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: John Alojz Kodric

Heard: December 6, 2016, in Toronto, Ontario
Reasons for Decision: December 12, 2016

REASONS FOR DECISION

Hearing Panel of the Central Regional Council:

Mark J. Sandler	Chair
Kenneth P. Mann	Industry Representative
Joseph Yassi	Industry Representative

Appearances:

Michelle Pong	)	Counsel for the Mutual Fund Dealers Association of Canada
Greg Temelini	)	Counsel for the Respondent

Introduction

1. On December 5, 2016, Staff of the Mutual Fund Dealers Association of Canada (the "MFDA") and John Kodric (the "Respondent") entered into a settlement agreement (the "Settlement Agreement") in which the Respondent agreed to a proposed settlement of matters for which the Respondent could be disciplined pursuant to ss. 20 and 24.1 of MFDA By-law No. 1.

2. On December 6, 2016, after hearing submissions from counsel, we approved the Settlement Agreement, and signed an Order reflecting that approval. These are our written reasons for doing so.

Registration History

3. The Respondent commenced employment in September 1996 as an insurance agent. Between March 27, 1998 and September 4, 2014, he was registered in Ontario as a mutual fund salesperson/dealing representative with Manulife Securities Investment Services Inc. or its predecessors ("Manulife"), a Member of the MFDA. At all material times, he conducted business in Brampton, Ontario.

4. Manulife terminated the Respondent on September 4, 2014.

5. The Respondent is not currently registered in the securities industry in any capacity. On September 22, 2015, the Ontario Securities Commission refused the reactivation of the Respondent's registration. Its reasons reflect that he may be suitable for registration after a period of at least 12 months from the date of the Commission's decision, subject to certain terms and conditions set out in its reasons. The Respondent states that he has a firm which is aware of his current circumstances and is willing to sponsor his registration as a mutual fund dealing representative on the terms set forth in the Commission's decision.

Securities Related Business Outside the Member

Sakha Enterprise Corporation

6. In or about January 2008, the Respondent's brother-in-law, MS, advised the Respondent that he had accepted employment with Sakha Enterprise Corporation ("Sakha"). According to its website, Sakha is a Toronto-based company which is involved in gold and timber production in Russia.

7. In May 2008, the Respondent personally invested $20,000 in Sakha.

8. Between July 2008 and September 4, 2015, the following 10 clients who were serviced by the Respondent and two other individuals (the "Investors") purchased shares of Sakha totaling $248,133:

Investor Name	**Date of Investment**	**Amount**
Client JG	2008	$37,500 CAD
Clients NC and MC	December 12, 2008	$30,633 CAD
Client VR	December 2008	$30,000 CAD ($25,000 USD)
Client MD	Post April 2008	$30,000 CAD ($25,000 USD)
Clients SS and NS	Unknown	$60,000 CAD ($50,000 USD)
Clients PJ and BJ	Unknown	$30,000 CAD ($25,000 USD)
DK	Unknown	$30,000 CAD ($25,000 USD)
FB	Unknown	Unknown
Client MR	Unknown	Unknown
	TOTAL	**$248,133 CAD**

9. The Respondent states that (a) many of the Investors are family friends or long time personal friends; (b) at no time did he actively promote or endorse the investments in Sakha; (c) he made it clear that his own investment was a personal and speculative one made, amongst other reasons, because his brother-in-law worked at Sakha; and (d) he also made it clear that he was neither recommending the investment nor registered to do so.

10. The Respondent acknowledges having facilitated the sale of shares of Sakha by carrying out the following:

a) when asked for information about Sakha, referring Investors to the Sakha website or providing publicly available information about Sakha off the company website, including the nature of its business and that it was attempting to get listed on a stock exchange;
b) telling Investors about a Sakha presentation at a hotel in Mississauga and thereafter attending the same seminar;
c) when asked about his personal investments, telling the potential investors about his personal holdings, including that he held shares of Sakha;
d) letting Sakha know that there may be potential investors that would be contacting it and advising potential investors that they could contact Sakha if they wished to purchase shares;
e) providing Sakha with the names and telephone numbers of certain potential investors, including clients, after being asked to do so by the clients;
f) at the request of potential investors, delivering payments from them to Sakha for the purchase of its shares;
g) at the request of potential investors, delivering share certificates issued by Sakha to them;
h) from time to time, if requested by the Investors, informing the Investors of any update he might have respecting the status of the Sakha investments.

11. Sakha shares were not approved by Manulife for sale by its Approved Persons, including the Respondent. Manulife did not have a referral arrangement with Sakha. The sales of the Sakha shares to the Investors were not processed for the account or through the facilities of Manulife. At no time did the Respondent disclose his activities pertaining to Sakha to Manulife, nor did Manulife approve such activities.

12. The Respondent's activities pertaining to Sakha gave rise to a conflict or potential conflict of interest with clients as the Respondent personally held shares in Sakha and his

brother-in-law was employed by Sakha. While the Respondent states that he disclosed the information underlying this conflict or potential conflict of interest to clients, he acknowledges that he did not make such disclosure in writing or take adequate steps to ensure it was addressed by the exercise of responsible business judgment influenced only by the best interests of the client.

13. There is no evidence that the Respondent received fees or commissions from Sakha as a result of engaging in the conduct described above.

14. Sakha's shares are currently listed in the over-the-counter market in the United States with a reported per share value of $0.006. Sakha's shares are not actively traded and the company does not appear to be operating.

15. The Respondent and the Investors have lost substantially all of the monies they invested in Sakha. Some of the Investors have been offered and received compensation from Manulife.

The Respondent Recommended an Unsuitable Leverage Investment Strategy to Two Clients

16. In or about October 2007, the Respondent recommended and facilitated the implementation of a leverage investment strategy in the accounts of client JG and client VR whereby the clients:

(a) borrowed funds from their Manulife One account;
(b) used these funds to obtain 2-for-1 investment loans;
(c) used the monies from the Manulife One account and the 2-for-1 investment loans to purchase mutual funds, including return of capital ("ROC") mutual funds, which were expected to generate monthly distributions; and
(d) used the distributions generated by the mutual funds to pay the monthly costs associated with the borrowed monies and re-invest the difference/excess back into the investment account.

17. The monies from the Manulife One Account and the 2-for-1 investment loans were structured as interest-only loans.

18. The leverage investment strategy recommended by the Respondent was based on the premise that the mutual funds purchased with the borrowed monies would generate proceeds (i.e., distributions) each month which would be greater than the costs associated with the loans and, as such, the strategy would pay for itself. The Respondent told the clients that the distributions must be reinvested so that these funds would be available to offset any future losses. The Respondent explained that should the distributions be insufficient to cover the interest costs on the loans, any difference would have to be covered by the clients out of their own pockets. The Respondent told the clients that the strategy was long term (a minimum of ten years) and explained that its success was dependent on market returns which could not be guaranteed.

19. The Respondent states that before the leverage was applied for, he met with both clients on multiple occasions to discuss in detail the use of leverage as an investment strategy.

20. The leverage investment strategy recommended by the Respondent was high risk and was acknowledged as such by both clients. The clients both executed forms acknowledging the risks associated with borrowing to invest. The mutual funds purchased pursuant to the strategy were not high risk.

21. Manulife assessed and approved the leverage strategy for both client JG and client VR. Manulife has offered compensation to both client JG and client VR.

Client JG

22. Client JG is 58 years old. He did not complete high school. He is a salesperson at a car dealership whose income is based upon sales commissions. Prior to 2011, client JG earned annual commissions ranging from $80,000 to $104,000.

23. In about 2002 or 2003, the Respondent met client JG at the car dealership when client JG sold a car to the Respondent. Client JG subsequently became a client of Manulife and his accounts were serviced by the Respondent.

24. Before October 2007, client JG had participated in two leverage strategies, both of which were successful.

25. In June 2007, the Respondent illustrated a leverage strategy to client JG after client JG asked about how he could accelerate his returns. In October 2007, client JG requested that the Respondent prepare the loan documents so that he could proceed with the leverage strategy. At the time the Respondent recommended this strategy, client JG had a net worth of $340,000.

26. In order to implement the leverage investment strategy, on or about October 11, 2007, client JG borrowed $100,000 from his Manulife One account. He then applied for a $200,000 2-for-1 investment loan from B2B Trust, using the monies he had borrowed from the Manulife One account as collateral for the B2B Trust loan.

27. The Respondent completed client JG's loan application to B2B Trust and presented it to client JG for him to sign. The loan application executed by client JG acknowledged that he had a "high" risk tolerance.

28. Based upon the Respondent's recommendation regarding the leverage investment strategy, client JG invested the $300,000 he had borrowed from his Manulife One account and from B2B Trust into mutual funds, including ROC mutual funds. Thereafter, as recommended by the Respondent, client JG reinvested the excess proceeds. In this regard, the Respondent states that client JG did not agree with the Respondent respecting the type of reinvestment. The Respondent states that in light of this, the Respondent suggested that perhaps it was best if client JG reverted to managing his own accounts. The Respondent states that shortly thereafter, client JG terminated his relationship with the Respondent.

29. The loans were unsuitable for client JG because client JG did not have the ability to withstand investment losses without jeopardizing his financial security if the leverage investment strategy did not perform as the Respondent represented it should.

Client VR

30. Client VR is 47 years old. He completed one year of university. He is employed by a retail company as a warehouse manager and handler.

31. In September 2007, the Respondent illustrated a leverage strategy to client VR. The Respondent states that he met with client VR on numerous occasions to discuss the leverage strategy.

32. At the time the Respondent recommended the leverage investment strategy, client VR had good investment knowledge. He had not previously borrowed monies to invest in leveraged mutual funds. Client VR had an income of approximately $56,600 per year and a net worth of approximately $192,400.

33. On about September 20, 2007, client VR borrowed $100,000 from his Manulife One account in order to implement the leverage investment strategy.

34. Client VR then applied for a $200,000 2-for-1 investment loan from B2B Trust, using the monies he had borrowed from the Manulife One account as collateral for the B2B Trust loan. The loan application executed by VR acknowledged that he had a “high” risk tolerance.

35. The loans were unsuitable for client VR. Client VR client VR did not have the ability to afford the monthly costs associated with the loans without relying on anticipated monthly proceeds from the investments. He also did not have the ability to withstand investment losses without jeopardizing his financial security if the leverage investment strategy did not perform as the Respondent represented it should.

Pre-signed Forms and Failure to Obtain Client Initials

36. Between February 2008 and February 2014, the Respondent obtained and maintained eight blank pre-signed account forms and five partially completed Order Entry Authorization forms. During the same period, the Respondent made changes to three account forms, at the request of the clients, but did not obtain the clients' initials beside the changes.

37. The account forms included Order Entry Authorizations, Know-Your-Client forms, Client Information Changes, Pre-authorized Contribution Forms, and Point of Sale Disclosures. The five partially completed pre-signed forms were Order Entry Authorizations in respect of nominee accounts in which no signature was required to effect a trade. The Respondent used these five forms to record the clients' verbal order entry authorizations. The Respondent acknowledges that the Order Entry Authorization forms were signed and dated with the sell instructions completed, but no purchase amounts were entered. The Respondent did not populate the purchase amounts because he was waiting for confirmation of the amounts the clients had available from the proceeds from placing the sell orders. After receiving the clients' initial order entry instructions, the Respondent would thereafter contact the clients with the current pricing and dollar amounts available for the purchase(s) discussed, proceed with the purchase instructions based on the clients' verbal instructions and then record the purchase amount on the pre-signed forms as a way to record the completed transaction(s).

38. In respect of the other eight forms, the Respondent states that he had no intention of using the forms and/or filling out the blank portions of the forms.

39. Manulife found these forms in April 2014 during a review of the client files maintained by the Respondent.

40. There is no evidence that the Respondent received any financial benefit from engaging in the conduct described above beyond the commissions and fees that he would ordinarily be entitled to receive. There is also no evidence of any client harm arising from the Respondent's conduct.

Failure to Abide by Member's Request

41. On March 28, 2014, Manulife met with the Respondent to discuss a complaint submitted by client JG against the Respondent. During the interview, the Respondent informed Manulife that he planned to contact clients to obtain their position on the complaint in order to counter the position taken by client JG. Manulife asked the Respondent not to contact any of his clients regarding this matter due to privacy concerns.

42. Notwithstanding Manulife's request, the Respondent contacted several clients to obtain letters regarding the Respondent's role in their investments in Sakha. Between March 30, 2014 and April 8, 2014, eight clients provided the Respondent with letters regarding the clients' dealings with the Respondent and their investments in Sakha.

43. The Respondent states that he contacted these clients in order to defend himself against client JG's allegations and that in doing so he acceded to Manulife's request respecting the protection of privacy as he never disclosed client JG's name or any other private information. Rather, he disclosed only that someone had placed a complaint against him that he was trying to defend.

The Respondent's Personal Background and Circumstances

44. This is the first time the Respondent has been the subject of a MFDA disciplinary hearing. The Respondent has cooperated with the MFDA's investigation into these issues. The Respondent states that since his departure from Manulife, the Respondent's income has dropped significantly and his family has suffered economic hardship. The Respondent states that he is the primary breadwinner in his household for his wife and four children.

Contraventions

45. The Respondent admits the following contraventions of the Rules, Policies and By-law of the MFDA:

a) between July 2008 and September 4, 2015, he engaged in securities related business that was not carried out for the account and through the facilities of the Member by facilitating the sale of shares of Sakha Enterprises Corporation totaling $248,133 to at least 10 clients and two other individuals contrary to MFDA Rules 1.1.1 and 2.1.1;

b) between October 2007 to September 4, 2015, he failed to ensure that the leveraged investment strategy recommendations for client JG and client VR were suitable for the clients having regard to their financial circumstances, including but not limited to, the clients' ability to afford the costs associated with the investment loans and withstand investment losses in the event that the investment strategy did not perform as the Respondent represented it should, contrary to MFDA Rules 2.2.1 and 2.1.1;

c) between February 2008 and February 2014, he obtained and maintained eight blank and five partially completed pre-signed account forms, and three account forms which the Respondent had made changes to after the clients had signed the account forms, at the request of the clients, but failed to obtain the clients' initials beside the changes, contrary to MFDA Rule 2.1.1;

d) between March 28, 2014 and April 8, 2014, he failed to abide by the Member's request to not make contact with clients in response to a client complaint, contrary to MFDA Policy No. 3 and MFDA Rule 2.11.

Analysis

46. The parties jointly proposed the following disposition in accordance with their settlement agreement:

(a) a one year prohibition on the authority of the Respondent to conduct securities related business in any capacity while in the employ of or associated with any MFDA Member, pursuant to section 24.1.1(e) of MFDA By-law No. 1;

(b) a fine in the amount of $45,000, pursuant to section 24.1.1(b) of MFDA By-law No. 1, payable as follows:

i. $10,000 payable on or before the date of the settlement hearing; and

ii. The balance of $35,000 payable in 7 monthly instalments of $5,000 each, commencing on January 9, 2017;

(c) costs in the amount of $5,000, pursuant to section 24.2 of MFDA By-law No. 1; and

(d) the Respondent shall in the future comply with MFDA Rules 1.1.1, 2.1.1, 2.2.1 and 2.11 and MFDA Policy No. 3;

47. Counsel advised us that the $10,000 first instalment respecting the proposed fine, and the $5,000 proposed costs had already been remitted to the MFDA, subject, of course, to our acceptance of the proposed terms of settlement.

48. We have instructed ourselves, as a matter of law, as to how to deal with settlement agreements. In the context of criminal proceedings, a joint submission as to penalty is not to be rejected by a trial judge unless the proposed disposition would bring the administration of justice into disrepute or otherwise be contrary to the public interest. The same high deference to joint submissions and settlement agreements exists within the administrative or regulatory context. That high level of deference advances the public interest by promoting certainty of disposition, encouraging full cooperation between the parties, and ultimately resulting in more efficient and timely hearings.

49. The assessment of penalty is discretionary. There can be a range of reasonable outcomes in each case. Where the proposed disposition, agreed upon by the parties, falls within the range of reasonable outcomes, the hearing panel should not decline to accept it simply because it might have favoured another reasonable disposition.

50. The Respondent's conduct, particularly when viewed cumulatively, was serious. It involved multiple breaches of the Rules over an extended period of time. Twelve investors, including ten clients, lost substantially all of the monies they invested in Sakha, although some

have received compensation from the Member. Because this securities related business was not carried out for the account and through the facilities of the Member, the Member had no opportunity to monitor this business or ensure compliance with the Rules. The Respondent failed to ensure that the leverage investment strategy recommendations for two clients were suitable for those clients. The unsuitability of leverage strategies for clients is a recurrent theme in various regulatory prosecutions. A strong message is required to deter similar misconduct. Similarly, pre-signed forms and the potential dangers associated with them have also figured prominently in prior hearing panel decisions.

51. On the other hand, the Respondent has never previously been the subject of MFDA disciplinary proceedings. He recognizes the seriousness of his misconduct, has accepted responsibility for it and obviated the need for a lengthy and costly hearing. He lost substantially all of the monies he invested in Sakha as well. We were presented with no evidence of dishonesty or deceit on the Respondent's part in his interactions with clients, which we sometimes see in cases involving unsuitable investment recommendations.

52. In our view, the proposed disposition falls within the range of reasonable outcomes available to us. Accordingly, we are prepared to accept it. It meets the ends of specific and general deterrence, sends the appropriate message to the profession and to the public as a whole, and takes into consideration all of the relevant principles that inform the imposition of penalty. These include, but are not limited to, the need to protect the public, and promote confidence in the industry, the markets and in existing enforcement processes.

53. In so concluding, we are mindful of the Ontario Securities Commission's refusal of reactivation of the Respondent's registration in September 2015 for at least one year. Enforcement Counsel advised us that the MFDA would have sought a longer period of prohibition than the period agreed upon if not for the action taken by the Commission. We agree that the Commission's order is properly considered by us in determining whether the one year prohibition is adequate. The cumulative effect of the Commission's order and the proposed disposition here (including a prohibition, fine and costs) serves the public interest.

Order

54. For these reasons, the Settlement Agreement was approved.

55. We are grateful to the parties for their assistance, most particularly their hard work in putting forward a joint position that is in the public interest.

DATED this 12th day of December, 2016.

"Mark J. Sandler"

Mark J. Sandler
Chair

"Kenneth P. Mann"

Kenneth P. Mann
Industry Representative

"Joseph Yassi"

Joseph Yassi
Industry Representative

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