



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

File No. 200718

MUTUAL FUND DEALERS ASSOCIATION OF CANADA

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: Kenneth Roy Breckenridge

DISCIPLINARY HEARING

Heard: October 31, 2007
Toronto, Ontario

DECISION and REASONS

Hearing Panel of the Ontario Regional Council:

Thomas J. Lockwood, Q.C.	Chair
Sandy Grant	Panel Member
Richard Williams	Panel Member

Appearances:

Jason Bennett)	for Mutual Fund Dealers Association
)	of Canada
Kenneth Roy Breckenridge)	not in attendance personally or by
)	counsel

1. THE ALLEGATIONS

By Notice of Hearing, dated the 22nd day of June, 2007, the following allegations were made against Kenneth Roy Breckenridge (“Respondent”):

Allegation #1: Between November 2002 and October 2004, the Respondent engaged in securities related business outside the accounts and facilities of the Member by recommending and facilitating the investment of client funds in the total amount of approximately \$1.9 million in a security unknown to and unapproved by the Member, contrary to MFDA Rule 1.1.1.

Allegation #2: Between November 2002 and April 2006, the Respondent failed to observe high standards of conduct in the transaction of business and engaged in business conduct that was unbecoming and detrimental to the public interest by deliberately concealing from the Member business activity he was engaging in outside the Member, contrary to MFDA Rule 2.1.1(b) and (c).

2. SERVICE

The Notice of Hearing provided for a First Appearance by teleconference before the Hearing Panel at 121 King Street West, Suite 1000, Toronto, Ontario, on Wednesday, September 5, 2007, at 10:00 a.m. At that time, the Respondent did not appear. Further, no one appeared on his behalf.

At the First Appearance, Enforcement Counsel filed two Affidavits showing that the Respondent had been served with the Notice of Hearing. In an Affidavit of Josie Costantini, which was marked as Exhibit 2, it was deposed that on June 22, 2007, a copy of the Notice of Hearing and related documents were sent to the Respondent at his last known address as recorded in the Records of the National Registration Database, with which the Respondent is or was registered. This package was delivered to that address on June 26, 2007.

In an Affidavit, sworn on the 28th day of June, 2007, John Hall Vollmar, swore that, on June 27, 2007, he personally served the Respondent with, *inter alia*, the Notice of Hearing. This Affidavit was marked as Exhibit 3.

After considering Exhibits 2 and 3 and hearing the submissions of Enforcement Counsel, the Hearing Panel concluded that the Respondent had been properly served with the Notice of Hearing under both Rule 4.2(1)(a) and Rule 4.2(1)(b) of the MFDA Rules of Procedure and that he was aware of the proceedings against him.

On the First Appearance, the Hearing Panel was also advised that the Respondent had not served or filed a Reply within 20 days of being served with the Notice of Hearing, as required by Rule 8.1(1) of the Rules of Procedure.

We ordered that the Hearing on the merits in this matter would take place before the Hearing Panel at 121 King Street West, Suite 1000, Toronto, Ontario, on Wednesday, October 31, 2007, commencing at 10:00 a.m.

We further ordered that Staff was to send a letter to the Respondent, via regular and registered mail, advising him of the date, time and place of the Hearing on the merits. The letter was also to remind the Respondent of his entitlement to appear and be represented by counsel or agent at the Hearing and make submissions, present evidence and call, examine and cross-examine witnesses. The letter was, finally, to advise the Respondent that he still could participate in the proceedings despite his failure to file a Reply in accordance with the Rules of Procedure. A copy of the formal Order of the Hearing Panel, dated September 5, 2007, was to be enclosed with the letter.

The Respondent did not appear on October 31, 2007. No one appeared on his behalf.

Prior to October 31, 2007, the Respondent forwarded a lengthy Reply to Enforcement Counsel who, in turn, made arrangements for a copy of same to be delivered to members of the Hearing Panel. This Reply was considered in detail by the Hearing Panel and was marked as Exhibit 6 at the Hearing on the merits.

Just prior to the commencement of the Hearing on the merits on October 31, 2007, the Hearing Panel was provided with a series of e-mails, which had passed between the Respondent and Enforcement Counsel between October 24, 2007, and October 30, 2007. This exchange of e-mails was marked as Exhibit 7 at the Hearing.

In the last paragraph of the October 24, 2007, e-mail, the Respondent stated, in part, that "I am also entertaining the idea of attending the Hearing" In the last paragraph of his e-mail of October 30, 2007, the Respondent stated, in part: "I question whether there is any value for me to attend the Hearing as I am entering a guilty plea and cannot add any more information than I have"

In a voice mail message left with Enforcement Counsel just minutes prior to the commencement of the Hearing, the Respondent advised that he had tried to make it to the Hearing, that he was stuck in traffic and that he was definitely not going to be able to attend the Hearing. In order to give the Respondent every opportunity to attend, the Hearing Panel delayed, for a short time, the commencement of the Hearing on the merits on October 31, 2007.

When the Respondent did not appear, the Hearing on the merits commenced with the proviso that if the Respondent appeared, prior to the end of the Hearing, he would be at liberty to fully participate in the Hearing. The Respondent did not appear prior to the end of the Hearing.

In our view, every reasonable attempt was made by Staff and by the Hearing Panel to ensure that the Respondent could, if he so chose, participate fully in the Hearing. Both his Reply and the series of e-mails, expanding on his Reply, were marked as Exhibits and fully considered by the Hearing Panel in coming to its decision.

Rule 13.5(1) of the MFDA Rules of Procedure provides that:

“13.5 Where a Respondent Fails to Attend a Disciplinary Hearing

- (1) Where a Respondent, having been served with a Notice of Hearing, fails to attend the hearing of the proceeding on its merits, the Hearing Panel may proceed in accordance with Rule 7.3.”

Rule 7.3(1)(a) provides that:

“7.3 Failure to Attend Hearing

- (1) Where a Respondent fails to attend the hearing on the date and at the time and location specified in the Notice of Hearing, the Hearing Panel may:
- (a) proceed with the hearing without further notice to and in the absence of the Respondent;”

In our opinion, the Respondent was properly served with the Notice of Hearing, was aware of the date, time and location of the Hearing on the merits and chose not to attend in person but to rely on the written submissions contained in his Reply and subsequent e-mails.

3. MANNER OF PROCEEDING

Although Rule 7.3(1)(b) of the Rules of Procedure does authorize the Hearing Panel to accept the facts alleged and conclusions drawn by the Corporation in the Notice of Hearing as proven where the Respondent fails to

attend the Hearing on the date, time and location specified in the Notice of Hearing, Enforcement Counsel sought to prove the Allegations by means of admissible evidence. We agreed with that approach.

4. PRESENTATION OF EVIDENCE

In addition to the Reply and the exchange of e-mails between the Respondent and Enforcement Counsel, the evidence before the Hearing Panel, with respect to this matter, consisted of an Affidavit of Lorraine Bate Boerop, an Investigator with the MFDA, sworn October 23, 2007, along with 17 Exhibits. This was marked as Exhibit 5.

Enforcement Counsel advised the Hearing Panel that Exhibit 5 contained sensitive client information, including the names of the clients. He requested that a redacted version of this Affidavit, removing personal information relating to the former clients of the Respondent, be marked as the actual Exhibit. He confirmed that a full and unredacted version had been provided to the Respondent. Enforcement Counsel further advised that Exhibit E to this Affidavit consisted of various documents executed by clients, including Subscription Agreements, Letters of Direction, cheques, transfer forms, as well as Account Statements. He requested that Exhibit 5E be marked as “Confidential” pursuant to the provisions of Rules 1.8(2) and (5) of the MFDA Rules of Procedure. These Rules provide as follows:

“1.8 Hearings Open to the Public

- (2) A Panel may order that all or part of a hearing be heard in the absence of the public where the Panel is of the opinion that intimate financial or personal matters or other matters may be disclosed at the hearing which are of such a nature, having regard to the circumstances, that the desirability of avoiding disclosure thereof in the interests of any person affected or in the public interest outweighs the desirability of adhering to the principle that hearings be open to the public.

- (5) Exhibits, documents and transcripts relating to that part of a hearing that is held in the absence of the public shall be marked “Confidential” and shall be kept separate from the public record, and access to this material shall only be by order of the Panel.”

After considering the submissions of counsel and reviewing the material, we agreed to mark as Exhibit 5 a redacted version of the Affidavit and mark Exhibit 5E as “Confidential”. We did this to protect client confidentiality.

5. THE EVIDENCE

Rule 1.6(1) of the MFDA Rules of Procedure provides, in part, that:

- “(1) a Panel may admit as evidence any testimony, document or other thing, including hearsay, which it considers to be relevant to the matters before it and is not bound by the technical or legal rules of evidence.”

Accordingly, we ruled that Exhibits 5, 6 and 7 formed admissible evidence before us. This evidence established the following:

The Respondent was registered in Ontario as a mutual fund salesperson with FundEX Investments Inc. (“FundEX”), from November 26, 1999, to May 24, 2006, when he was terminated for cause as a result of the conduct which was the subject matter of this proceeding. At the time of the Hearing, the Respondent was not registered in the securities industry in any capacity.

Between October 2002 and December 2003, the Respondent recommended and facilitated investments in Capital Associate Management, SVG Ltd. (“CAM”) by 59 clients of FundEX. In 67 separate transactions, detailed in Exhibit 5, the 59 clients invested a total of \$1,722,622.35 Cdn. and \$85,266.34 U.S. in CAM.

CAM, in materials distributed to prospective investors, claimed to be “a St. Vincent Grenadines based investment management and trading company” whose objective was to “provide access to specialized expertise in the management of currency and arbitrage trading, acquisition/merger, IPO, commodities trading through an actively managed portfolio.” In these materials, CAM claimed that it had “assembled a world class advisory board with broad experience and knowledge.”

CAM purported to offer 4 different managed investment accounts, 3 of which made monthly income payments. The Respondent was provided with individualized monthly statements for each client account, purportedly showing the status of each such account. The Respondent, in turn, forwarded these statements to the clients.

In or about October 2004, CAM stopped making monthly income payments to investors. The Respondent then began making monthly payments, from his own personal account, to certain of his clients in place of CAM. In total, he paid \$50,707.92 to 11 of his clients between October 2004 and March of 2006. In November and December of 2004, the Respondent paid, out of his own funds, a total of \$12,931.25 back to CAM which, he was advised, would assist CAM in making monthly payments to the clients. The Respondent believed that CAM was experiencing temporary financial difficulties and would reimburse him for any out of pocket payments he made to the clients once these financial problems subsided. When FundEX became aware of the Respondent’s outside business activities in March of 2006, they immediately suspended his trading ability.

All of the Respondent’s meetings with his clients, concerning CAM related matters, took place at the FundEX branch office. All of the CAM related paperwork was completed on the FundEX premises.

There is no evidence that the Respondent received any compensation from CAM, although he did admit that he believed that, once the off-shore projects “got going”, he would “potentially see compensation coming down and they would start a compensation scale . . . in the ½% range” in exchange for him referring FundEX clients to CAM.

Between October 2002 and March 2003, the Respondent invested approximately \$34,500.00 of his own funds in CAM. In February of 2003, he assisted his wife, a FundEX client, in investing in excess of \$25,500.00 in CAM.

The Respondent knowingly facilitated investments in CAM using one or more of the following methods:

- (a) providing funds directly to CAM;
- (b) redeeming mutual funds on behalf of clients and sending the proceeds directly to CAM;
- (c) redeeming mutual funds on behalf of clients and directing the fund companies to send the proceeds directly to CAM;
- (d) exchanging cash in self-directed RSP accounts of clients for shares of a private British Columbia corporation, with the cash then purportedly being transferred by that corporation to CAM to be invested off-shore or;
- (e) redeeming mutual funds in an RSP account of a client at an MFDA member firm, transferring the contents of the account to a registered account at an IDA member firm and then purchasing shares of a private corporation with the cash received by that corporation purportedly being transferred to CAM to be invested off-shore.

FundEX conducted an annual audit of the Respondent’s office in March 2003, March 2004, April 2005 and March 2006. In none of those audits did the Respondent advise FundEX of his outside business activity. In fact, on several occasions, he specifically indicated to the contrary.

For example, during the 2004 audit review, he confirmed the following information:

- (a) he was not involved in any referral arrangements;
- (b) he was not involved in any non-permissible activities, such as direct trading, discretionary trading, trading in securities or other exempt products;
- (c) he was not offering advice on any securities for which he was not licensed.

The 2004 audit report sent to the Respondent contained the following statement:

“FundEX Associates are prohibited from trading directly with a fund company or intermediary. All transactions must be processed through FundEX to ensure compliance with all securities acts, policies and regulations. Any transactions placed directly, circumventing FundEX as the Associate’s dealer, will place the Associate’s registration with FundEX in jeopardy.”

The 2005 audit report also contained the above statement. It contained a further statement, namely that any transactions which could not be placed on the FundEX Back Office Trading System, but which were sent directly to a fund company for processing, must be reported to the Regional Branch Manager via e-mail. It stated that the purpose of this was to enable FundEX to perform its supervisory responsibilities.

The 2005 audit report also stated that, during the review, the Respondent confirmed:

- (a) that he would only enter into referral arrangements approved by FundEX;
- (b) that he would not be involved in any non-permissible activities such as direct trading, discretionary trading, trading in securities or other exempt products; and
- (c) he would not offer advice on any securities for which he was not licensed.

The 2006 audit report contained the outline of a lengthy questionnaire and indicated answers given by the Respondent to certain questions. When asked what he would do if there was a product that he wanted to sell, which was not on the approved list, he replied that he would have to go to FundEX to request approval. He said that he would not sell a product which was not on the approved list. When asked, "What outside business activities are you involved in?" he replied "None."

The FundEX Compliance Manual also made it clear that an Approved Person, such as the Respondent, could not pay compensation to a client to resolve a complaint and that all such monetary resolutions had to be referred to and handled by the head office of FundEX. On October 10, 2005, the Respondent acknowledged in writing that he had read and understood the information contained in the Compliance Manual.

In a statement provided to the MFDA investigator, on April 24, 2006, the Respondent admitted that he knew that his CAM related activities were prohibited by FundEX and outside of the scope of his registration as a mutual fund salesperson and, for that reason, he actively concealed his CAM related activities from FundEX from October of 2002 until April of 2006.

On March 30, 2006, FundEX received a complaint from one of its clients regarding investments which she had made in CAM on the advice of the Respondent. On April 10, 2006, FundEX advised the Respondent that it had received a complaint involving CAM and requested a written response on or before April 17, 2006, concerning his working relationship with the complainant, including an explanation as to why he recommended CAM, evidence that he had disclosed to FundEX all of his outside business activities, details of any compensation which he had paid to clients respecting any investment losses along with a complete copy of the complainant's file.

On April 14, 2006, the Respondent replied, in writing, to FundEX's request for information and, for the first time, disclosed to FundEX his outside business activity involving CAM. He stated, *inter alia*, "I did not bring this investment to FundEX's attention, as I was hopeful that this would be solved before now. I did not receive any commission or remuneration for referring to (CAM). I was hopeful the investment with (CAM) would prove very good and help get back client's losses they incurred in mutual funds."

By letter, dated April 24, 2006, the Respondent was notified by FundEX that his mutual fund trading activity had been suspended. On April 25, 2006, FundEX notified the Respondent that his trading activity would remain suspended until May 24, 2006, at which time his registration as an Approved Person with FundEX would be terminated.

6. REPLY

The position of the Respondent with respect to the Allegations is set out in a lengthy Reply, as well as in an exchange of e-mails with Enforcement Counsel.

In these documents, the Respondent candidly admits that Allegations 1 and 2 in the Notice of Hearing have been established. He admits that he engaged in securities related business outside of the accounts and facilities of the Member and that he deliberately concealed this business activity from the Member.

The Respondent stated that he was attempting to do what he thought was best for his clients. He said that his clients were losing a considerable amount of money in their mutual fund portfolios with what the Respondent described as "the crash in markets around the 2001 - 2003 periods." He said that, by February 2001, he was receiving numerous complaints from clients because of the significant drop in their portfolio values.

On February 27, 2001, he wrote a lengthy letter to one of the fund managers expressing his concerns. In that letter, he stated that the problem was not with the markets but with the management of the funds in question. He provided a detailed analysis of his concerns.

The Respondent stated that, in April of 2001, he was told by the fund company that his assessment was incorrect and that he was best to trust the investment decisions of its experts, who were doing a good job.

The Respondent continued to believe that the losses of his clients were due to speculative purchases by the fund managers. He indicated that he could not bring himself to tell customers that they were invested in good quality funds with good management when he did not believe that to be true. He said that, during the drop in the market, his clients lost \$3 million to \$4 million and over 20% of his base business went elsewhere.

He stated that, in 2002, he was introduced to CAM by one of his clients. He began personally investing in CAM in October of 2002. He then began to recommend and facilitate the investment in CAM by his clients. This began in October of 2002 and continued through to December 2003, by which time a total of 59 clients had made 67 separate investments totalling approximately \$1.8 million. He stated that he also recommended and facilitated investments in CAM by his wife, his children and his in-laws. He stated that only when his clients complained to him about the drop in their portfolio values did he advise them of the existence of CAM. He stated that if a client did not complain about the value of his portfolio, he was not advised of the existence of CAM.

He said that by 2004, he had found a number of mutual funds which he felt were of good quality and, consequently, no longer recommended that his clients invest in CAM.

He stated that he never put his clients into the CAM investments for the purpose of making a personal income. He said he was never compensated for assisting in making these investments, although he did admit that he anticipated being compensated once the CAM projects got up and going. He candidly admitted that he knew that what he was doing was outside of his mutual fund licensing.

When CAM defaulted on making monthly payments to certain of his clients, beginning in October of 2004, the Respondent made these monthly payments himself. He admitted that he did not disclose this to FundEX. He said that he was hopeful that CAM would solve its problems and be able to repay his clients. If not, it had been his intention to make monthly payments until all of the clients had received their money back. In March 2006, one of his clients complained to FundEX and that led to his dismissal.

7. APPLICABLE RULES

Allegation #1, in the Notice of Hearing, alleges a breach of MFDA Rule 1.1.1. This Rule states:

“1. RULE NO. 1 – BUSINESS STRUCTURES AND QUALIFICATIONS

1.1 Business Structures

1.1.1. **Members.** No Member or Approved Person (as defined in By-law 1.1) 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 (except as expressly provided in the Rules) and in accordance with the By-laws and Rules, other than:
 - (i) such business as relates solely to trading in deposit instruments conducted by any Approved Person not on account of the Member, and

- (ii) such business conducted by an Approved Person as an employee of a bank and in accordance with the *Bank Act (Canada)* and the regulations thereunder and applicable securities legislation.
- (b) all revenues, fees or consideration in any form relating to any business engaged in by the Member is paid or credited directly to the Member and is recorded on the books of the Member;
- (c) the relationship between the Member and any person conducting securities related business on account of the Member is that of:
 - (i) an employer and employee, in compliance with Rule 1.1.4,
 - (ii) a principal and agent, in compliance with Rule 1.1.5, or
 - (iii) an introducing dealer and carrying dealer, in compliance with Rule 1.1.6;
- (d) the business or trade or style name under which such securities related business is conducted is in accordance with Rule 1.1.7.”

By-law 1.1 of MFDA By-law No. 1 defines an Approved Person, as follows:

“**Approved Person**” means, in respect of a Member, an individual who is a partner, director, officer, compliance officer, branch manager, or alternate branch manager, employee or agent of the Member who conducts or participates in the dealer business of the Member and who (i) is registered, licensed or approved in the appropriate category, where required by applicable securities legislation, by the securities commission having jurisdiction, and (ii) is designated and qualified as such in accordance with the Rules, or (iii) is otherwise subject to the jurisdiction of the Corporation;”

By-law 1.1. of MFDA By-law No. 1 defines securities related business, as follows:

“1. DEFINITIONS

In this By-law and in the Rules and Policies, unless the context otherwise specifies or requires:

“**securities related business**” means any business or activity (whether or not carried on for gain) engaged in, directly or indirectly, which constitutes trading or advising in securities for the purposes of applicable securities legislation in any jurisdiction in Canada, including for greater certainty, securities sold pursuant to exemptions under applicable securities legislation;”

Allegation #2, in the Notice of Hearing, alleges a breach of MFDA Rule 2.1.1. This Rule states:

“2.1.1 **Standard of Conduct.** Each Member and each Approved Person of a Member shall:

- (a) deal fairly, honestly and in good faith with its clients;
- (b) observe high standards of ethics and conduct in the transaction of business;
- (c) not engage in any business conduct or practice which is unbecoming or detrimental to the public interest; and
- (d) be of such character and business repute and have such experience and training as is consistent with the standards described in this Rule 2.1.1, or as may be prescribed by the Corporation.”

8. FINDINGS AND THE LAW

Enforcement Counsel presented the Hearing Panel with both submissions and supplementary submissions, as well as two very extensive casebooks, for which we are indebted.

Allegation #1

Section 1(1) of the *Ontario Securities Act*, R.S.O. 1990 c.S.5, defines a “security” as, among other things:

“(b) any document, constituting evidence of title to or interest in the capital, assets, property, profits, earnings or royalties of any person or company, . . . [and]

(n) any investment contract,”

“Trading” is defined in section 1.1. of the *Securities Act* as:

“(c) any receipt by a registrant of an order to buy or sell a security . . . [and] . . .

(e) any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of any of the foregoing;”

MFDA Rule 1.1.1(a) prohibits an Approved Person from engaging in securities related business that is not carried on for the account of the Member, through the facilities of the Member, and in accordance with MFDA By-laws and Rules.

The Respondent’s conduct in recommending CAM to clients of FundEX and facilitating the investments therein, constituted “securities related business” for the purposes of this proceeding.

We agree with the submission of Enforcement Counsel that MFDA Rule 1.1.1(a) is fundamental to the regulatory mandate of the MFDA to enhance investor protection and strengthen public confidence in the Canadian mutual fund industry. This Rule creates a regime where an Approved Person is only

permitted to sell investment products that have been first approved for sale by the Member with which the Approved Person is registered and which are sold through the facilities of that Member.

Rule 1.1.1(a) is designed to protect both the Member and its clients. When a transaction is done off the books, the Member loses its ability to supervise the transaction and to take responsibility for the suitability of the transaction for the investor.

Previous MFDA Hearing Panels have held that an Approved Person who facilitates investments by clients of the Member in products or companies unknown to and unapproved by the Member, or who acts as an intermediary between clients and the perpetrators of an investment scheme, is engaged in securities related business outside of the Member and has, therefore, breached Rule 1.1.1.

In the Matter of Joseph Van Der Velden and Andrew Stokman, MFDA Hearing Panel, Reasons for Decision dated October 14, 2005, pp. 2-3

In the Matter of Ernest Ming Chung Lo, MFDA Hearing Panel, Reasons for Decision dated April 3, 2006, p. 12

The evidence clearly established that the Respondent engaged in securities related business outside of the accounts and facilities of his Member, FundEX, by engaging in the following activities:

- (a) the Respondent recommended CAM to 59 FundEX clients and facilitated the transfer to CAM of over \$1.8 million in clients' funds;
- (b) CAM, to the knowledge of the Respondent, was not known to FundEX;
- (c) CAM securities, including investment accounts and/or investment contracts, were not, to the knowledge of the Respondent, approved for sale by FundEX;

- (d) none of the clients' funds received by CAM were, to the knowledge of the Respondent, in any way recorded in the books, records or accounts of FundEX; and
- (e) the Respondent's securities related business in respect of CAM was knowingly not conducted in accordance with MFDA By-laws and Rules.

Accordingly, we unanimously find that the conduct of the Respondent breached MFDA Rule 1.1.1 and that Allegation #1 has been established.

Allegation #2

The evidence before the Hearing Panel clearly established, and the Respondent candidly admitted, that he knew that his outside business activities in respect of CAM were prohibited by FundEX and outside of the scope of his registration as a mutual fund salesperson. For those reasons, over a lengthy period of time, he actively and deliberately concealed these activities from FundEX.

A number of annual audits were conducted of the Respondent's office during the period of time when he was improperly engaging in securities related business outside the accounts and facilities of FundEX. Each of those audits reminded the Respondent of his duties and obligations. In each of those audits, he knowingly misled FundEX by, at no time, revealing his CAM related activities. The period of active concealment lasted approximately 3 ½ years. The Respondent intentionally circumvented FundEX's internal controls by providing false answers to the FundEX compliance staff during annual compliance audits.

On October 10, 2005, the Respondent signed an Acknowledgement that he had read and understood the FundEX Compliance Policies and Procedures Manual. A section of this manual specifically states that an Approved Person cannot pay compensation to a client to resolve a complaint. The Respondent signed this Acknowledgement during a period of time in which he was making

monthly payments to certain clients after CAM had ceased making payments to them.

MFDA Rule 2.1.1 sets out the standard of conduct expected of Approved Persons. The Rule is designed to protect the public interest by requiring Approved Persons to adhere to a high standard of ethical conduct. The Rule articulates the most fundamental obligations of all registrants in the securities industry.

It is clear that, by actively concealing from FundEX the business activity he was engaging in outside the accounts and facilities of FundEX, the Respondent failed to observe high standards of ethics and conduct in the transaction of business and also failed to refrain from engaging in business conduct or practice which was unbecoming or detrimental to the public interest. We have no hesitation in finding that Allegation #2 has been established.

9. PENTALLY REQUESTED

In his supplementary submissions, Enforcement Counsel sought the following sanctions:

- (a) pursuant to section 24.1.1(e) of MFDA By-law No. 1, a permanent prohibition on the authority of the Respondent to conduct securities related business while in the employ of, or associated with, any MFDA Member;
- (b) pursuant to section 24.1.1(b) of MFDA By-law No. 1, a fine in the range of \$225,000.00 to \$350,000.00 for recommending and facilitating the investment of client funds in the total amount of approximately \$1.8 million in a security unknown to and unapproved by the Member;

- (c) pursuant to section 24.2(d) of MFDA By-law No. 1, costs attributable to conducting the investigation and prosecution of this matter in the amount of \$7,500.00.

10. FACTORS TO BE CONSIDERED

The primary goal of securities regulation is the protection of the investor.

In the Matter of Robert Roy Parkinson, MFDA Hearing Panel, Reasons for Decision dated April 29, 2005, pp. 20-21

Sanctions should be preventative, protective and prospective in nature.

In the Matter of Arnold Tonnies, MFDA Hearing Panel, Reasons for Decision dated June 27, 2005, p. 22

In the Matter of Stephan Headley, MFDA Hearing Panel, Reasons for Decision dated February 21, 2006, p. 24

In exercising its discretion to impose a penalty, the Hearing Panel should take into account the following considerations:

- (a) the protection of the investing public;
- (b) the integrity of the securities markets;
- (c) specific and general deterrence;
- (d) the protection of the MFDA's membership; and
- (e) the protection of the integrity of the MFDA's enforcement processes.

Parkinson, *supra*, at page 21

Tonnies, *supra*, at page 22

Headley, *supra*, at page 24

Previous Hearing Panels have set out a number of additional factors which should be considered when determining an appropriate penalty. These include:

- (a) The seriousness of the allegations proved against the respondent;

- (b) The respondent's experience in the capital markets;
- (c) The level of the respondent's activity in the capital markets;
- (d) The harm suffered by investors as a result of the respondent's activities;
- (e) The benefits received by the respondent as a result of the improper activity;
- (f) The risk to investors and the capital markets in the jurisdiction, were the respondent to continue to operate in capital markets in the jurisdiction;
- (g) The damage caused to the integrity of the capital markets in the jurisdiction by the respondent's improper activities;
- (h) The need to deter not only those involved in the case being considered, but also any others who participate in the capital markets, from engaging in similar improper activity;
- (i) The need to alert others to the consequences of inappropriate activities to those who are permitted to participate in capital markets; and
- (j) Previous decisions made in similar circumstances.

Parkinson, supra, at page 22

Tonnies, supra, at page 23

Headley, supra, at pages 25 and 26

We considered the following aggravating factors:

1. The actions of the Respondent in engaging in securities related business outside the accounts and facilities of FundEX were planned and deliberate.
2. The actions of the Respondent in concealing from FundEX the CAM related business activity were planned and deliberate.
3. The Respondent's CAM related activities extended over a lengthy period of time, namely from October of 2002 to December of 2003.

4. The improper activities of the Respondent were not isolated. Rather, they were numerous, consisting of recommending and facilitating the transfer of approximately \$1.8 million on behalf of 59 FundEX clients into 67 investments of a security unknown to and unapproved by FundEX.
5. Virtually none of the money invested by the clients through the Respondent has been returned to or recovered by the clients.
6. The Respondent has acknowledged that when he was engaging in this activity, he was aware that FundEX policies prohibited him from promoting, recommending or referring investment products or companies that were not approved by FundEX. He deliberately breached the internal policies and procedures of FundEX.
7. Throughout this period of time, the Respondent was aware that his registration status in Ontario did not permit him to sell, promote or recommend CAM or refer FundEX clients to CAM. He deliberately acted outside the scope of his registration.
8. The Respondent entered into private settlement arrangements with a number of clients, who had invested in CAM, despite the fact that he knew or ought to have known that he was prohibited from doing so.
9. For a period of approximately 3 ½ years, from October of 2002 to April of 2006, the Respondent actively concealed his misconduct from FundEX by intentionally providing false answers to compliance staff during annual compliance audits.
10. Although the Respondent did not receive any compensation as a result of his misconduct, he believed that he would receive such compensation in the future.

Against the above aggravating factors, we weighed the following mitigating factors:

1. The Respondent co-operated with the MFDA in the course of its investigation.

2. The Respondent co-operated with his Member once it discovered his outside business activities.
3. The Respondent has no discipline history.
4. The Respondent invested his own money and that of his spouse and family members in CAM in the mistaken belief that CAM was a sound investment.
5. The Respondent made partial restitution to clients by making monthly payments from his own personal funds to certain clients when CAM stopped doing so. He also reinvested certain of his own funds back into CAM in the belief that this would assist CAM in making monthly payments.
6. The Respondent has suffered significant personal monetary losses as a result of his actions.
7. The Respondent has demonstrated regret and remorse.
8. The Respondent candidly admitted his wrongdoing to the Hearing Panel.
9. The Respondent has endured significant personal suffering as a result of his actions.

11. PENALTIES IMPOSED

(a) Permanent Prohibition

In our view, it is incumbent upon the Hearing Panel to communicate to the Respondent, to the public and to the mutual fund industry as a whole, that serious consequences will befall those who are engaged in activities similar to those of the Respondent. In our view, there should be a permanent prohibition on the ability of the Respondent to conduct securities related business in any capacity while in the employ of, or associated with, any MFDA Member.

(b) Fine

In our view, the fine which we impose in this matter should reflect a careful weighing of both the aggravating and mitigating factors outlined above. It also should be of a sufficient amount to deter others from engaging in similar

misconduct, improve overall compliance by mutual fund industry participants and foster public confidence in the securities industry.

After carefully reviewing the numerous authorities cited to us by Enforcement Counsel, and considering the factors outlined above, we are unanimously of the view that a fine in the amount of \$350,000.00 should be imposed on the Respondent with respect to Allegations #1 and #2.

(c) Costs

Section 24.2 of By-Law No. 1 provides that:

“A Hearing Panel may in any case in its discretion require that the . . . Approved Person pay the whole or part of the costs of the proceedings before the Hearing Panel and any investigations relating thereto.”

We believe that the imposition of costs in the circumstances of this case is appropriate and order same to be fixed in the amount of \$7,500.00.

Dated at Toronto, this 14th day of November 2007.

“Thomas J. Lockwood”

Thomas J. Lockwood, Q.C.
Chair

“Sandy Grant”

Sandy Grant
Panel Member

“Richard Williams”

Richard Williams
Panel Member