



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

**IN THE MATTER OF A SETTLEMENT HEARING
PURSUANT TO SECTION 24.4 OF BY-LAW NO. 1 OF
THE MUTUAL FUND DEALERS ASSOCIATION OF CANADA**

Re: Dino DeRosa

Heard: October 4, 2018 in Toronto, Ontario
Decision and Reasons: November 13, 2018

DECISION AND REASONS

Hearing Panel of the Central Regional Council:

Martin L. Friedland, CC, QC	Chair
Guenther W.K. Kleberg	Industry Representative
Joseph Yassi	Industry Representative

Appearances:

Shelly Feld)	Enforcement Counsel for the Mutual Fund
)	Dealers Association of Canada
)	
)	
Dino DeRosa)	Respondent, in person
)	
)	

Background

1. This is a Settlement Hearing under Section 24.4 of By-law No. 1 of the Mutual Fund Dealers Association of Canada (the “MFDA”). The Hearing was held on October 4, 2018. The full Settlement Agreement, dated October 2, 2018, entered into between Staff of the MFDA and Dino DeRosa (the “Respondent”) is available on the MFDA website. Mr. De Rosa was not represented by counsel and appeared in person.

2. The Panel reserved its decision on the proposed Settlement Agreement at the conclusion of the October 4th hearing. This is our decision and the reasons for the decision.

3. A Notice of Hearing was issued by the MFDA on November 20, 2017. A first appearance took place on January 22, 2018 at which time a five-day hearing was scheduled for October 1 to 5, 2018. A Settlement was reached on October 2, 2018 and the present Settlement Hearing was scheduled for October 4, 2018.

4. This is the last MFDA case in a series of cases involving extremely serious misconduct by a MFDA Member, W.H. Stuart Mutuals Ltd. (“W.H. Stuart Ltd.” or “W.H. Stuart”), its senior officers, Dianne Stuart and Howard Stuart. Dianne and Howard Stuart were the founders and co-owners of W.H. Stuart Ltd. (See *Re W.H. Stuart Mutuals Ltd. et al.* 2016 LNCMFDA 73 and 201532 (penalty); *Re Rumball* 201521; *Re McBurney* 2015 LNCMFDA 153; and a hearing involving the Stuarts’ son, J.H.M. Stuart, for failing to cooperate *Re Stuart* 2015 LNCMFDA 152.)

5. An earlier Hearing Panel in 2016 relating to W.H. Stuart Ltd., Dianne Stuart and Howard Stuart stated (2016 LNCMFDA 73 at paragraph 64):

“The evidence revealed that Dianne Stuart and W.H. Stuart engaged in a massive scheme of dishonesty over a period of approximately 10 years or more. It was perpetuated in a variety of ways, including but not limited to the bogus Note Program. At its core was the falsification and concealment of records, and a pattern of deceit...The efforts taken to disguise this scheme of dishonesty from the MFDA and other regulators, auditors, investors, and others were truly staggering in their breadth, duration and level of sophistication.”

6. These persons and other Approved Persons of W.H. Stuart Ltd. were soliciting and accepting millions of dollars from clients of W.H. Stuart Ltd. for investment in promissory notes that typically promised clients a 7% annual rate of return (the “Note Program”). The promissory notes were issued by W.H. Stuart Ltd. and related companies and were not carried on for the account of the Member or recorded on the books and records of the Member. Liabilities associated with the Note Program were not reported on financial reports that were signed and submitted to the MFDA on a monthly basis.

7. In addition to operating the Note Program for several years, Dianne Stuart also engaged in other activities, such as processing unauthorized transactions in client accounts and misappropriated the proceeds of such transactions.

8. W. H. Stuart Ltd. became a Member of the MFDA in March 2003. Its membership was terminated on May 16, 2013, and on May 17, 2013, the MFDA and the Ontario Securities Commission approved the bulk transfer of client accounts and the registrations of Approved Persons of W.H. Stuart Ltd. to Keybase Financial Group Inc. (“Keybase”), a Member of the MFDA.

9. After a liability and then a penalty hearing in 2016, Dianne Stuart and her husband, neither of whom participated in the hearings, were permanently prohibited from conducting securities related business in any capacity for a Member of the MFDA and substantial fines and costs were awarded. Dianne Stuart was fined \$7 million and Howard Stuart was fined \$1 million. Neither fine has yet been paid in whole or in part.

10. The head office of W.H. Stuart Ltd. was in Markham Ontario. There were, according to the Respondent, at various times, perhaps four or five hundred Approved Persons working for the Member across Canada. There were no branch offices.

The Respondent

11. Since May 18, 2000, Mr. DeRosa, the Respondent, was registered in Ontario as a mutual fund salesperson/dealing representative. From March 26, 2003 to May 17, 2013, the Respondent was an Approved Person of W.H. Stuart Ltd. From November 19, 2002 to September 28, 2009, the Respondent was also registered as a trading officer of W.H. Stuart Ltd. For various periods, the Respondent was registered in almost all provinces in Canada. From December 29, 2005 to May 16, 2013 when W. H. Stuart Ltd.'s membership in the MFDA was terminated, the Respondent was registered as the Chief Compliance Officer ("CCO") of the Member.

12. At all material times the Respondent operated out of the Member's head office in Markham, Ontario. Since the Respondent's registration was transferred to Keybase, the Respondent has serviced client accounts as an Approved Person of Keybase, but Keybase has not permitted the Respondent to work in a compliance or supervisory role.

13. There have been relatively few MFDA cases disciplining an MFDA Chief Compliance Officer. Counsel for the MFDA told us that the present hearing is "one of the first, if not the first, MFDA case of a Chief Compliance Officer who was not part of the directing mind of the Member."

Contraventions

14. The Respondent admits in paragraph 85 of the Settlement Agreement that between 2006 and April 2013, he, in his capacity as CCO of W.H. Stuart Ltd, "failed to identify regulatory concerns and take adequate supervisory action including completing reasonable supervisory investigations in response to red flags that indicated or could have revealed, that W.H. Stuart's principals and Approved Persons were soliciting off-book investments in promissory notes issued by W.H. Stuart, its principals and related entities, contrary to MFDA Rules 1.1.1, 2.5.3 and 2.1.1."

15. Paragraph 86 of the Settlement Agreement states that the Respondent "admits that between February 2011 and April 2013, the Respondent, in his capacity as CCO of W.H. Stuart, received complaints concerning the accounts of clients SI, DR and MD but failed to ensure that:

- a) the complaints were reported to the MFDA on the Member Event Tracking System ('METS');
- b) reasonable supervisory investigations into the subject matter of the complaints were conducted;
- c) the complaints were dealt with promptly and fairly; and
- d) records were maintained of the investigation and proposed resolution of the complaints;

contrary to MFDA Rules 1.2.2 (now 1.4), 2.1.1, 2.14, 2.5.3 and MFDA Policy Nos. 3 and 6.”

16. Paragraph 87 of the Settlement Agreement states: “The Respondent admits that:

between December 2011 and April 2013, the Respondent signed the certificate of partners or directors on behalf of W.H. Stuart that accompanied the submission of the Member’s monthly and annual financial reports to the MFDA when he knew or ought to have known that the financial reports contained inaccurate financial information, contrary to MFDA Rules 3.5.1 and 1.1.2 and MFDA Rule 2.1.1.”

17. The details of the facts concerning these admissions are contained in paragraphs 22 to 68 of the Settlement Agreement and it is unnecessary to set them out in detail here. In the following three paragraphs are examples of some of the many ‘red flags’ which should have alerted the Respondent that something was going on outside the books of the Member and the purview of the MFDA.

18. SI, a longstanding client of W.H. Stuart complained to a mutual fund company about various activities in her account. A copy of this letter was sent to the Respondent. In that letter, she noted that a person working at W.H. Stuart had recommended that she sell a mutual fund investment and purchase a “term investment at a 7% annual rate.” The Respondent did not follow up on this complaint.

19. The person selling the Investment Note was DH, an unregistered individual who regularly attended and worked at the W.H. Stuart head office. Commencing in the spring of 2009, DH began

working at the office of W.H. Stuart on a regular basis, soliciting investments in the Note Program from clients. He attended at the head office multiple times each week for several hours at a time. He occupied office or boardroom space in the office on most occasions and was granted access to client files and telephoned many of W.H. Stuart clients to encourage them to invest in the Note Program. In his emails to clients (using a W.H. Stuart e-mail address) he used the title “Manager of Sales and Marketing, Stuart & Associates.” The Respondent obviously should have questioned what DH was doing at the W.H. Stuart office and the appropriateness of the business activities that DH was engaged in, considering the fact that DH was an unregistered individual who was regularly accessing the office facilities and client files of W.H. Stuart.

20. A third “red flag” was that one of the Member’s Approved Persons, Gerald Rumball (“Rumball”) specifically sent an e-mail to the Respondent in July, 2005 “requesting guidance and direction from the Respondent concerning the paper work required to transfer client money from the ‘7% program’ into mutual funds. The Respondent did not question Rumball about the “7% program investment.”

Importance of a Chief Compliance Officer

21. The Respondent admits in paragraph 21 of the Settlement Agreement that: “As CCO of W.H. Stuart, the Respondent was responsible for monitoring adherence by the Member and any person conducting business on account of the Member to the By-laws, rules and Policies of the MFDA and to applicable securities legislation.”

22. There are many rules, regulations and policy statements with respect to the role and various obligations of compliance officers, such as informing the Ultimate Designated Person and the Board of suspected wrongdoing. The Panel has examined those rules. They do not, however, deal as clearly as one would like with the situation we see here, where there is an obligation to report suspected wrongdoing to the very persons who have been the cause of the wrongdoing. Rule 2.5.3(b), for example, states that the chief compliance officer must report suspected non-compliance to the Ultimate Designated Person and to the board of directors. A similar approach can be seen in Notice MR-0037 and MR-0057 (“The Chief Compliance Officer must report the

results from its monitoring to management and the board of directors...”) and in National Instrument 31-103, s. 5.2. We suggest that the MFDA re-examine the various rules and policy statements and consider adding a rule or policy guidance to deal specifically with the situation presented by the present case.

23. The responsibilities of a CCO is well stated by an IIROC panel in *Re Northern Securities* (2012 LNIIOC 63) at paragraph 102, which dealt with a situation where the CCO reported to the person who was the cause of the problems:

“It is this Panel’s opinion that the wording of the rules referred to does not fully describe the breadth or depth of the responsibilities which a CCO has for ensuring that the Dealer Member and all its employees comply with IIROC rules, securities legislation and good business practices, and which are expected, or ought to be expected, according to acceptable industry standards. In this Panel’s opinion, acceptable industry standards for a CCO reasonably require, or ought to require, that they diligently and proactively monitor and update practices and procedures to guard against any questionable practices, that they question business practices until they receive an explanation which satisfies them that nothing untoward is happening, and that they generally act as the moral compass to ensure compliance with the rules, laws and good business practices. They must be prepared to diligently challenge... practices that may be questionable, even if those practices or explanations come from their superiors in the firm.”

24. Supervision must not be based on trust alone. As the Ontario Securities Commission stated in *Re Rowan* (2008), 31 OSCB 1615: “It is insufficient for a CCO to accept information provided by a registered representative at face value...industry standards dictate that trust in a registered representative should always be accompanied by independent check of the information provided...”

25. If the Respondent had followed up the many red flags that were clearly within his view, the wrongful conduct by others might have come to light earlier.

26. The Respondent’s conduct in not questioning the many clear signs of wrongdoing in the present case is egregious. Staff submitted that the Respondent, in his capacity as CCO, had both supervisory and compliance responsibilities and failed to fulfill these obligatory functions. The Panel accepts these submissions.

Terms of Settlement

27. The Respondent agreed in paragraph 88 to the following terms of settlement:
- a) from the date of an order accepting this Settlement Agreement, the Respondent shall be permanently prohibited from conducting securities related business in any capacity as an Approved Person of, or in association with, any Member of the MFDA, pursuant to s. 24.1.1(e) of MFDA By-law No. 1;
 - b) the Respondent shall pay a fine in the amount of \$10,000 which shall be payable on the date of an order accepting this Settlement Agreement, pursuant to s. 24.1.1(b) of MFDA By-law No. 1;
 - c) the Respondent shall pay costs in the amount of \$5,000 which shall be payable on the date of an order accepting this Settlement Agreement, pursuant to s. 24.2 of MFDA By-law No. 1; and
 - d) the Respondent will attend in person on the date when a Settlement Hearing is scheduled to take place.
28. There is no question that the egregious conduct by the Respondent requires that he be “permanently prohibited from conducting securities related business” as stated in paragraph 27(a) above.
29. The payment of costs of \$5,000 seems reasonable and will partially cover the costs incurred by the MFDA.
30. The only question in this hearing that the Panel had difficulty with was the relatively low financial penalty for such serious misconduct by the Respondent in his role as a Chief Compliance Officer.

Importance of Respecting Settlements

31. The case law makes it clear that Settlement Agreements should be encouraged and respected.

32. Settlements can be important and useful in achieving outcomes which further the goals of the securities regulatory context. The British Columbia Court of Appeal stated with respect to a settlement by the B.C. Securities Commission (*B.C. Securities Commission v. Seifert* [2007] B.C.J. No. 2186, para. 49 (B.C.C.A.)):

“Settlements assist the Commission to ensure that its overriding objective, the protection of the public, is met. Settlements proscribe activities that are harmful to the public. In so doing, they are effective in accomplishing the purposes of the statute. They provide means of reaching a flexible remedy that is tailored to address the interests of both the Commission and the person under investigation.”

33. Hearing Panels should respect settlements worked out by the parties. A Panel does not know what led to a settlement, what was given up by one party or the other in the course of the negotiations, and what interest each party has in agreeing to resolve the matter. The Panel cannot go beyond the Settlement Agreement. There are almost always facts that play a role in the settlement which are not set out in the Settlement Agreement or brought to the attention of the Panel. There were significant negotiations in the present case.

34. As a Panel stated (*Re Keshet*, File No. 201419 at paragraph 7), to take one of many such cases: “It is well established that hearing panels should not interfere lightly in negotiated settlements and should not reject a settlement agreement unless it views the proposed penalty clearly falling outside a reasonable range of appropriateness.” There are many similar statements by MFDA Panels, stemming from the leading decision of *Re Milewski* [1999] I.D.A.C.D. No. 17, which stated: “A District Council considering a settlement agreement will tend not to alter a penalty that it considers to be within a reasonable range, taking into account the settlement process and the fact that the parties have agreed. It will not reject a settlement unless it views the penalty as clearly falling outside a reasonable range of appropriateness.”

Should the Panel Accept the Settlement Agreement?

35. A Panel can accept or reject a Settlement Agreement. It cannot modify it.

36. One important factor in the present case leading to a lesser penalty than might ordinarily be imposed is that the Respondent worked diligently with W.H. Stuart Ltd. in dealing with the aftermath of the improper conduct by the Member and others. Paragraph 73 of the Settlement Agreement states: “After the MFDA commenced disciplinary action against W. H. Stuart and Dianne Stuart on April 29, 2013...the Respondent was assigned responsibility initially for complaint handling and subsequently for all management functions of W.H. Stuart until the client accounts of W.H. Stuart could be transferred to Keybase on May 17, 2013 in accordance with an agreement of purchase and sale.”

37. After the bankruptcy and insolvency of W.H. Stuart, the Respondent assisted the Investment Protection Fund (“IPC”) in the claims process to compensate eligible clients of W.H. Stuart who could establish that they suffered losses attributable to the bankruptcy of W.H. Stuart. So far, the IPC has evaluated 252 claims for compensation, totalling approximately \$7.5 million. See paragraphs 76 and 77 of the Settlement Agreement.

38. Further, the Respondent did not promote or sell the 7% Investment Notes to his clients. He therefore gained no compensation from the improper activity of the Stuarts and others. Nor did he profit from his own failure to investigate, except that he was able to continue working for W.H. Stuart. Fines often reflect the extent to which a Respondent profited by his or her actions.

39. We also note that the Respondent did not have any prior disciplinary history.

40. There is also the possibility that the Respondent will lose about \$200,000 which – strangely – he kept as “cash on deposit” with the Member from 2002 to 2013, a very lengthy period. He has made a claim to the IPC for this loss. Whether he will be compensated by the IPC remains to be seen. The protection fund is, we were informed, waiting until this proceeding is completed to decide what to do. The IPC regulations provide that a customer eligible for compensation ‘does

not include...a person who caused or materially contributed to the insolvency of a Member.” The matter is, of course, for the IPC and not for this Panel to determine.

41. The MFDA took into account that the Respondent did not have the financial resources to pay a larger sum than a \$10,000 fine and \$5,000 costs. Paragraph 83 of the Settlement Agreement states: “The Respondent has produced financial information to MFDA Staff including tax returns and banking records to support his assertion that as a result of the reduction of his income since 2013 and the loss of approximately \$200,000 in retirement savings as a consequence of the bankruptcy and insolvency of W.H. Stuart, the Respondent lacks the financial resources to pay substantial financial penalties.” Moreover, as a result of this Hearing, the Respondent will lose his registration and his income will decrease from what it had been.

42. Paragraph 84 also notes that the “Respondent has cooperated with Staff’s investigation and has substantially reduced the length and complexity of this proceeding by entering into a settlement agreement with Staff.” The Settlement Agreement shows a level of remorse, which was also expressed in the Respondent’s final comments to the Panel.

43. If the Panel rejects the Settlement Agreement and thereby brings about a lengthy hearing, the costs to the MFDA would be substantial. Moreover, litigation is rarely a sure thing. The eventual result might well be a significantly higher penalty, but it is more than likely that the MFDA would not be able to collect the higher penalty, just as they have been unable to date to collect the very high penalties imposed upon Dianne and Howard Stuart. The MFDA, it appears, believed that obtaining the sum of \$15,000 through a Settlement Agreement was better than getting a higher fine which could not be collected and at the same time expending significant financial and other resources in a lengthy hearing.

44. Moreover, in some of the cases cited to us, particularly with respect to branch managers, the financial penalty was very low or even in some cases zero. (See *Re Cunningham* 2010 LNCMFDA 54; *Re Dibley* 201655; and *Re Greenberg* 2014 LNCMFDA 82). We also note in the cases involving Dianne and Howard Stuart, that the Member itself was not fined because the Member was bankrupt and had no funds to pay a fine.

45. In the related case of *Re Rumball* (201521) the Panel accepted a fine of \$25,000 in a Settlement Agreement where the Respondent between 2003 and 2013 solicited and accepted more than \$2.5 million from 12 clients of W.H. Stuart for investment in the Note Program. Unlike the Respondent in the present case, he obtained commissions from these transactions. Like the Respondent he was relatively impecunious at the time of the hearing. The Panel stated: ‘We recognize that a fine in this amount will not always adequately address serious conduct. However, in the particular circumstances of this case, the proposed fine is reasonable.’

46. Deterrence, specific and general, is a strong consideration in setting penalties. Barring a person from the industry is normally a stronger deterrent than a fine.

47. Counsel for the MFDA stressed to us that the fine in the present case was because of the somewhat unique facts and circumstances of this case and will not be seen by the MFDA as a precedent for later cases involving the role of the CCO.

48. The Panel finds that the penalty and the costs agreed to in this case, coupled with barring the Respondent from conducting securities related MFDA business falls within “a reasonable range of appropriateness.”

49. For the above reasons the Panel accepted the Settlement Agreement.

DATED this 13th day of November, 2018.

“Martin L. Friedland”

Martin L. Friedland, CC, QC
Chair

“Guenther W.K. Kleberg”

Guenther W.K. Kleberg
Industry Representative

“Joseph Yassi”

Joseph Yassi
Industry Representative

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