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: David Michael Gordon

Heard: September 23, 2019 in Vancouver, British Columbia
Decision: September 23, 2019
Reasons for Decision: December 5, 2019

REASONS FOR DECISION

Hearing Panel of the Pacific Regional Council:

The Hon. Thomas R. Braidwood, QC	Chair
Darlene Barker	Industry Representative
Holly Millar	Industry Representative

Appearances:

Justin Dunphy	)	Enforcement Counsel for the Mutual Fund Dealers Association of Canada
Tom Newnham	)	Counsel for the Respondent
David Michael Gordon	)	Respondent, in person

1. This hearing was duly constituted by the Mutual Fund Dealers Association of Canada ("MFDA") to consider a settlement agreement dated July 31, 2019 (the "Settlement Agreement), between the MFDA and David Michael Gordon (the "Respondent").

Contraventions

2. The Settlement Agreement contains the contraventions, which contraventions by the terms of the Settlement Agreement the Respondent admits. The contraventions are as follows:

a) between 2009 and May 2016, the Respondent failed to ensure that an investment recommendation he made to at least 6 clients to invest in precious metals sector funds was suitable heaving regard to the client's relevant Know-Your-Client ("KYC") factors, including their age, employment status, investment objectives, investment knowledge, risk tolerance, and time horizon, and the risks associated with concentrating their investment portfolio in precious metals sector funds, contrary to MFDA Rules 2.2.1 and 2.1.1.; and

b) between 2009 and May 2016, the Respondent failed to full and adequately explain, or omitted to explain the risks and benefits of investing in precious metals sector funds to at least 6 clients, thereby failing to ensure that his recommendations were suitable for the clients and keeping with their investment objectives, contrary to MFDA Rules 2.2.1 and 2.1.1.

Terms of Settlement

3. The Respondent agreed to the terms of the settlement as follows:

a) he shall be permanently prohibited from conducting securities related business in any capacity while in the employ of or associated with any MFDA Member;

b) he shall pay a fine of $25,000.00 (the "Fine");

c) he shall pay costs of $2,500.00 (the "Costs");

d) the payment of the Fine and Costs are to be made by way of certified funds as follows:

    i) $15,000.00 (Fine) upon acceptance of the Settlement Agreement by the Hearing Panel;

ii) $2,500.00 (Costs) upon acceptance of the Settlement Agreement by the Hearing Panel;

iii) $5,000.00 (Fine) on or before the last business day of the sixth month following the date of Settlement Agreement; and

iv) $5,000.00 (Fine) on or before the last business day of the twelfth month following the date of Settlement Agreement.

The Test

4. The role of the Hearing Panel at a settlement hearing is fundamentally different than its role at a contested hearing. As stated by the MFDA Hearing Panel in *Sterling Mutuals Inc. (Re),* citing the I.D.A. Ontario District Council in *Milewski (Re)*:

> "We also note that while in a contested hearing the Panel attempts to determine the correct penalty, in a settlement hearing the Panel 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."
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> *Sterling Mutuals Inc. (Re)*, MFDA File No. 200820, Hearing Panel of the Central Regional Council, Decision and Reasons dated August 21, 2008 at para. 35
>
> *Milewski (Re)*, [1999] IDACD No. 17 at p. 10, Ontario District Council Decision dated July 28, 1999

5. The Hearing Panel considered whether the any of the following were relevant when determining whether the proposed settlement should be accepted:

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 settlement agreement 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.

Sterling Mutuals Inc. (Re), supra, at para.34 and the decisions cited therein

6. Investor protection is the primary goal of securities regulation, whether in the context of a settlement hearing or a contested hearing.

Pezim v *British Columbia (Superintendent of Brokers),* [I 994) 2 SCR 557 (SCC) at paras. 59, 68

Breckenridge (Re), MFDA File No. 200718, Hearing Panel of the Central Regional Council, Decision and Reasons dated November 14, 2007 at para. 74.

7. In addition to investor protection, the goals of securities regulation include fostering public confidence in the capital markets and the securities industry.

Pezim, Supra, at paras. 59, 68

8. The Hearing Panel considered the following factors, where applicable, when determining whether the penalty is appropriate:

a) the seriousness of the allegations proved against the Respondent;

b) the Respondent's past conduct, including prior sanctions;

c) the Respondent's experience and level of activity in the capital markets;

d) whether the Respondent recognizes the seriousness of the improper activity;

e) the harm suffered by investors as a result of the Respondent's activities;

f) the benefits received by the Respondent as a result of the improper activity;

g) the risk to investors and the capital markets in the jurisdiction, were the Respondent to continue to operate in capital markets in the jurisdiction;

h) the damage caused to the integrity of the capital markets in the jurisdiction by the Respondent's improper activities;

i) 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;

j) the need to alert others to the consequences of inappropriate activities to those who are permitted to participate in the capital markets; and

k) previous decisions made in similar circumstances.

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

Fike (Re), MFDA File No. 2017102, Hearing Panel of the Central Regional Council Decision and Reasons dated December 7, 2017

Lemay (Re), MFDA File No. 201634 Hearing Panel of the Pacific Regional Council Decision and Reasons dated February 28, 2017

9. In cases involving the type of misconduct in the present case, MFDA staff submitted the following factors as set out in the Sanction Guidelines which are relevant to the Hearing Panel's decision:

a) general and specific deterrence;

b) public confidence;

c) seriousness of the allegations proved against the Respondent;

d) the Respondent's recognition of the seriousness of the misconduct;

e) benefits received by the Respondent and harms suffered by the investors;

f) previous decisions made in similar circumstances; and

g) ability to pay.

Excerpts from the MFDA Sanction Guidelines

Seriousness of Misconduct

10. The present case is extremely serious.

11. MFDA Rule 2.1.1 sets the standard of conduct to be followed by all 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 has been interpreted and applied in a purposive manner

in a wide range of circumstances. As stated by the MFDA Hearing Panel in *Breckenridge (Re)*: "The Rule articulates the most fundamental obligations of all registrants in the securities industry."

Breckenridge (Re), supra, at p. 20

12. MFDA Rule 2.1.1 requires that each Member and Approved Person deal fairly, honestly, and in good faith with clients, observe high standards of ethics and conduct in the transaction of business, and refrain from engaging in any business conduct or practice which is unbecoming or detrimental to the public interest.

13. MFDA Rule 2.2.1 (prior to December 3, 2010) states, in part:

> **2.2.1 "Know-Your-Client"**. Each Member and Approved Person shall use due diligence:
>
> a) to learn the essential facts relative to each client and to each order or account accepted;
>
> b) to ensure that the acceptance of any order for any account is within the bounds of good business practice; and
>
> c) to ensure that each order accepted or recommendation made for any account of a client is suitable for the client and in keeping with the client's investment objectives.

MFDA Rule 2.2.1

14. MFDA Rule 2.2.1 codifies the "Know-Your-Client" and "Suitability" obligations that have consistently been recognized as "an essential component of the consumer protection scheme of [securities legislation] and a basic obligation of a registrant and a course of conduct by a registrant involving a failure to comply with them is an extremely serious matter."

15. "The·Know-Your-Client" Rule, referred to as the "Cardinal Rule" by the Hearing Panel in *Lamoureux (Re),* is the cornerstone obligation of an Approved Person's dealings with clients.

16. In the present matter, the Respondent failed to accurately record the KYC information of his clients in order for them to invest in precious metals sector funds. With respect to all 6 clients, the Respondent failed to ensure the investments were suitable in regards to the clients' relevant KYC factors, including, age, employment status, investment objectives, investment knowledge, risk tolerance, and time horizon.

Registration History

17. The Respondent has been registered in the securities industry since 1992.

18. From November 9, 2006 to May 13, 2016, when he retired, the Respondent was registered in British Columbia as a mutual fund salesperson (now known as a dealing representative) with FundEX Investments Inc. ("FundEX"), a Member of the MFDA.

19. The Respondent is not currently registered in the securities industry in any capacity.

20. At all material times, the Respondent had an office in the Campbell River, British Columbia area and served clients throughout British Columbia.

Agreed Facts

The Gold Strategy

21. Between 2009 and May 2016, the Respondent recommended an investment strategy to at least 6 clients whereby the clients would purchase, among other things, precious metals (predominantly, gold) sector mutual funds (the "Gold Strategy").

22. In the course of recommending the Gold Strategy to clients, the Respondent represented that, among other things:

a) the price of gold and other precious metals was poised to increase due to an imminent decline in the stock market; or
b) investing in gold and precious metals sector funds was a safer alternative to investing in the stock market generally.

Client A and B

23. Clients A and B were clients of the Respondent since the 1980s. From November 2006 to June 2016, clients A and B were clients of FundEX and the Respondent was the Approved Person responsible for servicing their investment accounts at FundEX.

24. Clients A and B are spouses.

25. Since about 2007, clients A and B made monthly withdrawals from Registered Retirement Income Fund ("RRIF") accounts they each held at FundEX.

26. Clients A and B also each held a Registered Retirements Savings Plan ("RRSP") at FundEX.

27. In February 2009, clients A and B implemented the Gold Strategy. Clients A and B sold their existing investments totaling $103,000 in their RRSP and RRIF accounts, and invested 50% of the monies in the BMG Bullion Fund and 50% of the monies in a money market fund.

28. At the time the Respondent recommended the Gold Strategy, clients A and B:

a) were 68 years old;
b) Client A had low investment knowledge and was retired;
c) Client B had moderate investment knowledge and was a house cleaner;
d) had limited net worth (less than $200,000);
e) had limited income (less than $30,000 per year) and required their investment holdings to pay for living expenses; and
f) had limited ability to withstand investment losses.

29. After clients A and B implemented the Gold Strategy, the clients continued making monthly redemptions of the money market mutual fund in order to pay living expenses.

30. By January 2013, clients A and B had depleted their holdings of the money market fund through monthly withdrawals to pay living expenses and held only the BMG Bullion Fund in their accounts at FundEX.

31. After the money market holdings were depleted, clients A and B began making monthly redemptions of the BMG Bullion Fund in order to pay living expenses.

32. Notwithstanding that the Respondent was aware that clients A and B had depleted their holdings of the money market fund and were redeeming their holdings of the BMG Bullion Fund to pay living expenses, he did not recommend that the clients rebalance their accounts at FundEX.

33. Commencing in about May 2013, client B began emailing the Respondent and expressing concerns about the performance of the Gold Strategy. For example, on May 7, 2013, client B sent an e-mail to the Respondent stating:

> I was just wondering why my funds went down $4,245.57 from March 15 to April 15, was there a crash in my funds or something? At this rate I'll be out of money very quickly. Could you please let me know.

34. The Respondent replied the same day and stated:

> Gold/silver/platinum dropped from April 6 to the April 15, 2013, then it has come back up about 60% of the drop…There is a split in prices between Paper Gold and Real gold. The experts believe it will bounce back to the $1500+, then work its way up over the year. We moved to the Real Gold because of all the problems in the world, and things are getting worse… Things are going to end badly (just when) and I want to have real assets, (gold/silver/platinum). Things can go real badly at anytime. I want to stay put for now and be patient… It will take a jump, problem is just when? The longer it goes the bigger the jump. We are heading for either major inflation or major financial adjustment. That is why the gold and silver. It is coming. [Emphasis added.]

35. On July 23, 2013, client B sent an e-mail to the Respondent stating:

> I just got my Transaction Confirmation and as of from May 15 to June 16th I have gone down $2,359.13 and [client A] has gone down $6,021.82 from May 1 to June 28th. At this rate we won't have any money left in 10 months. Is there something we can do or are we still to hold out.

36. The Respondent responded on the same day and stated:

> On June 28, 2013 Gold/Silver bottom out and is now climbing. Problem is that it went too far up in 2011 then went too far down this year… The world problem (financially) just keep getting worse and worse. They keep printing money. The question is when will there be a lose (*sic*) in the US Dollar confidence…It is up again today and the Magic Technical point is $1350. It is $1342 right now. If it

> closes over $1350 the experts say things will take off. We have to stay put, it is happening. [Emphasis added.]

37. On November 22, 2014, client B sent an email to the Respondent stating:

> I was just wondering if there is anywhere else I can put my money as it is going down pretty fast…I haven't got a heck of a lot left so it is kind of scary when it goes down so fast.

38. On November 25, 2014, the Respondent responded by email and stated:

> World GDP is dropping rapidly and heading for a recession. Which will lead to more money printing… Gold is a Currency... Problem has been the Silver dropped more. I know if you have time, it will come back. Problem is when? [Emphasis added.]

39. In this response e-mail dated November 25, 2014, the Respondent provided options for clients A and B to move their investments into Guaranteed Investment Certificates but advised client B that the "problem is interest rates are low and have not really changed in 5 years."

40. Notwithstanding that the Respondent was aware of the concerns expressed by the clients with respect to the Gold Strategy, the Respondent did not recommend rebalancing their accounts until November 25, 2014.

41. The Respondent failed to fully explain the risks associated with concentrating clients A and B's investment portfolio in precious metals sector funds. The Respondent states he explained some of the risks of investing in precious metals sector funds, but he failed to provide a balanced presentation of the risks and minimized the risks when he described the Gold Strategy.

42. In June 2016, clients A and B transferred their accounts out of FundEX.

43. Clients A and B suffered losses as result of having a concentrated position in precious metals sector funds.

44. In January 2017, clients A and B submitted a complaint with FundEX with respect to the Respondent's handling of their accounts.

45. Clients A and B suffered losses as result of having a concentrated position in precious metals sector funds.

46. On December 15, 2017, FundEX compensated clients A and B for these losses.

Client MB

47. From November 2006 to June 2016, client MB was a client of FundEX and the Respondent was the Approved Person responsible for servicing her investment accounts at FundEX.
On November 27, 2006, the Respondent recorded the following information on client MB's New Client Application Form:

a) Occupation: Retired;
b) Income: $30,000 to $50,000;
c) Net Worth: Over $200,000;
d) Investment Knowledge: Fair (Low);
e) Liquidity: 5+ years;
f) Investment Objectives: Balanced; and
g) Portfolio Risk Rating: 50% Low to Moderate and 50% Moderate.

48. In February 2009, the Respondent states he discussed various investment options with client MB but recommended that client MB implement the Gold Strategy. Based upon this advice, client MB switched $63,303 in CI Global High Dividend Advantage Fund and $3,476 in CI International Fund to the BMG Bullion Fund.

49. At the time the Respondent recommended the Gold Strategy, client MB:

a) was 72 years old and retired;
b) had low investment knowledge;
c) wanted a low risk investment;
d) had limited income (between $30,000-$50,000 per year) and required her investment holdings to pay for living expenses; and
e) had limited ability to withstand investment losses.

50. On April 22, 2011, the Respondent updated client MB's KYC information as follows:

a) Occupation: Retired;
b) Income: $50,001 to $70,000;

c) Net Worth: Over $200,001;

d) Investment Knowledge: Good (Moderate);

e) Liquidity: 5 years and over;

f) Investment Objectives: Growth; and

g) Portfolio Risk Rating: 50% Moderate, 30% Moderate to High, 20% High.

51. Client MB told the Respondent she wanted low risk investments and she had low investment knowledge. In the April 22, 2011 KYC update, the Respondent failed to accurately record client MB's investment knowledge and portfolio risk rating (i.e., risk tolerance). The Respondent recorded client MB's investment knowledge as "Good", and her portfolio risk rating as "50% Moderate, 30% Moderate to High and 20% High".

52. On September 8, 2011, at the Respondent's recommendation, client MB switched $50,000 from the CI Money Market Fund to the CI Signature Gold Fund.

53. On September 11 and 19, 2012, at the Respondent's recommendation, client MB switched a total of $50,000 from the CI Money Market Fund to the CI Signature Gold Fund. As a result, as of December 31, 2012, client MB held approximately 50% of her portfolio in precious metal sector funds.

54. Between 2009 and 2012, client MB's holding in precious metals sector funds in her portfolio increased from approximately 28% to 50%. The Respondent did not recommend that client MB rebalance her account to decrease the level of concentration.

55. The other clients are substantially in the same financial position and knowledge as the three above identified.

Mitigating Circumstances

56. The Respondent has been registered in the securities industry since 1992. The Respondent was also registered as an Approved Person from November 2006 until November 2016. During that time, the Respondent was not subject to any discipline by the MFDA.

57. By entering into this Settlement Agreement, the Respondent has accepted responsibility for his misconduct and avoided the necessity of the MFDA incurring additional time and expense associated with conducting a full hearing of the allegation.

58. The conduct engaged in by the Respondent resulted in clients with portfolios that were overly concentrated in precious metals sector funds that were high risk and potentially unsuitable given the Respondent's position that his investment strategy of investing in precious metals sector funds was not high risk. This exposed clients to market risks and volatility that would not otherwise have occurred had the clients held a more diversified portfolio, and also resulted in total losses of $73,585.00 as a result of their concentrated positions. FundEX compensated the clients for these losses.

59. The Respondent poses a risk to other investors and the market at large if he is allowed to return to the industry. The facts demonstrate that the Respondent will circumvent the KYC process with his own practices, where such rules impeded his ability to recommend precious metals sectors funds to clients.

Deterrence

60. The proposed penalty is necessary and sufficient to achieve the goals of a specific and general deterrence, having regard to the factors described above. The penalty demonstrates that the Respondent's misconduct in all of the circumstances is serious and has significant consequences. The penalty will also deter others in the capital markets from engaging in similar activity.

Conclusion

61. Having regard to all of the foregoing factors, the Hearing Panel is unanimously of the opinion that the penalties proposed in the Settlement Agreement will advance the public interest and enhance investor protection and ensure high standards of conduct in the mutual fund industry.

DATED this 5th day of December, 2019.

"Thomas R. Braidwood"
The Hon. Thomas R. Braidwood, QC
Chair

"Darlene Barker"
Darlene Barker
Industry Representative

"Holly Millar"
Holly Millar
Industry Representative

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