



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: Sebastian Eduardo Encalada

Heard: February 20, 2018 in Toronto, Ontario

Decision: February 20, 2018

Reasons for Decision: April 30, 2018

REASONS FOR DECISION

Hearing Panel of the Central Regional Council:

John Lorn McDougall, QC	Chair
Kenneth P. Mann	Industry Representative
Guenther W. K. Kleberg	Industry Representative

Appearances:

David Babin)	Counsel for the Mutual Fund Dealers
)	Association of Canada
)	
)	
James Milne)	Counsel for the Respondent
)	
)	
Sebastian Eduardo Encalada)	Respondent, in person
)	

I. INTRODUCTION

1. By Notice of Hearing dated September 6, 2017, the Mutual Fund Dealers Association of Canada (“MFDA”) alleged misconduct against Sebastian Eduardo Encalada (“Respondent”)

2. The Notice of Hearing called for a hearing on the matter to be held on November 14, 2017 before a hearing panel of the Central Regional Council (“Hearing Panel”). On the return of the Notice of Hearing, the matter was adjourned to February 20, 2018 for a hearing on the merits.

3. The Notice of Hearing sets out the following allegations of violations of the By-laws, Rules or Policies of the MFDA:

Allegation #1: Between March 2015 and October 2015, the Respondent opened an account for an individual and processed 18 transactions in the account, without the individual’s knowledge or authorization, thereby engaging in:

- a) discretionary trading, contrary to MFDA Rules 2.3.1 and 2.1.1; and/or
- b) conduct that increased the Respondent’s chances of qualifying for a bonus or other compensation through a branch incentive program, which gave rise to a conflict or potential conflict of interest with the interests of the individual that the Respondent failed to address by the exercise of responsible business judgment influenced only by the best interests of the individual, contrary to MFDA Rules 2.1.4 and 2.1.1.

Allegation #2: Between March 2015 and October 2015, the Respondent signed an individual’s signature or initials on two account forms in order to open an account and process 18 transactions in the individual’s account, contrary to MFDA Rule 2.1.1.

4. The Respondent filed a Reply dated October 16, 2017 in which, inter alia, he denied the allegations set out in the Notice of Hearing. He included in his Reply the following “Additional Facts” concerning his medical condition as it related to his ability to work and specifically with reference to Allegation #1 b) above:

1. At the time of the alleged incident, the Respondent was undergoing treatment for a serious medical condition. He ceased working altogether in September 2015 and since that time, the Respondent has been on long term disability related to these serious medical issues.
2. The Respondent has been prescribed and regularly takes medications for his illnesses which have kept him from working and otherwise living a normal life. He has since been in recovery for his illness, and is showing significant improvement with the regular assistance of his family and his medical professionals. It is his hope that he will one day be able to return to work and return to a normal life.
3. Due to his medical issues, the Respondent had no reasonable prospect whatsoever to qualify for a bonus or other compensation for the actions in this proceeding. The Respondent was simply trying to do his job and serve the complainant's interests at all times relevant to his action.

5. Immediately before the hearing on February 20, 2018, the Hearing Panel was advised that the matter had been settled. We were provided with a Settlement Agreement dated February 20, 2018 ("Settlement Agreement") and after reading it, the hearing commenced. It is to be noted that there is no mention of Allegation #1 b) in the Settlement Agreement.

6. In the event, Staff chose not to proceed with Allegation #1 b). During oral submissions Staff counsel made the following statement:

In the case this [*sic*], this wasn't undertaken by the respondent in this instance for his own benefit or to undertake the misconduct for the sake of client harm. It was undertaken on a basis that is significantly more benign than that, I think is the appropriate way to phrase it. The point of putting that into the submissions is just to underscore the point that this respondent was not seeking to harm any clients or to commit fraud or other types of activities that will often arise from signature falsification or discretionary trading on an unauthorized basis.

7. Section 24.4.3 of MFDA By-law No. 1 and Rule 15.2 of the MFDA Rules of Procedure require that 10 days' notice be given ahead of a settlement hearing. Staff and the Respondent applied for an order abridging the time so the matter could proceed without giving the required 10 days' notice.

8. Upon being satisfied that the Hearing Panel had the jurisdiction to grant the order sought and upon the representation that there was nobody with an interest in the proceedings that was not aware of the proposed settlement, the Hearing Panel granted the order sought.

9. In Part V of the Settlement Agreement the Respondent in paragraph 27 admits that:

- a) between March 2015 and October 2015, he opened an account for an individual and processed 18 transactions in the account, without the individual's knowledge or authorization, thereby engaging in discretionary trading, contrary to MFDA Rules 2.3.1 and 2.1.1; and
- b) between March 2015 and October 2015, he falsified an individual's signature or initials on two account forms in order to open an account and process 18 transactions in the individual's account, contrary to MFDA Rule 2.1.1.

10. Staff and the Respondent agreed to terms and conditions of the settlement and the Respondent has consented to the making of an order against him as follows:

- a) The Respondent's authority to conduct securities related business in any capacity while in the employ of or associated with any MFDA Member shall be prohibited for a period of one year from the date of the order, pursuant to section 24.1.1(e) of MFDA By-law No. 1;
- b) The Respondent shall pay a fine in the amount of \$5,000 pursuant to section 24.1.1(b) of By-law No. 1;
- c) The Respondent shall pay costs in the amount of \$5,000 pursuant to section 24.2 of By-law No. 1 upon acceptance of this Settlement Agreement;
- d) The Respondent's fine and costs shall be payable as follows:
 - i. \$2,500 payable on or before the date of the settlement hearing; and
 - ii. \$7,500 payable no later than 60 days from the date that the Settlement Agreement is accepted by the Hearing Panel;

- e) If the Respondent fails to comply with the provision of subparagraph (d)(ii), the authority of the Respondent to conduct securities related business while in the employ of or associated with a Member of the MFDA shall be immediately suspended without further notice or order of the Hearing Panel until such time as the Respondent demonstrates to the satisfaction of Staff that he has complied with the provisions of subparagraph (d)(ii); and
- f) The Respondent will attend in person, on the date set for the Settlement Hearing.

II. SETTLEMENT AGREEMENT AND AGREED FACTS

11. The additional portions of the Settlement Agreement which are relevant to these Reasons for Decision are as follows:

IV. AGREED FACTS

Registration History

- 6. Between November 9, 2012 and November 3, 2016, the Respondent was registered in Ontario as a dealing representative with TD Investment Services Inc. (“TDIS”), a Member of the MFDA.
- 7. At all material times, the Respondent operated out of a TDIS branch located in Brampton, Ontario.
- 8. The Respondent is not currently registered in the securities industry in any capacity.

Unauthorized Discretionary Trading

- 9. At all material times, IM was a retail banking client of TD Canada Trust (“TD Bank”). IM was not a client of TDIS until the Respondent, without the knowledge or authorization of IM, opened an account for IM at TDIS and processed trades in the account, as described in greater detail below.
- 10. In February 2015, IM sold his home and deposited the proceeds from the sale into his savings account at TD Bank.
- 11. On or about March 15, 2015, the Respondent contacted IM by telephone to discuss options for the use of the proceeds from the sale of IM’s house. The Respondent had previously arranged a mortgage at TD Bank for a separate investment property that IM had purchased.

12. IM was considering the purchase of another home in the near future and did not want to subject his money to any investment risk. Therefore, IM informed the Respondent that he wanted to open a high interest savings account and maintain the proceeds of the home sale on deposit in that bank account.

13. On March 27, 2015, without the knowledge or authorization of IM, the Respondent completed a Non-Registered Account Application Form (“NRAAF”) in IM’s name, and processed two purchases in the account:

- a) TD Monthly Income Fund in the amount of \$40,000; and
- b) TD Comfort Balanced Portfolio in the amount of \$60,000.

14. On the same day, the Respondent also set up, without the knowledge or authorization of IM, a Pre-Authorized Purchase Plan (“PPP”) that automatically invested an additional \$500 each month from IM’s savings account into each of the two funds described above.

15. Between March 27, 2015 and October 22, 2015, the unauthorized PPP resulted in 14 additional trades being processed in IM’s account, including the purchase of \$3,500 of units of the TD Monthly Income Fund and \$3,500 of units of the TD Comfort Balanced Portfolio.

16. IM did not meet with the Respondent on March 27, 2015, authorize the Respondent to open a mutual fund account for him, sign the NRAAF, or authorize the fund purchases or the implementation of the PPP.

17. The Respondent falsified IM’s signature on the NRAAF in order to open an account for IM at TDIS and process the transactions described in paragraphs 13 – 15 above.

18. On July 23, 2015, the Respondent prepared and completed a Transaction and Account maintenance Form (the “Transaction Form”) for IM’s account at TDIS, and processed two additional purchases in the account:

- a) TD Monthly Income Fund in the amount of \$10,000; and
- b) TD Comfort Balanced Portfolio in the amount of \$35,000.

19. IM did not meet with the Respondent on July 23, 2015, sign the Transaction Form, or authorize the Respondent to process fund purchases in IM’s account at TDIS.

20. The Respondent falsified IM’s signature or initials on the Transaction Form in order to process the transactions described in paragraph 18 above.

III. DECISION

12. After considering the Settlement Agreement and the full submissions made by Staff and counsel for the Respondent, and deliberating briefly, the Hearing Panel unanimously accepted the Settlement Agreement. The Hearing Panel made an order to that effect and indicated that Reasons for Decision would follow in due course. These are those Reasons for Decision.

IV. REASONS AND ANALYSIS

13. MFDA Rule 2.1.1 states the following:

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.

14. MFDA Rule 2.1.1 is designed to protect the public interest by requiring Approved Persons to adhere to a high standard of ethical conduct. The Rule has been interpreted and applied in a purposive manner in a wide range of circumstances. As stated by the MFDA Hearing Panel in *Breckenridge*: “The Rule articulates the most fundamental obligations of all registrants in the securities industry”.

Breckenridge (re), MFDA File No. 200718, Hearing Panel of the Central Regional Council, Decision and Reasons dated November 14, 2007, at para. 71.

15. MFDA Hearing Panels have routinely found that both discretionary trading and the falsification of client signatures are a breach of Rule 2.1.1.

Hayat (Re), MFDA File No. 201210, Hearing Panel of the Central Regional Council, Decision and Reasons dated May 21, 2013, at para 4.

McPherson (Re), MFDA File No. 201209, Hearing Panel of the Pacific Regional Council, Decision and Reasons dated October 1, 2013, at para. 14.

Mammone (Re), MFDA File No. 201113, Hearing Panel of the Central Regional Council, Decision and Reasons dated March 12, 2012, at para. 12.

15. Staff submitted that the Respondent's misconduct was serious. Hearing Panels of the MFDA have held that, where an Approved Person engages in discretionary trading, they have engaged in serious misconduct.

Ewens (Re), MFDA File No. 201714 Hearing Panel of the Prairie Regional Council, Decision and Reasons dated April 6, 2017 ("*Ewens*"), at para. 17.

Izzio (Re), MFDA File No. 201355, Hearing Panel of the Central Regional Council, Decision and Reasons dated July 30, 2014.

16. Approved Persons, under no circumstances, are permitted to engage in discretionary trading because it is incompatible with their registered status as a dealing representative. As the Hearing Panel in *O'Brien* held:

Individuals registered as investment counsel or portfolio managers have discretionary trading authority, and investment advisors are permitted to conduct discretionary trades in managed or discretionary accounts, provided they have explicit written consent. However, mutual fund salespeople are not permitted to conduct discretionary trades and must always contact the client prior to making any transactions. Where an Approved Person fails to obtain client instructions prior to executing a trade, he engages in discretionary trading beyond the terms of his or her registration as a mutual funds salesperson.

O'Brien, (Re) MFDA File No. 200809, Hearing Panel of the Atlantic Regional Council, Decision and Reasons dated November 25, 2008 at para. 19.

17. MFDA Staff considers the falsification of a client signature and subsequent use of a falsified form to be a more serious contravention of MFDA Rule 2.1.1. Unlike pre-signed account forms, where the client knows he or she is signing an incomplete form to be used in some way, in the case of a form falsified by the Approved Person, the possibility, if not probability, exists that the client is unaware of the Approved Person's actions.

Techer (Re), MFDA File No. 201662, Hearing Panel of the Prairie Regional Council, Decision and Reasons dated December 5, 2016, at paras. 37 – 38.

MacPherson (Re), MFDA File No. 201621, Hearing Panel of the Prairie Regional Council, Decision and Reasons dated April 6, 2017, at para. 17.

18. These are discrete breaches in that discretionary trading involves trading without first obtaining the client's instructions while signature falsification is simply unauthorized trading utilizing a forged signature or initials of the client. As Staff recognized in its submissions, while both discretionary trading and falsification are serious offences, the latter is significantly more so, not the least because it entails the loss of the audit trail. But it is much more than that in that it is completely contrary to the governing principles of the securities industry.

19. The hearing panel in *Bell* made the following statement which aptly captures this Hearing Panel's view:

Forgery is always serious. It is unequivocally condemned because it is fundamentally dishonest and dangerous. Any act of forgery is a step onto a steep and slippery slope of deception that is always potentially harmful to clients and actually harmful to the Member firm and the securities industry as a whole. While there is no such thing as a "minor case" of forgery, we can distinguish between more and less egregious examples of forgery...Less egregious examples of forgery are distinguished by the absence of aggravating factors, which may be viewed obversely as the presence of mitigating factors.

Bell (Re), [2005] I.D.A.C.D. No. 15

20. The term "signature falsification" for the act of signing the signature or initials of a client to a document without the client's knowledge is a euphemism for the more elemental word "forgery", a fact which the hearing panel in *Bell* recognized. The act of forging a client's signature strikes at the very heart of the relationship of trust which must exist between client and representative.

21. Staff made submissions regarding the suitability of the penalties which had been agreed to in the Settlement Agreement. In support of its application for approval, Staff made reference to the numerous matters which Hearing Panels have long considered when deciding whether a proposed settlement should be accepted as follows:

- a) Whether acceptance of the settlement agreement would be in the public interest and whether the penalty imposed will protect investors;
- b) Whether the settlement agreement is reasonable and proportionate, having regard to the conduct of the respondent as set out in the settlement agreement;
- c) Whether the settlement agreement addresses the issues of both specific and general deterrence;
- d) Whether the proposed settlement will prevent the type of conduct described in the settlement agreement from occurring again in the future;
- e) Whether the settlement agreement will foster confidence in the integrity of the Canadian capital markets;
- f) Whether the settlement agreement will foster confidence in the integrity of the MFDA; and
- g) Whether the settlement agreement will foster confidence in the regulatory process itself.

In the Matter of Rodney Jacobson, [2007] MFDA Hearing Panel of the Prairie Regional Council, MFDA File No. 200712, Decision dated July 13, 2007 (“*Jacobson*”) at pp. 9 and 12.

In the Matter of Investors Group Financial Services, [2004] MFDA Hearing Panel of the Ontario Regional Council, MFDA File No. 200401, Reasons for Decision dated December 16, 2004 at pp. 2-3.

In the Matter of IQON Financial Inc. (Re), [2007] MFDA Hearing Panel of the Pacific Regional Council, MFDA File No. 200713, Decision and Reasons dated May 24, 2007 at p. 9.

22. Staff submitted that it would be in the public interest for the Hearing Panel to accept the Settlement Agreement, having in mind that the primary goal of securities regulation is the protection of the investor.

Pezim v. British Columbia (Superintendent of Brokers), [1994] 2 S.C.R. 557 at paras. 59, 68.

23. Staff went on to urge the Hearing Panel not to interfere lightly with, and to give deference to, a negotiated settlement as long as the penalties agreed to are within the reasonable range of

appropriateness given the conduct of the Respondent. The primary basis for this submission was that it is in the public interest to facilitate early resolution of such matters which are harmful to the public perception of the industry, thereby fostering confidence in the regulatory regime. The force of this submission is unquestioned and more than justifies the usual *prima facie* disinclination on the part of hearing panels to interfere with the completion of settlements that fall within the broad range of what is reasonably appropriate in all the circumstances of the case.

24. From the written and oral submissions of Staff, it appears that there was no loss suffered as a result of the Respondent's admitted acts. Certainly the client IM suffered no loss but it is not clear whether the Dealer repaid any market losses. Staff did not seem to know when asked about it and counsel for the Respondent was unable to provide any information. The Hearing Panel therefore concluded that, had there been significant losses covered by the Dealer, we would have been told.

25. The Respondent's misconduct is serious and, in the case of signature falsification, gravely so. However, having reviewed the authorities referred to us by Staff and the factors to be considered in arriving at a conclusion whether the penalties agreed to fall within a reasonable range of appropriateness, we concluded that they did. There were several aspects to this case that were important components to our evaluation.

Tonnies (Re), MFDA File No. 200503, June 27, 2005, paras 45 and 46.

Breckenridge, supra, para 77 and the decisions cited therein.

26. First, the Respondent recognized the serious nature of his conduct and actively cooperated with Staff. He appeared in person at the hearing and was represented by counsel who made useful submissions.

27. Second, the Respondent has had no previous instances of professional misconduct.

28. Third, there appears to have been no harm suffered by the Respondent's client, IM.

29. Staff is of the view that the Respondent would pose no risk should he return to the securities industry as this was a single instance of misconduct. We accepted that submission as likely being correct.

30. Fourthly, we were influenced in a favourable way by the fact that Staff took the position that the Respondent's transgressions, while serious, were not motivated by self-gain and that he received no benefit from his conduct. This was a pivotal distinction which was influential in our decision to accept the settlement.

31. Finally, we reviewed the previous decisions that Staff supplied as being made in similar circumstances. While there was a range of severity of penalty in the list, it seemed to us that the milder factual matrix in the present case fitted in with the lower end of the penalties imposed and thus this case fitted within the reasonable range of appropriateness using the previous decisions as a measure.

Rounthwaite (Re), MFDA File No. 201123, Hearing Panel of the Central Regional Council, Decision and Reasons dated July 30, 2012.

Carney (Re), MFDA File No. 201646, Hearing Panel of the Central Regional Council, Decision and Reasons dated May 9, 2017.

V. CONCLUSION

32. It is for the foregoing reasons that we granted the order accepting the Settlement Agreement on February 20, 2018.

DATED this 30th day of April, 2018.

“John Lorn McDougall”

John Lorn McDougall, QC
Chair

“Kenneth P. Mann”

Kenneth P. Mann
Industry Representative

“Guenther W. K. Kleberg”

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