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

IN THE MATTER OF A DISCIPLINARY HEARING

PURSUANT TO SECTIONS 20 AND 24 OF BY-LAW NO. 1

OF THE MUTUAL FUND DEARLERS ASSOCIATION OF CANADA

Re: Kerry Scharfenberg

Heard: January 6, 2009 – Edmonton, Alberta
Panel Decision: March 9, 2009

DECISION AND REASONS

Hearing Panel of the Prairie Regional Council:

Garrett Wilson, Q.C.	Chair
M.E. (Elaine) Bradley	Industry Representative
Erwin Granson	Industry Representative

Appearances:

Kara L. Beitel	)	For the Mutual Fund Dealers Association
	)	of Canada
Kerry Scharfenberg	)	Not in attendance personally or represented
	)	by Counsel

1. Kerry Scharfenberg (“Scharfenberg”) was employed from 1998 to August 21, 2006 as a mutual fund salesperson by Investors Group Financial Services Inc. (“Investors Group”) and was registered as such in the province of Alberta. On and after February 8, 2002, the date upon which Investors Group became a Member of the MFDA, Scharfenberg became an Approved Person subject to the By-laws, Rules and oversight of the Mutual Fund Dealers Association of Canada (“MFDA”).

2. On August 21, 2006, Scharfenberg was terminated by Investors Group following an investigation into his handling of certain client accounts.

3. On July 4, 2008, Scharfenberg was personally served with a Notice of Hearing issued by MFDA under the authority of its By-laws alleging that Scharfenberg had violated Rules of the MFDA as specified in the said Notice of Hearing.

4. The Notice of Hearing clearly stated that it was returnable, and would be first considered by a Hearing Panel meeting by teleconference, at the offices of the MFDA in Calgary, Alberta, on Friday, September 19, 2008, at 10:00 a.m. It further stated that Scharfenberg, as the Respondent named in the said Notice of Hearing, should file with the MFDA and its enforcement counsel, either in written form or electronically, a Reply to the Allegations within twenty days of service of the said Notice of Hearing.

5. No Reply to the Notice of Hearing was filed by Scharfenberg or anyone on his behalf, within the said time limit, or at all.

6. This Hearing Panel, designated and authorized in accordance with the provisions of Section 19.9 of By-Law No. 1 of the MFDA, met by teleconference on Friday, September 19, 2008, at the MFDA offices in Calgary, Alberta, the time and place specified in the said Notice of Hearing. Proof of personal service upon Scharfenberg of the Notice of Hearing on July 4, 2008, in the form of the Affidavit of Rod Foster, sworn on July 7, 2008, was presented to the Hearing Panel which noted Rule 13.4(1) of the Rules of Procedure of the MFDA. That Rule provides as follows:

(1) The Hearing Panel may allow the evidence of a witness or proof of a particular fact or

document to be given by sworn statement unless an adverse party reasonably requires the attendance of the witness at the hearing for cross-examination.

7. The Hearing Panel accepted the Notice of Hearing and the said Affidavit of Rod Foster, which were filed as Exhibits 1 and 2 respectively, and determined that service of the Notice of Hearing had been personally effected upon Scharfenberg in accordance with the requirements of Rule 4 of the Rules of Procedure.

8. Scharfenberg did not appear on September 19, 2008, nor did anyone on his behalf. At its teleconference meeting on that date, this Hearing Panel made the following order:

> "The hearing on the merits in this matter shall take place before a Hearing Panel of the Prairie Regional Council at the Fairmont Hotel MacDonald, 10065 – 100th Street, Edmonton, Alberta on Tuesday, January 6, 2009, at 10:00 a.m. (Alberta) or as soon thereafter as the hearing can be held."

9. On January 6, 2009, this Hearing Panel met in person in the Jasper Room of the Fairmont Hotel MacDonald at 10:00 a.m. Scharfenberg did not appear in person, or by counsel or agent.

10. The MFDA was represented by counsel, Kara L. Beitel.

11. In response to inquiry from the Hearing Panel, Ms. Beitel advised that no further service of process or notice had been effected upon Scharfenberg, but that the Hearing Panel's Order of September 19, 2008, had been publicized by inclusion on the MFDA website and by issue of a News Release advising of the time and place set for the hearing.

12. The Hearing Panel addressed Rule 7.3 of the Rules of Procedure, which provides as follows:

> (1) Where a Respondent fails to attend the hearing on the date and at the time and location specified in the Notice of Hearing, the Hearing Panel may:
>
> (a) proceed with the hearing without further notice to and in the absence of the Respondent; and
>
> (b) accept the facts alleged and conclusions drawn by the Corporation in the Notice of Hearing as proven and impose any of the penalties and costs described in sections 24.1 and 24.2 respectively of MFDA By-law No. 1.

13. The nature and extent of the Allegations and Particulars contained in the Notice of Hearing are, in the opinion of the Hearing Panel, serious in the extreme. They are set out in full as follows:

> **NOTICE** is further given that staff of the MFDA alleges the following violations of the By-laws, Rules or Policies of the MFDA:
>
> **Allegation #1:** Between February 8, 2002 and August 2006, the Respondent misappropriated approximately $332,155 from 6 clients, thereby failing to deal fairly, honestly and in good faith with the clients, contrary to MFDA Rule 2.1.1.
>
> **Allegation #2:** Between February 8, 2002 and August 2006, the Respondent processed transactions in the accounts of clients without their instructions, knowledge or authorization, contrary to MFDA Rule 2.1.1.
>
> **PARTICULARS**
>
> **NOTICE** is further given that the following is a summary of the facts intended and alleged to be relied upon by the MFDA at the hearing:
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> ***Registration History***
>
> 1. From 1998 to August 21, 2006, the Respondent was registered in Alberta as a mutual fund salesperson with Investors Group Financial Services Inc. ("IG").
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> 2. The Respondent was terminated by IG on August 21, 2006 as a result of the events described herein. The Respondent is no longer registered in the securities industry in any capacity.
>
> 3. IG has been a Member of the MFDA since February 8, 2002.
>
> **Allegation #1**
>
> 4. Between February 8, 2002 and August 2006, the Respondent misappropriated approximately $332,155 from 6 clients, as more particularly described below.
>
> ***Clients AJ and JJ***
>
> 5. AJ and JJ were husband and wife and clients of IG. The Respondent was the mutual fund salesperson responsible for their account. Between February 8, 2002 and September 2004, the Respondent misappropriated $133,824 from AJ's and JJ's joint account. None of the events and transactions described below were known to or approved by AJ, JJ or the other clients whose accounts were utilized by the Respondent to carry out the misappropriations.
>
> 6. On October 9, 2001, the Respondent sent an email to IG's Customer Service Department requesting that the address on AJ's and JJ's account be changed to PO Box 360, Lac La Biche, Alberta, T0A 2C0.

7. On the same date, the Respondent sent an email to IG's National Call Centre requesting that account statements for AJ and JJ be sent to PO Box 1857, Cold Lake, Alberta, T9M 1P4 ("PO Box 1857"). PO Box 1857 was controlled by the Respondent.

8. On November 5, 2001, the Respondent sent a second email to IG's Customer Service Department requesting that the address on AJ's and JJ's account be changed again, this time to PO Box 1857.

9. On January 16, 2002, the Respondent sent an Interfund Transfer - Email Transfer request to IG requesting that $8,000 be transferred from AJ's and JJ's joint account to the account of client PL.[1]

10. On April 25, 2002, the Respondent sent an email to IG's Customer Service Department requesting that AJ's and JJ's phone number be changed in IG's records to (780) 812-1897, the Respondent's cell phone number.

11. On April 29, 2002, the Respondent sent an Interfund Transfer - Email Transfer request to IG requesting that $17,000 be transferred from AJ's and JJ's joint account to the account of client LB.

12. On February 13, 2003, the Respondent sent an Interfund Transfer - Email Transfer request to IG requesting that $5,200 be transferred from AJ's and JJ's joint account to the account of client GH.

13. On February 26, 2003, the Respondent sent an Interfund Transfer - Email Transfer request to IG requesting that $1,500 be transferred from AJ's and JJ's joint account to the account of client PM.

14. On March 3, 2003, the Respondent sent an investment application form to IG requesting that a new money market chequing account be opened for AJ and JJ. Neither AJ nor JJ were aware of or authorized the opening of this account. Their signatures on the account application form were forged. The phone number and address on the money market account cheques were the phone number of the Respondent and the address of a PO Box controlled by him. After the money market account was opened, the Respondent processed transfers of amounts in AJ's and JJ's joint account to the money market account.

15. Between April 29, 2003 and September 17, 2004, the Respondent wrote 28 cheques totalling $130,124.24 on AJ's and JJ's money market account without their knowledge or authorization, thereby misappropriating the monies. The majority of these cheques were deposited in the bank account of Betty Scharfenberg, the Respondent's wife.

[1] The Respondent did not become subject to the jurisdiction of the MFDA until IG became a Member of the MFDA on February 8, 2002. In this Notice of Hearing, descriptions of amounts misappropriated by the Respondent before February 8, 2002 have been included because they form part of the sequence of events but the amount of such transactions have not been included in the calculation of the total amount alleged to have been misappropriated by the Respondent.

16. On September 10, 2004, the Respondent processed a transfer of $20,000 from the account of client SB into AJ's and JJ's joint account.

17. On September 15, 2004, the Respondent wrote his final cheque on AJ's and JJ's money market account, 10 days prior to beginning similar activity in the account of client SB, as described in the "Client SB" section below.

18. Between October 2001 and September 2004, the account statements and portfolio summaries generated by IG for the accounts of AJ and JJ were sent to PO Box 1857, controlled by the Respondent. The Respondent provided AJ and JJ with fraudulent account statements and portfolio summaries he created in order to conceal the change of address for their accounts, the opening of the money market account and his misappropriations of monies in their accounts.

19. On September 30, 2001, prior to the Respondent's initial address change for AJ's and JJ's account, their account was valued at $131,496.49. On September 30, 2004, their account was valued at $793.72.

20. The following chart summarizes the amounts misappropriated by the Respondent from the account of AJ and JJ:

Misappropriation Summary for Clients AJ and JJ	**Amount**
Misappropriated by unauthorized cheques written on clients' account	$ 130,124.24
Misappropriated by unauthorized transfers from clients' account	$ 23,700.00
Replaced by unauthorized transfers to clients' account	$ 20,000.00
Net amount misappropriated from clients	**$ 133,824.24**

Client SB

21. SB was a client of IG. The Respondent was the mutual fund salesperson responsible for SB's account. Between September 2004 and August 2006, the Respondent misappropriated $141,670 from SB's account. None of the events and transactions described below were known to or approved by SB or the other clients whose accounts were utilized by the Respondent to carry out the misappropriations.

22. On August 24, 2004, the Respondent sent an email to IG's Customer Service Department requesting that the address on SB's account be changed to PO Box 157, Cold Lake, Alberta, TM9 1P1 ("PO Box 157"). PO Box 157 was controlled by the Respondent.

23. On September 1, 2004, the Respondent sent IG an investment application form requesting that a new money market chequing account be opened for SB. SB was not aware of and did not authorize the opening of this account. SB's signature on the

investment application form was forged. After the money market account was opened, the Respondent processed transfers of amounts in SB's investment account to the money market account.

24. On September 10, 2004, the Respondent processed a transfer of $20,000 from SB's account to the account of clients AJ and JJ.[2] The instructions on the transfer form stated "Transfer funds to sister's account in IG". SB is not the sister of AJ or JJ. SB's signature on the transfer form was forged.

25. Between September 2004 and August 2006, the Respondent wrote 70 cheques totalling $189,653 on SB's money market account without SB's knowledge or authorization. All of the cheques were deposited in the bank account of Betty Scharfenberg, the Respondent's wife. The phone number and address on the cheques were the phone number of the Respondent and the address of a PO Box controlled by him.

26. On November 29, 2005, the Respondent processed a transfer of $20,000 from the account of client and brother-in-law HS to SB's account. The instructions on the transfer form stated "Transfer to Mothers Acct". SB is not the mother of HS.

27. On April 25, 2006, the Respondent processed a transfer of $20,000 from the account of client OG to SB's account.

28. On May 25, 2006, the Respondent transferred an additional $20,000 from OG's account to SB's account.

29. On August 10, 2006, the Respondent processed a transfer of $6,000 from the account of client PD to SB's account.

30. Between September 2004 and August 2006, the account statements and portfolio summaries generated by IG for SB's accounts were sent to PO Box 157, controlled by the Respondent. The Respondent provided SB with fraudulent account statements and portfolio summaries he created in order to conceal the change of address for SB's accounts, the opening of the money market account and his misappropriations of monies in SB's accounts.

31. On June 30, 2004, prior to the Respondent's initial address change for SB's account, SB's portfolio was valued at $250,805.75. By June 30, 2006, the portfolio was valued at $109,757.81. The fraudulent June 30, 2006 statement provided to SB by the Respondent valued her portfolio at $263,850.59.

32. The following chart summarizes the amounts misappropriated by the Respondent from the account of SB:

[2] This transaction is the same one as described in paragraph 16. Throughout this Notice of Hearing, there are numerous other instances in which it is alleged the Respondent transferred monies between the accounts of clients, such that the same transaction is described in different sections of the Notice of Hearing. These transactions are too numerous to cross-reference individually but may be identified by their identical date.

Misappropriation Summary for Client SB	Amount
Misappropriated by unauthorized cheques written on client's account	$ 189,653.00
Misappropriated by unauthorized transfers from client's account	$ 20,000.00
Replaced by unauthorized transfers to client's account	$ 66,000.00
Net amount misappropriated from client	**$ 143,653.00**

Client AL

33. AL was a client of IG. The Respondent was the mutual fund salesperson responsible for AL's accounts. Between January 15, 2001 and February 15, 2004, AL provided the Respondent with eight cheques totalling $17,273.59 for deposit in his money market chequing account.[3]

34. The Respondent directed AL to make all of the cheques payable to the Respondent personally. The Respondent deposited all of the cheques into a bank account controlled by the Respondent, thereby misappropriating the funds. The amount misappropriated by the Respondent from AL after February 8, 2002 was $8,677.59.

35. The Respondent concealed the misappropriations by processing unauthorized redemptions from AL's RRSP account[4] and using the proceeds to fulfill AL's requests for withdrawals from his money market account.

Client OG

36. OG was a client of IG. The Respondent was the mutual fund salesperson responsible for her account. Between April 2006 and July 2006, the Respondent misappropriated $40,000 from OG's accounts. None of the events and transactions described below were known to or approved by OG or the other client, SB, whose account was utilized by the Respondent to carry out the misappropriations.

37. On April 25, 2006, the Respondent processed a transfer of $20,000 from OG's account to the account of client SB.

38. On May 25, 2006, the Respondent processed a transfer of an additional $20,000 from OG's account to the account of client SB.

39. As described in the "Client SB" section above, after the Respondent had transferred the funds from OG's account to SB's account, the Respondent wrote cheques

[3] Four of these cheques, totalling $8,596, preceded the date of the MFDA's jurisdiction, February 8, 2002 and therefore have not been included in the total amount alleged to have been misappropriated by the Respondent. See Note 1.
[4] These redemptions had tax consequences for AL for which he was subsequently compensated.

on SB's money market account and deposited them in bank accounts under his control, thereby completing his misappropriation of OG's monies.

40. The following chart summarizes the amounts misappropriated by the Respondent from the account of OG:

Misappropriation Summary for Client OG	**Amount**
Misappropriated by transfers from client's account	$ 40,000.00
Net amount misappropriated from client	**$ 40,000.00**

Client PD

41. PD was a client of the Respondent. In 2006, the Respondent misappropriated $6,000 from the account of PD.

42. On August 10, 2006, the Respondent processed a transfer of $6,000 from PD's account to the account of client SB.

43. As described in the "Client SB" section above, after the Respondent had transferred the funds from PD's account to SB's account, the Respondent wrote cheques on SB's money market account and deposited them in bank accounts under his control, thereby completing his misappropriation of PD's monies.

44. On October 4, 2006 (after the Respondent's termination), IG received a letter purporting to be from PD with a bank draft for $6,000 and instructions to deposit the monies into PD's account. PD did not write the letter.

45. The following chart summarizes the amounts misappropriated by the Respondent from the account of PD:

Misappropriation Summary for Client PD	**Amount**
Misappropriated by transfer from client's account	$ 6,000.00
Replaced by Respondent	$ 6,000.00
Net amount misappropriated from client	**$ 0.00**

Clients IS and RS – The Respondent's conduct is detected

46. IS and RS were clients of IG. IS is the mother of RS. The Respondent was the mutual fund salesperson for their accounts.

47. On October 27, 2005, IS instructed the Respondent to open an account for RS and provided the Respondent with a cheque in the amount of $1,000 to deposit in the account. The Respondent did not set up an account for RS.

48. On December 28, 2005, the Respondent sent an email to IG's Client Services Department requesting that the address on IS's account be changed to PO Box 157.

49. On June 30, 2006, the Respondent sent an email to IG's Client Services Department requesting that the address on IS's account be changed to PO Box 1857.

50. On July 21, 2006, as a result of the request to change the address on IS's account, IG's Audit Department sent an address verification letter to IS.

51. On July 26, 2006, the Respondent opened an account for RS using the address of PO Box 1857 and deposited $1,025 into the account by way of a money order.

52. Between the date that IS instructed the Respondent to open an account for RS and the date the account was opened, the Respondent provided IS with fraudulent account statements he had created in order to make it appear as though he had opened an account for RS and deposited the $1,000 cheque originally provided to him by IS.

53. In response to the letter from the IG Internal Audit Department, IS advised IG that she had concerns with RS's account. IG's Internal Audit Deparment conducted a review and testing of activity in the accounts of clients serviced by the Respondent, resulting in his termination on August 21, 2006.

54. Following the termination of the Respondent, IG has paid affected clients compensation in the total amount of $471,656, including forgone growth on their investments.

Summary

55. Between February 8, 2002 and August 21, 2006, the Respondent misappropriated approximately $332,155 from 6 clients, thereby failing to deal fairly, honestly and in good faith with the clients, contrary to MFDA Rule 2.1.1.

Allegation #2

56. Between February 8, 2002 and August 2006, the Respondent processed transactions in the accounts of clients without their instructions, knowledge or authorization, contrary to MFDA Rule 2.1.1. The Respondent engaged in this activity in order to conceal:

(i) transactions whereby he misappropriated monies from, and returned monies to, client accounts; and
(ii) his failure to carry out instructions and requests received from clients.

57. The Respondent carried out the following unauthorized transactions:

(a) Unauthorized transfers between client accounts:

Date	From Account	Amount Transferred	To Account
29-Apr-02	AJ/JJ	$17,000.00	LB
13-Feb-03	AJ/JJ	$5,200.00	GH

26-Feb-03	AJ/JJ	$1,500.00	PM
10-Sep-04	SB	$20,000.00	AJ/JJ
25-Apr-06	OG	$20,000.00	SB
25-May-06	OG	$20,000.00	SB
10-Aug-06	PD	$6,000.00	SB

(b) Unauthorized new account openings: the Respondent submitted investment application forms to open money market accounts for clients AJ and JJ, and SB and then transferred funds from their respective investment accounts to the money market accounts, all without their knowledge or authorization;

(c) Forged cheques: the Respondent forged client signatures on 98 cheques drawn on the money market accounts referred to in (c) above; and

(d) Failure to follow client instructions: the Respondent opened an RESP account for client JL four years after being instructed to do so and an investment account for client RS one year after being instructed to do so, without their knowledge or authorization.

14. Ms. Beitel advised that it was her position "because the Respondent has failed to attend and has failed to serve any reply, that all of the allegations in the Notice of Hearing can be taken as proven."

15. The Hearing Panel agreed, the Chair stating, "We will accept the Notice of Hearing and the allegations therein as now proven, in the absence of Mr. Scharfenberg or any representation on his behalf."

16. Ms. Beitel tendered in evidence the Affidavit of Harold Eric Wenzel, sworn December 17, 2008 to which was appended a large number of exhibits. Mr. Wenzel is an investigator with MFDA and had carried out an extensive investigation of the conduct of Scharfenberg in respect to the clients identified in the Notice of Hearing.

17. Pursuant to the authority of Rule 13.4(1), the Hearing Panel accepted the Affidavit as Exhibit 3. At the request of Ms. Beitel, and to ensure the anonymity of the clients whose affairs were exposed in the exhibits, all the exhibits to the said Affidavit were marked separately as Exhibit 4 and marked "confidential."

18. The Notice of Hearing charges Scharfenberg with two violations of MFDA Rule 2.1.1, which provides as follows:

> **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.

19. The Notice of Hearing does not refer to Scharfenberg as an "Approved Person of a Member" and neither does the Affidavit of Mr. Wenzel. "Approved Person" is defined in Section 1 of By-law No. 1 of the MFDA as follows:

> "Approved Person" means, in respect of a Member, an individual who is a partner, director, officer, compliance officer, branch manager, or alternative branch manager, employee or agent of the Member who conducts or participates in the dealer business of the Member and who: (i) is registered, licensed or approved in the appropriate category, where required by applicable securities legislation, by the securities commission having jurisdiction, and (ii) is designated and qualified as such in accordance with the Rules, or (iii) is otherwise subject to the jurisdiction of the Corporation;

20. Both the Notice of Hearing, the facts alleged in which are now accepted by us, and the Affidavit of Mr. Wenzel, state that Scharfenberg was "registered in Alberta as a mutual fund salesperson with IG" from 1998 to August 21, 2006. IG became a Member of MFDA on February 8, 2002.

21. We have no hesitation in finding that Scharfenberg was an "employee or agent" of IG on February 8, 2002, and that, upon IG becoming a Member of IG at that date, Scharfenberg became an Approved Person, was such at all times material to the matter before us, and is subject to the jurisdiction of the MFDA. We note, as was pointed out to us by Ms. Beitel, the provisions of Section 24.1.4 of By-law No. 1 of the MFDA:

> 24.1.4 *Jurisdiction*
>
> (a) *Former Members.* For the purposes of Sections 20 to 24 inclusive, any Member,

> Approved Person or other person subject to the jurisdiction of the Corporation shall remain subject to the jurisdiction of the Corporation notwithstanding that such Member has ceased to be a Member, Approved Person or other person subject to the jurisdiction of the Corporation.

22. The section is not as clear as it might be, but we accept it as providing that the jurisdiction of MFDA over Scharfenberg continues in spite of the fact that he was dismissed as an employee of IG on August 21, 2006 as stated by both the Notice of Hearing and the Affidavit of Mr. Wenzel.

23. Specifically, Allegation #1 in the Notice of Hearing charges that Scharfenberg "misappropriated" monies from his clients "thereby failing to deal fairly, honestly and in good faith with the clients." This is clearly a reference to the actual wording of subsection (a) of Rule 2.1.1.

24. Allegation #2 charges that Scharfenberg "processed transactions in the accounts of clients without their instructions, knowledge or authorization." Here no reference is made to any one of the four subsections of Rule 2.1.1.

25. Having accepted "the facts alleged and conclusions drawn" in the Notice of Hearing, pursuant to Rule 7.3, we do not propose to add to the 57 paragraphs of narrative contained therein. In considering the application of those facts and conclusions to Rule 2.1.1 we find it unnecessary to delve into esoteric interpretations of the words employed in the Rule. Their plain and ordinary meaning is more than sufficient in the light of the described conduct Scharfenberg has impliedly acknowledged by his failure to reply to the Notice of Hearing, or in any way participate in these proceedings. Those 57 paragraphs accuse Scharfenberg of behaviour that constitutes forgery, misappropriation of client funds, fraud, deceit and concealment, all of which is clearly in violation of any interpretation or application of Rule 2.1.1.

26. Unhesitatingly, we find that by his conduct, Scharfenberg clearly violated subsection (a) of Rule 2.1.1 as charged in Allegation #1, and also subsections (b) and (c) of the said Rule. Allegation #1 is fully made out.

27. As noted, Allegation #2 does not refer specifically to any subsection of Rule 2.1.1, but we find that for an Approved Person to "process transactions in the accounts of clients without their instruction, knowledge or authorization" is a contravention of the requirement to "deal fairly, honestly and in good faith" with said clients, particularly when the transactions are designed to benefit the Approved Person and are contrary to the interests of the clients. Similarly, we find such conduct to be in contravention of subsections (b) and (c) of Rule 2.1.1.

28. Allegation #2 is also fully made out.

PENALTY

29. The authority of a Hearing Panel to impose a penalty for infractions is found in Section 24 of By-law No. 1 of the MFDA, which provides as follows:

> 24.1.1 *Approved Persons*
>
> A Hearing Panel of the applicable Regional Council shall have power to impose upon an Approved Person or any other person under the jurisdiction of the Corporation any one or more of the following penalties:
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> (a) a reprimand;
>
> (b) a fine not exceeding the greater of:
>
> (i) $5,000,000.00 per offence, and
>
> (ii) an amount equal to three times the profit obtained or loss avoided by such person as a result of committing the violation;
>
> (c) suspension of the authority of the person to conduct securities related business for such period and upon such terms as the Hearing Panel may determine;
>
> (d) revocation of the authority of the person to conduct securities related business in any capacity for any period of time;
>
> (e) prohibition of the authority of the person to conduct securities related business in any capacity for any period of time;
>
> (f) such conditions of authority to conduct securities related business as may be considered appropriate by the Hearing Panel;

if, in the opinion of the Hearing Panel, the person:

(g) has failed to carry out any agreement with the Corporation;

(h) has failed to comply with or carry out the provisions of any federal or provincial statute relating to the business of the Member or of any regulation or policy made pursuant thereto;

(i) has failed to comply with the provisions of any By-law, Rule or Policy of the Corporation;

(j) has engaged in any business conduct or practice which such Regional Council in its discretion considers unbecoming or not in the public interest; or

(k) is otherwise not qualified whether by integrity, solvency, training or experience.

30. Previous discipline tribunals in the investment industry have established a number of factors to be considered when assessing penalty. Some of these are:

(a) the protection of the investing public;
(b) the integrity of the securities market;
(c) specific and general deterrence;
(d) the protection of the governing body's membership; and
(e) the protection of the integrity of the governing body's enforcement processes.

(See: *In The Matter of Arnold Tonnies,* Hearing Panel of the Prairie Regional Council, MFDA, Panel Decision dated June 27, 2005. p. 22.)

31. On occasion these factors have been judicially reviewed and approved, most recently by the British Columbia Court of Appeal which considered (because of a jurisdiction problem) the appropriateness of general deterrence. *Thow* v. *B.C. Securities Commission,* (2009) BCCA 46.

32. This Hearing Panel considers deterrence to be the primary feature of any penalty tailored to best suit the circumstances of the case before us.

33. The B.C. Court of Appeal quoted the Supreme Court of Canada in a 2004 decision, an

appeal from the B.C. Court: *Re Cartway Resources Corp.* (2004) 1 S.C.R. 672.

> "…it is reasonable to view general deterrence as an appropriate, and perhaps, necessary, consideration in making orders that are both protective and preventative…the notion of general deterrence is neither punitive nor remedial. A penalty that is meant to generally deter is a penalty designed to discourage or hinder like behaviour in others."

34. The Court of Appeal then approved a number of principles applicable to sentences in investment securities discipline matters, as follows, (with some paraphrasing):

- the paramount objective (of the legislation) is to protect the public and ensure public confidence in our markets.
- the (legislation) is designed to discourage detrimental forms of commercial behaviour.
- the purpose of the…public interest jurisdiction is not punitive; it is protective and preventative – (discipline) orders are prospective in their orientation, used to prevent likely future harm to capital markets.
- this interpretation is consistent with regulatory legislation in general, "whose focus is on the protection of societal interests, not punishment of an individual's moral faults."
- general deterrence is an appropriate factor in formulating an administrative penalty…in the public interest; it falls squarely within the public interest jurisdiction…to maintain investor confidence in the capital markets.
- the deterrence, both specific and general, associated with an order made…is prospective in orientation and aimed at preventing future conduct.

35. Scharfenberg engaged in a deliberate, cunning campaign of deceit, fraud and forgery designed to drain funds from the accounts of six clients for his personal use and benefit. We note that this dishonest conduct extended over a period of nearly five years until it was detected and terminated by his dismissal. We note also that Scharfenberg initiated this misappropriation with the account of a husband and wife who were at the time 85 and 69 years of age and converted to his own control and benefit a total of $153,824.24 of their funds.

36. It should be noted that in the course of his machinations Scharfenberg forged signatures to a total of 98 cheques drawn on his clients' money market accounts (Notice of Hearing, paragraph 57 (c); Wenzel Affidavit, Exhibit 3, paragraph 76). A number of other forgeries were committed on various account authorizations. The seriousness of just this aspect of the entire campaign of dishonesty cannot be overemphasized.

37. Scharfenberg misappropriated a total of $409,477.24, some of which was replaced,

mostly from the accounts of the affected clients as he carried out a form of shell game, moving funds between accounts without authority. The MFDA calculates the total net defalcation at $332,155.00. Scharfenberg's employer was obliged to reimburse these monies, including lost income, for a total compensation of $471,656.00.

38. Allegation #2 relates to the unauthorized transfers between client accounts perpetrated by Scharfenberg as he attempted to conceal his misappropriations. These transfers totalled $89,700.00.

39. Scharfenberg's conduct was callous and deliberate. He intentionally deprived his clients of monies that he turned to his own use and benefit, and did so without apparent concern for the hurt and harm he thus caused. He not only disgraced himself, he also brought disrepute to his employer and to the industry.

40. We see no mitigating factors here. Scharfenberg had no previous disciplinary history, but that undoubtedly was a feature that contributed to his ability to carry out such an infamous breach of the trust that had been placed in him. He made no attempt to assist in the investigation of his conduct, made no reply to the Notice of Hearing, and has shunned this hearing. He has not disgorged any of the funds he converted to his benefit. He has made no apology nor shown any contrition in even the slightest way.

41. The investment industry, and certainly the mutual fund segment of that industry, is built, predicated and dependent upon trust. The public must be assured and confident that the representatives of that industry are worthy of trust, that they are persons of integrity and honour.

42. This Hearing Panel has determined to impose a penalty that will signal to the public that breaches of trust and contraventions of the MFDA regulations are treated with deserving severity and that will, to the extent possible, deter others from such conduct in the future.

43. We have reviewed a number of authorities and decisions of previous disciplinary panels that have considered the question of the appropriate penalties in similar cases. We consider that it is not appropriate to fix a fine that bears closely to the total defalcation as it smacks of recovery,

or enforced disgorgement.

44. As authorized by By-law No. 1, Section 24.1.1.(c), we order that Kerry Scharfenberg be permanently prohibited from conducting securities related business while in the employ of or associated with any MFDA Member, pursuant to MFDA By-law No. 1, Section 24.1.1(e).

45. With respect to Allegation #1, we impose a fine of $400,000.00.

46. With respect to Allegation #2, we impose a fine of $100,000.00.

47. We consider a total fine of $500,000.00 to be appropriate to the misconduct established, and have allocated that total between Allegations #1 and #2 out of an abundance of caution and with reference to the seriousness of the defalcations that fell within each Allegation.

48. Ms. Beitel proposed that costs be paid by Scharfenberg in the amount of $7,500.00. We noted from a review of previous decisions that $7,500.00 appeared to be almost a traditional award of costs. In response to our inquiry, Ms. Beitel advised that the actual costs in this matter would significantly exceed that number. We also think so, and we see no reason why the MFDA should subsidize these unfortunate proceedings any more than necessary. Accordingly, we order that costs be paid to the MFDA in the sum of $25,000.00.

SUMMARY

49. We find that the two Allegations set out in the Notice of Hearing have been fully made out, and we order as follows:

1. The Respondent, Kerry Scharfenberg, is permanently prohibited from conducting securities related business while in the employ of or associated with any MFDA Member, pursuant to MFDA By-law No. 1, Section 24.1.1(e);
2. With respect to Allegation #1, Scharfenberg shall pay a fine in the amount of $400,000.00, pursuant to MFDA By-law No. 1, Section 24.1.1(b);
3. With respect to Allegation #2, Scharfenberg shall pay a fine in the amount of

$100,000.00, pursuant to MFDA By-law No. 1, Section 24.1.1(b); and

4. Scharfenberg shall pay costs in the amount of $25,000.00, pursuant to MFDA By-law No. 1, Section 24.2.

Dated this 9th day of March, 2009.

"Garret Wilson"
Garrett Wilson, Q. C., Chair

"M.E. (Elaine) Bradley"
M.E. (Elaine) Bradley, Industry Representative

"Erwin Granson"
Erwin Granson, CMA, Industry Representative