse, parent or child of the Approved Person.

Q. And the purpose of this document was to show VK¹⁴ as a client of Bonnie Stacey upon her death; do you agree with me?

A. Her account needed to be transferred if I was to do anything with regards to her estate.

...

Q. I put to you that this document was created solely for the purpose of papering the record to suggest that you were no longer her advisor at the time of her death.

A. That's correct.

The Chair: It was being suggested to you in effect that this document is in the nature of a sham, that it's just being [done] to paper the file to make it look like something which it wasn't ...

A. That's correct.

The Chair: So, you're agreeing that this is just being done to make it look like something it wasn't.

A. Well, no. VK knew that we had to – we're going to have to move it and it wasn't a sham as such, but we had to do the – we had to –the paperwork had to be – had to be done.

...

Q. And Bonnie Stacey was not present with VK to your knowledge when that document was created, the document that's Exhibit 6-21?

A. I'm just wondering. Was she? Was she? Was she? Was she? Was she?

Q. Eleven days prior to VK's death.

A. No. Bonnie did go over to the hospital and had VK sign. We didn't date it at that time....She did go over and she was – she was there but VK was in failing health, no question about it....

The Chair:So, your evidence is that Bonnie Stacey would have to go witness this document, sign[ed] or the subject of a stamp by VK, you can't remember which.

A. I can't remember which.

...

The Chair: ... And what was the time frame that you say the document was actually signed to your understanding by VK because you said it wasn't on May 15th, 2008.

¹⁴ Initials have been substituted when these passages are reproduced.

A. It was between – between February and March I think in that period.

The Chair: And is there any reason that you understand why the document wouldn't have been dated the day it was witnessed as opposed to May 15th, 2008?

A. No, and I can't answer that. You know, VK – VK signed. She understood that that had to be done and for whatever reason we didn't do the transaction, didn't transfer the account until – until I think we finally realized that we have to do this because VK is now very much failing.

The Respondent denied Staff's suggestion that the document was only created after VK passed away.

68. On May 26, 2008, VK passed away. On September 17, 2008, the Respondent and GL were formally appointed as the co-executors and trustees pursuant to VK's will. The Respondent took steps, as co-executor and trustee, to distribute the contents of VK's estate to the beneficiaries.

69. In cross-examination, the Respondent was asked about the propriety of accepting the appointment as co-executor of VK's estate. He testified that this was not raised as an issue with him for some time. He did ask Valerie Nixon, the lawyer who facilitated the formal appointment following VK's death, whether he should accept the appointment. She purportedly told him that this was what VK wanted and that he should do so. As well, she noted that there would be a co-executor. The Respondent conceded that Ms. Nixon did not have the MFDA guidelines when she spoke to him.

70. The Respondent testified that VK was in difficult physical shape near the end of her life; she only trusted the Respondent and GL with her affairs. The Respondent wrote the bills that needed to be paid. He never mismanaged anything. Nor did he seek compensation for what he did. From December 2007 until her death, VK was mostly at the hospital. There was no family member other than GL who was prepared to come forward. The Respondent believed that he was the only one willing to help. GL asked him to arrange the funeral as well.

Findings Respecting Allegation #3

71. The MFDA alleges that by accepting and acting upon a power of attorney and by

accepting his appointment as estate trustee for the estate of VK and acting on the resulting authority, the Respondent contravened MFDA Rules 2.3.1, 2.1.4 and 2.1.1(b) and (c) and failed to address a significant conflict of interest by the exercise of responsible business judgment influenced only by the best interests of the client.

72. At the relevant time, Rule 2.3.1 was clear. The Respondent was precluded from accepting or acting upon a general power of attorney or other similar authorization from a client in his favour while he was an Approved Person. There is no dispute that the Respondent accepted and acted upon a general power of attorney from his client VK. Nor is there any dispute that he was aware of, and accepted, his designation as the co-executor and trustee of VK's estate before she died, regardless of when the formal appointment was later made.

73. A power of attorney is specifically addressed in Rule 2.3.1. We conclude that the designation as co-executor and trustee of a client's estate constitutes a "similar authorization" within the meaning of the Rule. Even if it did not, by acting as a co-executor and trustee of the estate of a client with whom the Respondent had unresolved personal financial dealings, the Respondent was in a conflict of interest which prevented him from exercising responsible business judgment solely in the best interests of the client. PI Kingston's November 23, 2004 Compliance Notice made this clear to the Respondent. This allegation has been proven.

The Client LJ

The Evidence Respecting Allegation #1: Conflict of Interest

74. LJ was born on August 2, 1936. She and her husband TJ were longstanding clients of the mutual fund dealers at which the Respondent was registered. The Respondent had served as their advisor since 1977.

75. The Respondent obtained an unsecured loan of \$10,000 from LJ.¹⁵ He agreed to make regular interest payments on the loan. It was to be a demand loan that would be repaid

¹⁵ The Respondent was unable to recall the precise date or year that the original loan took place. LJ's husband was still alive at the time. In the Respondent's statement to the MFDA, he felt that LJ and her husband agreed to the loan in 1998 or 1999. Exhibit 8-63 is an April 19, 2003 promissory note to LJ which replaces all previous notes. Any earlier notes are not available. Nothing turns on the precise date or year that the original loan took place.

immediately if a need arose. The promissory note bore interest at the rate of 6% per year. The Respondent described the interest rate as “arbitrary.”

76. The Respondent testified that LJ had asked if she could help him. She knew that he was in desperate shape at the hotel. The Respondent said okay. In his testimony, he said this:

Mr. Brauns: I shouldn't have at that time because every time we needed money, I was transcending a rule. But at that time we were just not aware of that...

The Chair: I just want to be clear on the record because that's what I was asking. When you say you were transcending a rule, what do you understand the rule to be that you were transcending?

Mr. Brauns: Well, borrowing personally. Borrowing from clients, okay....

77. In May 2000, TJ passed away.

78. On October 30, 2002, LJ made her will. She named her relative LM and the Respondent as co-executors and trustees. LJ passed away on February 26, 2004.

79. Between March 8, 2002 (when the MFDA acquired jurisdiction over the Respondent) and February 26, 2004, when LJ passed away, the Respondent did not repay the outstanding \$10,000 principal loan amount to his client LJ.

80. By emails dated April 30, 2004, LM questioned PI Kingston about whether it was appropriate for an investment advisor to be an executor of the estate. She was interested in the Respondent voluntarily withdrawing as an executor since he owed money to the estate and was therefore in a conflict. On May 5, 2004, the Respondent wrote to PI Kingston. He stated, in part:

The MFDA rules on borrowing money from clients came out in the next years following and I was aware that this note was in contravention to the stated rules that advisors could not borrow money from clients. The repayment should have been done when the rules were identified, but we have tried to make our corrections over time. In [LJ]'s case, her illness was in its final stages and I did not want to disturb the regular flow of interest that

she had gotten used to.

81. On May 7, 2004, the Respondent repaid the estate of client LJ the sum of \$10,129.59.

82. On June 1, 2004, the Respondent was formally appointed as co-executor and trustee of the estate.

Findings Respecting Allegation #1

83. When the Respondent's client, LJ, loaned him money for the hotel, he was in a blatant conflict of interest. He had a personal and financial interest in LJ investing \$10,000 in his hotel project without any security whatsoever. As we stated in connection with VK, this conflict of interest was so profound that he could not conceivably exercise responsible business judgment influenced only by the best interests of LJ. In our view, this conflict could only be resolved by an absolute prohibition on borrowing monies from LJ. Indeed, the Respondent appears to now acknowledge that he was absolutely prohibited from borrowing money from LJ while he was her mutual fund advisor.

84. As we have already stated, the allegations against the Respondent are only proven if he engaged in misconduct after he became an Approved Person subject to the jurisdiction of the MFDA on March 8, 2002. We are satisfied that his misconduct respecting his client LJ continued after the MFDA assumed jurisdiction over his activities. Again, there was no need for the MFDA to prove that LJ invested additional monies in the hotel after March 8, 2002. The Respondent continued to serve as LJ's mutual fund advisor. Her loan to the Respondent remained outstanding. Decisions were being made as to whether and what interest would be paid to LJ. As a result, he had continuing financial dealings with her. As he has acknowledged, he was obligated to repay the loan immediately to remain compliant with MFDA Rules. Alternatively, he could have made immediate arrangements to ensure that LJ was no longer a client. He did neither. This allegation has been proven.

85. In fairness, the fact that the Respondent regularly paid interest to LJ might be a relevant consideration on penalty. However, it also illustrates how problematic his conflict of interest was in relation to VK. LJ was receiving regular interest payments on her loan to the Respondent

while VK was not. The Respondent was increasing his personal indebtedness by borrowing from LJ. We reject the suggestion that the Respondent discussed every debt he was taking on with VK, their status, and the interest rates he was paying or agreed to pay in each instance.¹⁶

Evidence Respecting Allegation #3: Accepting Appointment as Estate Trustee

86. As already reflected, on October 30, 2002, LJ made the Respondent the co-executor and trustee under her will. On June 1, 2004, he was formally appointed.

87. At the relevant time, MFDA Rule 2.3.1 expressly prohibited an Approved Person from accepting¹⁷ or acting upon a power or attorney or other similar authorization from a client. The policies and procedures manual of PI Kingston dated May 16, 2001 contained the same prohibition.

88. The Respondent testified that when LJ died in 2004, his co-executor LM was acting unreasonably. She was incensed that she was not left more money. The two of them could not get along. She complained about his outstanding loan. The Respondent was instructed by his employer's compliance department to repay the loan right away. No issue was raised by the compliance department with his continuing role as co-executor. Given the disagreement between the executors, a lawyer was hired to administer the estate. The Respondent was never paid anything for his role and the lawyer completed everything. But the Respondent was not going to allow the co-executor to "rape" the estate.

Findings Respecting Allegation #3

89. At the hearing, the MFDA alleged that "[t]hese circumstances in which the Respondent accepted an appointment as estate trustee for client LJ's estate when he was a debtor owing money to the estate and when he was the mutual fund salesperson responsible for servicing the account of client LJ's estate, gave rise to an irreconcilable conflict of interest that could not be adequately addressed by the Respondent except by declining the appointment as estate trustee."

¹⁶ Exhibit 9, which was received as an Agreed Statement of Facts between the parties shows 21 loans that the Respondent obtained from various parties between 1995 and 2010 totaling \$1,577,000.

¹⁷ In relation to an authorization from a client that only becomes effective after that client's death and a formal appointment, the prohibition commences when the Approved Person "accepts" or "acts" upon the authorization (i.e. when the Approved Person agrees with a client to act as the executor under his/her will).

90. We agree. The Respondent was prohibited from accepting the authorization to act as the co-executor of his client's estate. His decision to accept the authorization, when LJ named him in her will, was particularly problematic given his outstanding loan to her. He cannot maintain that any alleged concerns about his co-executor explain his decision to do so, since his acceptance predated any such difficulties. He could not serve as co-executor free from a disabling conflict of interest. The fact that he repaid the loan once the issue was raised, and that, according to him, he was motivated by concerns about his co-executor's conduct not to decline the formal appointment may be relevant to penalty, but not to excuse his conduct. This allegation has been proven.

The Client SE

Evidence Respecting Allegation #1: Conflict of Interest

91. On November 23, 2004, PI Kingston circulated a compliance notice to remind Approved Persons, including the Respondent, of their obligation not to engage in personal financial dealings with clients by "borrowing funds from clients [or] having client cheques payable to the advisor or a corporation of the advisor for securities related transactions."

92. In July 2009¹⁸, the Respondent obtained an investment in Cesis of \$150,000 from SE. (It was not conceded by the Respondent that SE was a client at the material time. Accordingly, the evidence bearing on that issue will be addressed below.) The Respondent provided her with a promissory note from Cesis reflecting that she would receive 8% interest per year.

93. In July 2010, the \$150,000 loan was renewed for another year. SE understood that the Latvian economy was not performing well, and that this affected the hotel. Accordingly, she proposed to reduce the interest payable on her investment to 4%. That became the new rate.

94. In August 2011, after the Respondent was interviewed by MFDA Staff concerning this transaction and others, the Respondent arranged for Cesis to fully repay all amounts owed to SE.

¹⁸ It was also suggested that the investment by SE commenced in 2008. Even if this is so, it does not materially affect our findings.

95. SE was called as a witness by the Respondent. She is currently a pastor in Cleveland, Ohio. She lived in Canada from 1959 to 1981 and from 1982 to 1991. The Respondent was the voluntary treasurer at her church. There was never a question about his honesty or integrity.

96. While SE was a pastor in Ottawa, she invested \$2,500 with the Respondent in mutual fund RRSPs. He did not recommend any other products. In 1991, when she accepted a position in the United States, the Respondent recommended that she sell the RRSPs because under the Canada/U.S. securities rules, they could no longer be traded and he could no longer act as her advisor. She did not follow his advice, and allowed the investment to sit.

97. The Respondent never solicited SE to invest in Cesis. She approached him to invest in the hotel. He raised other options with her. He discussed the risk in doing so. She felt that the loan was open-ended, and that she could recall it at any time if she needed the money. It was renewed on a year-to-year basis. She confirmed that it was at her initiative that the interest rate on her loan was reduced. She was surprised when she learned that the MFDA had ordered that she be repaid. She felt that it wasn't anyone else's business. She did not know if the Respondent's business partner was consulted about the terms of her agreement with the Respondent. She was regularly paid interest in accordance with that agreement.

98. In cross-examination, SE was shown the PI Kingston statements concerning her investment account. The statements identify the Respondent as her advisor. However, she testified that the account had been dormant since 1991. As she understood it, it was just accruing interest. Because of her residency status, she was not permitted to add to that account. She could not recall if she signed documents to have her account moved when the Respondent changed his registration to a different dealer.

99. The Respondent testified that he was restricted in dealing with SE's account once she moved to the United States, other than allowing for liquidation. He would continue to earn trailer fees on the RRSPs she owned. But from his perspective, a client is somebody you can consult with and advise. It would have been simple, had it occurred to the Respondent, to transfer the account to somebody else when SE decided to loan him money. After the Respondent paid off SE's loan, he asked Ms. Stacey to send the relevant documentation to SE.

100. In cross-examination, the Respondent acknowledged, based on documentation shown to him, that in fact, there were occasional transactions processed in SE's account which were allowed at that time. He signed the documentation as her advisor. He assumed that he received trailer fees as well.

Findings

101. The Respondent remained SE's mutual fund advisor, albeit in a restricted capacity, once SE moved to the United States. He continued to receive trailer fees in connection with her RRSPs, and had the ability, at the very least, to take instructions from her to liquidate the RRSPs. To state the obvious, this situation was significantly less troubling, in some respects, than the others already described. That is relevant to penalty. However, the Respondent was precluded from borrowing money from SE, but did so. He was in a conflict of interest which prevented him from ensuring that he exercised responsible business judgment influenced only by SE's best interests. This allegation has been proven.

Alleged Securities Related Business with Multiple Lenders

The Evidence Respecting the Various Lenders Named in Allegation #2

102. As noted at the outset of these Reasons, the second allegation against the Respondent is that between 2005 and December 2009, he conducted securities related business that was not carried on for the account and through the facilities of the Member by soliciting or otherwise facilitating the investment of approximately \$625,000 by LS, RF, JM and SE in a company incorporated and controlled by the Respondent and failing to repay approximately \$225,000 of that amount.

103. The evidence pertaining to SE's \$150,000 investment has already been outlined.

104. In 2005, the Respondent obtained \$250,000 from LS for Cesis. In 1998, LS Ltd. had previously invested about \$300,000 in Cesis which had been repaid. As of May 2011, this loan had not been fully repaid.

105. In August 2009, the Respondent obtained \$50,000 from RF for Cesis. As of May 2011, the full amount of the investment remained outstanding.

106. In 2002, JM invested \$150,000 in Cesis. He was repaid. We are unclear as to whether this investment was made before or after March 8, 2002. JM was the same individual who purchased all of the shares in Cesis held by the estate of VK for \$25,000 and who contributed to the purchase of the land on which the hotel was built.

107. These and other loans obtained by the Respondent are outlined in Exhibit 9, which was tendered as an Agreed Statement of Facts.

108. There is no suggestion that these investments were known to the Member when they were made. None of them were carried on for the Member's account or through the facilities of the Member. None of these were investment products approved by the Member.

Findings

109. There was no real dispute as to the key underlying facts relied upon by Staff to support this allegation. The real issue was whether the Respondent was thereby engaged in securities related business.

110. At all relevant times, MFDA Rule 1.1.1 precluded an Approved Person from engaging in any securities related business unless carried on for the account of the Member, and through the facilities of the Member. "Securities related business" under MFDA By-law No. 1 means any business or activity that constitutes trading or advising in securities for the purposes of applicable securities legislation in any jurisdiction in Canada. This includes securities sold pursuant to exemptions under applicable securities legislation.

111. We agree with Staff's submissions that the Rule enables the Member to:

- (a) bring to bear its "Know-Your-Product" expertise;
- (b) more easily identify potential conflicts of interest related to the product;
- (c) ensure that the product is one which the Approved Person is qualified and registered

to sell and that the client is eligible to purchase; and

(d) fulfill its supervisory obligations, including the assessment of the appropriateness of the investment recommendation.

112. The Standard Associate Agreement with PI Kingston that the Respondent signed on June 21, 2002 also precluded him from “selling or engaging in a sales activity for any product that has not been approved by senior management and included on the approved product list, including any product that does not have a prospectus.”

113. Under s. 1 of the *Securities Act (Ontario)*¹⁹ (“the Act”), a “security” includes a note or other evidence of indebtedness, a share and any agreement providing that money received will be repaid. It is obvious that the definition of “security” easily extends to the Respondent’s agreements that he or Cesis will repay monies loaned to him or Cesis. Section 1 also provides that “trading” includes “any sale or disposition of a security for valuable consideration ...but does not include a purchase of a security²⁰ ... , a transfer, pledge or encumbrance of securities for the purpose of giving collateral for a debt made in good faith.” At the very least, the Respondent was disposing of securities so as to engage MFDA Rule 1.1.1. The jurisprudence supports this conclusion.²¹ So does a purposive interpretation of the Rule which is designed to protect clients in the ways described in paragraph 111. Apart from the reference to JM’s \$150,000 investment, which may not have been made after March 8, 2002, this allegation has been proven.

Conclusion

114. Based on the totality of the evidence, the MFDA has proven on a balance of probabilities that the Respondent has engaged in the three particulars of misconduct identified in the Amended Notice of Hearing. The hearings coordinator will set up a teleconference to set a date or dates to address the issue of penalty.

¹⁹ R.S.O. 1990, c. S.5 as amended.

²⁰ Except as provided for in clause (d) of the definition, which is not applicable here.

²¹ See *Wijaysri Sivasubramanian*, [2011] MFDA Central Regional Council, File No. 200506 dated August 22, 2005 at paras. 23 and 29; *Tadeusz (“Ted”) Bytnar*, [2011] MFDA Prairie Regional Council, File No. 201015, dated April 6, 2011 at paras. 13, 18-20.

DATED this 15th day of October, 2013.

“Mark J. Sandler”

Mark J. Sandler,
Chair

“Janet Himmeroder”

Janet Himmeroder,
Industry Representative

“Greg Juby”

Greg Juby,
Industry Representative

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