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: Rhys William Douglas Martell

Heard: March 13 and April 30, 2018 in Vancouver, British Columbia
Reasons for Decision: October 29, 2018

REASONS FOR DECISION

Hearing Panel of the Pacific Regional Council:

Joseph A. Bernardo	Chair
Holly A. Millar	Industry Representative
Barbara E. Fraser	Industry Representative

Appearances:

Christopher Corsetti	)	Counsel for the Mutual Fund Dealers Association of Canada
Rhys Martell	)	Respondent, In person

1. On October 21, 2017, Staff of the Mutual Fund Dealer's Association of Canada ("MFDA") and Rhys Martell ("Respondent") entered into a settlement agreement ("Settlement Agreement").

2. On March 13, 2018, the Settlement Agreement was presented to the Hearing Panel for acceptance in closed session.

3. After hearing and considering the submissions of MFDA enforcement counsel and the Respondent, the Hearing Panel adjourned the Hearing in order to give the parties an opportunity to obtain and provide additional relevant information.

4. The Hearing resumed on April 30, 2018, whereupon the parties tendered additional facts by mutual consent and made further submissions in favour of the Settlement Agreement.

5. After reviewing the totality of the facts and submissions, the Hearing Panel approved the Settlement Agreement. These are our reasons.

Agreed Facts

6. In summary, the MFDA and Respondent agree as follows:

a) The Respondent has been registered in the securities industry since 2008.
b) Between January 22, 2008 and July 28, 2015, the Respondent was registered as a mutual fund salesperson in British Columbia and Alberta with Investors Group Financial Services Inc. ("IG"), a Member of the MFDA, and carried on business in Abbotsford, British Columbia.
c) At all material times, IG's policies and procedures prohibited Approved Persons from engaging in discretionary trading; required them to obtain oral confirmation of client trading instructions; and required them to document the details of client instructions, including the date and time of the confirmation discussion.
d) The Respondent's clients were invested in portfolios comprised entirely of IG proprietary mutual funds.

e) The Respondent adjusted or rebalanced the asset allocations within his clients' portfolio, either annually or in response to his view of market trends.

f) IG made an asset allocation software program available to its Approved Persons for the purpose of developing balanced portfolios for their clients.

g) Relying on the "know your client" information on file for a client, the program generated a report that identified the changes in IG mutual fund holdings that would be required to bring a portfolio's asset allocation into conformity with the client's investment profile. Once a report was produced, the Approved Person was required to discuss it with the client and obtain instructions before processing any transactions.

h) On August 1, 2012, the Respondent sent individual emails to 18 clients advising that he would rebalance their portfolios upon receiving their approval by email reply. In these emails, the Respondent did not identify the amount, mutual fund selection, or timing of the proposed changes.

i) On August 9, 2012 and relying on reports generated by the asset allocation program, the Respondent processed a total of 274 fund switches in 18 accounts with the agreement of his clients, but exercising his own discretion with respect to the amount, mutual fund selection and timing of each trade.

j) In November 2012, an IG branch audit disclosed that the Respondent had processed the 274 trades without maintaining client authorization records.

k) On February 5, 2013, the Respondent was told by his branch manager that he should not accept email trading instructions alone, and that emails to clients should include a statement that instructions received by email, fax, or text would not be processed before he had an opportunity to discuss them with the client.

l) On March 20, 2015, the Respondent sent emails to 86 clients advising that he intended to rebalance their portfolios and seeking their authorization to do so. The emails included the proviso that client trading instructions would need to be discussed, but failed to identify the amount, mutual fund selection, or timing of the proposed changes.

m) In April 2015 and relying on reports generated by the asset allocation program, the Respondent processed a total of 538 fund switches further to the general approvals

provided by 78 of the 86 clients, but exercising his own discretion with respect to the amount, mutual fund selection and timing of each trade and without maintaining client authorization records.

n) On April 9, 2015, an IG branch audit disclosed that the Respondent had processed the 538 trades without maintaining client authorization records.

o) On May 1, 2015, IG issued a warning letter to the Respondent and placed him under close supervision for a six month period while it investigated his March and April, 2015 conduct.

p) Sometime prior to July 23, 2015, the Respondent secured a position of future employment with Worldsource Financial Management Inc. ("Worldsource"), a Member of the MFDA.

q) Between July 23, 2015 and July 25, 2015, the Respondent changed the pre-authorized contribution terms for the accounts of 20 clients who intended to transfer their accounts to Worldsource, changing them from a deferred sales commission to a no load fee structure. The Respondent did not maintain written records of the client instructions.

r) On July 28, 2015, the Respondent resigned from IG and on August 5, 2015 became registered as a mutual fund salesperson (now known as a dealing representative) at Worldsource.

s) The Respondent did not discuss the tax consequences of the trades mentioned above with any of his clients; he did not believe it was necessary, as the switches occurred within registered accounts.

t) IG communicated with the clients whose accounts were the subject of the discretionary trading. It did not receive any complaints from the clients about the Respondent.

u) Since the mutual fund switches exclusively involved the disposition and acquisition of IG funds, the Respondent's clients did not incur any costs or fees as a result of the trades.

v) The Respondent did not earn any commissions or service fees from the switches or the amendments made to client contribution terms.

w) The Respondent remains registered as a dealing representative with Worldsource.

x) The Respondent does not have any prior disciplinary history.

Misconduct

7. The essential obligation of Approved Persons, as mandated by MFDA Rule 2.1.1, is to observe ethical standards and refrain from business conduct unbecoming or detrimental to the public interest.

8. Among other things, this Rule requires Approved Persons to be scrupulous in following the specific conduct requirements of other MFDA Rules that are relevant to them. In this case, they are:

a) Rule 2.3.1, which explicitly prohibits an Approved Person from engaging in discretionary trading;
b) Rules 1.1.2 and 2.5.1, which obligates an Approved Person to follow the supervisory policies and procedures of the employing Member firm; and
c) Rule 5.1(b), which requires Approved Persons to record and maintain evidence of client trade instructions.

9. In the Settlement Agreement the facts establish, and the Respondent admits, that:

"a) between August 2012 and April 2015, the Respondent processed transactions in the accounts of clients, without obtaining client instructions in respect of the amount of the transaction, the mutual fund being purchase[d] or sold, or timing of the transactions, thereby engaging in discretionary trading, contrary to MFDA Rules 2.3.1 and 2.1.1; and
b) between July 23, 2015 and July 25, 2015, the Respondent failed to record and maintain evidence of client trade instructions with respect to transactions in client accounts, contrary to the Member's policies and procedures, and MFDA Rules 1.1.2, 2.5.1, 2.1.1, and 5.1(b)."

Standard

10. Settlement agreements are integral to effective securities regulation because they enable the efficient allocation of limited enforcement resources.

11. Settlements are also summary descriptions of misconduct developed by litigants opposed in interest, namely, the persons most familiar with the facts and most motivated to weigh their significance critically. When reviewing a settlement agreement, therefore, a hearing panel must be mindful that the factual record has been deliberately limited for the sake of eliminating controversy, while the proposed outcome was negotiated on the basis of a more complete understanding of the circumstances.

> *British Columbia Securities Commission v. Seifert*, 2007 BCCA 484 at paras. 26 and 31.

12. Section 24.4.3 of MFDA By-Law No. 1 reflects this practical reality by conferring only a narrow discretion on settlement hearing panels. A settlement hearing panel is not asked to decide whether it would itself order the same outcome on the same facts, but only whether the settlement agreement as presented should be accepted or rejected.

13. Moreover, the overwhelming consensus view emerging from previous decisions is that a hearing panel should accept a settlement agreement "unless it views the penalty as clearly falling outside a reasonable range of appropriateness."

> *Sterling Mutuals Inc. (Re)*, 2008 MFDA 16, at para. 37, citing the reasoning in Milewski (Re), [1999] I.D.A.C.D. No. 17 at p. 11, Ontario District Council Decision dated July 28, 1999.

14. Another way of saying the same thing is that it is incumbent on a hearing panel to accept a settlement agreement unless, in its reasonable judgment, the proposed penalty is clearly inappropriate.

Decision

15. The Settlement Agreement proposes the following penalties:

a) one month suspension;
b) $30,000 fine; and
c) $2,500 costs.

16. In assessing the appropriateness of these sanctions, the essential issue is whether, in light of the Respondent's repeated misconduct, they provide sufficient specific deterrence.

17. The fact that the rebalancing of client portfolios was limited to making switches between IG funds is significant in this regard. This meant that clients did not incur service charges from the asset reallocations and, it follows, the Respondent could not derive commissions or fees from them.

18. The Respondent's discretionary trading was indisputably a reflection of a poor understanding of his professional obligations. The Settlement Agreement does not explain why the Respondent repeated this misconduct despite being warned, but there is no basis for concluding it was motivated by financial gain.

19. The Respondent has no prior disciplinary history, and since the final misconduct episode in 2015 he has continued in the industry without any further problems being reported.

20. Enforcement counsel directed the Hearing Panel's attention to a range of previous settlement decisions involving similar misconduct. The penalties proposed in the Settlement Agreement fall squarely within the range of sanctions ordered in three recent discretionary trading decisions. In two of those cases, the respondents repeated the misconduct after being warned against it; in all three cases, the discretionary trading was compounded by other infractions, an aggravating feature absent in the present case.

Re James Gerard Carney, MFDA File No. 201646, May 9, 2017
Re Robert Stephen Mitchell, MFDA File No. 201689, June 23, 2017

21. Taking into account the facts as disclosed and the penalties ordered in relevant recent cases, the Hearing Panel concluded that the penalties agreed upon by the parties do not fall outside the reasonable range of appropriateness.

DATED this 29th day of October, 2018.

"Joseph A. Bernardo"
Joseph A. Bernardo
Chair

"Holly A. Millar"
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Industry Representative

"Barbara E. Fraser"
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Industry Representative

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