



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 DEALERS ASSOCIATION OF CANADA**

**Re: W.H. Stuart Mutuals Ltd., Marilyn Dianne Stuart and
Walter Howard Stuart**

Heard: February 16, 2016 in Toronto, Ontario
Decision and Reasons (Misconduct): April 25, 2016

**DECISION AND REASONS
(Misconduct)**

Hearing Panel of the Central Regional Council:

Mark J. Sandler
Kenneth P. Mann
Vasant Pachapurkar

Chair
Industry Representative
Industry Representative

Appearances:

Shelly Feld)	Counsel for the Mutual Fund Dealers
Paul Blasiak)	Association of Canada
)	
No one appearing for the)	
Respondents)	
)	
)	

Introduction

1. On November 27, 2014, the Mutual Fund Dealers Association of Canada (the “MFDA”) issued a Notice of Hearing respecting three Respondents: W.H. Stuart Mutuals Ltd. (“W.H. Stuart” or “the Member”), Marilyn Dianne Stuart (“Dianne Stuart” or “Ms. Stuart”) and Walter Howard Stuart (“Howard Stuart” or “Mr. Stuart”). The Notice contained the following allegations:

Allegation #1: Between March 26, 2003 and May 2013, Dianne Stuart and W.H. Stuart solicited and accepted approximately \$6 million from more than 180 clients purportedly to be invested on their behalf (the “Note Program”), which monies they failed to repay or otherwise account for.

Allegation #2: Between March 26, 2003 and May 2013, Dianne Stuart and W.H. Stuart actively concealed the activity in Allegations #1 and #3 from others at W.H. Stuart, external auditors, the MFDA and other regulators.

Allegation #3: Between March 26, 2003 and May 2013, in addition to failing to repay or otherwise account for the monies invested in the Note Program described in Allegation #1, Dianne Stuart and W.H. Stuart misappropriated or have otherwise failed to account for more than \$800,000 of investments and monies from over 30 clients.

Allegation #4: Dianne Stuart and W.H. Stuart failed to comply with interim orders of a Hearing Panel of the MFDA with respect to the matters in Allegations #1 and #3 above.

Allegation #5: Between March 26, 2003 and May, 2013, in the course of sustaining the Note Program described in Allegation #1, Dianne Stuart and W.H. Stuart failed to file accurate and complete financial reports, maintain minimum capital, segregate cash and property of W.H. Stuart clients, implement adequate internal controls or maintain accurate financial records.

Allegation #6: Commencing November 21, 2012, Howard Stuart failed to cooperate during the course of an investigation by failing to attend an interview requested by Staff to provide a statement and give information about the matters under investigation.

2. The earliest date contained in the allegations is March 26, 2003. This represents the date that W.H. Stuart became a Member of the MFDA.

3. Howard Stuart never attended or participated in these proceedings. Dianne Stuart initially retained counsel, filed a Reply, and participated personally or through counsel in teleconferences leading to the hearing on the merits. At the last such teleconference, she indicated that her counsel was no longer retained, and that she would not be participating personally or with the assistance of counsel in the proceedings. At the hearing panel's direction, Enforcement Counsel continued to keep her apprised of the ongoing proceedings.

4. Also at the hearing panel's direction, Enforcement Counsel wrote to the Member's Trustee in Bankruptcy ("the Trustee") to determine whether the Trustee intended to participate in these proceedings. By letter dated August 10, 2015, counsel for the Trustee advised Enforcement Counsel that no funds were available for distribution to pay liabilities owed to ordinary unsecured creditors of W.H. Stuart and that "the Trustee does not intend to file a Reply, request disclosure, attend or otherwise participate in the proceeding."

5. Rule 7.3(1) of the MFDA Rules of Procedure states that:

If 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 [Staff] 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.

6. The evidence satisfied us that all three Respondents chose not to attend or otherwise participate in the hearing on the merits, despite being given timely notice of the proceedings, and the opportunity to participate. We were entitled to proceed with the hearing without further notice to and in the absence of the Respondents. The allegations are serious, of interest or importance to many investors, the securities industry and the public, and deserving of evaluation on their merits. In the circumstances, it was in the public interest to proceed.

7. Rule 7.3(1) also permitted us to accept the facts alleged and the conclusions drawn in the Notice of Hearing as proven, without further formal proof. However, Enforcement Counsel took the position that in light of the gravity of the allegations and the interest in these proceedings, it was appropriate to lead evidence in support of the allegations. Counsel submitted – correctly in our view – that we could rely both upon the deemed findings and conclusions available pursuant to Rule 7.3(1) and the evidence in determining whether each of the allegations had been proven.

8. Enforcement Counsel relied largely upon the following affidavits, together with the exhibits appended to each:

- (a) the affidavits of Lara Rowles, Manager of Investigations at the MFDA, sworn on April 29, 2013, June 5, 2013, February 5, 2016 and February 16, 2016;
- (b) the affidavits of Laura Milliken, Managing Director of Financial Compliance at the MFDA, sworn on April 29, 2013, June 6, 2013 and February 10, 2016; and
- (c) the affidavit of Dorothy Sanford, President of the MFDA Investor Protection Corporation (the “IPC”) sworn on February 4, 2016.

9. The February 16, 2016 Rowles Affidavit, the April 29, 2013 Rowles Affidavit and the June 5, 2013 Rowles Affidavit contain much of the evidence respecting Allegations #1 to #4. The Sanford Affidavit describes the compensation process that the IPC implemented to determine which clients were entitled to compensation for losses resulting from the bankruptcy and insolvency of W.H. Stuart and to determine the amount of compensation payable under the terms of the IPC Coverage Policy. The February 10, 2016 Milliken Affidavit, the April 29, 2013 Milliken Affidavit and the June 6, 2013 Milliken Affidavit contain much of the evidence

respecting Allegation #5, as well as the Member's financial compliance history. Finally, the February 5, 2016 Rowles Affidavit addresses Allegation #6 pertaining to Howard Stuart.

10. Rule 13.4(1) of the MFDA Rules of Procedure provides that a 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. In accordance with this Rule, we allowed Enforcement Counsel to rely upon the above affidavit evidence in seeking to prove the Allegations. To state the obvious, by choosing not to participate in the proceedings, the Respondents gave up any right to seek the attendance of the affiants for cross-examination.

Registration Histories

W.H. Stuart

11. From 1986 until May 2013, W.H. Stuart was registered and carried on business as a mutual fund dealer in all Canadian provinces except Quebec. Between November 26, 1993 and August 15, 2000, W.H. Stuart was also registered in Ontario as a limited market dealer.

12. As earlier indicated, on March 26, 2003, W.H. Stuart became a Member of the MFDA.

13. On January 2, 2013, W.H. Stuart gave notice of its intention to resign from membership in the MFDA in connection with its proposed acquisition.

14. On May 10, 2013, a hearing panel made interim orders against W.H. Stuart and Dianne Stuart pursuant to s. 24.3 of MFDA By-law No. 1. The interim orders are addressed in more detail below. With appropriate regulatory approval, an asset purchase agreement was signed, resulting in the transfer of W.H. Stuart's client accounts and Approved Persons to Keybase Financial Group Inc. ("Keybase"), another Member of the MFDA.

15. On May 31, 2013, a hearing panel suspended W.H. Stuart from membership in the MFDA and required W.H. Stuart and Dianne Stuart to preserve and produce certain documents and information relevant to the current allegations. At that time, W.H. Stuart had approximately 18,800 client accounts and client assets under administration totaling \$583 million. During its membership in the MFDA, W.H. Stuart had between 200 and 400 Approved Persons providing client services.

Dianne Stuart

16. From July 10, 1986 to May 9, 2013, Dianne Stuart was registered as an officer of W.H. Stuart in all Canadian provinces except Quebec and Alberta.

17. On March 26, 2003, Dianne Stuart became an Approved Person of W.H. Stuart. While an Approved Person of W.H. Stuart, Dianne Stuart was registered in the following categories:

- (a) from November 20, 2009 to May 9, 2013: in Ontario and Manitoba, as the Ultimate Designated Person (“UDP”);
- (b) from September 28, 2009 to May 9, 2013: in Ontario, as a dealing representative;
- (c) from March 4, 2003 to May 9, 2013: in Ontario, as a director; and
- (d) from March 4, 2003 to May 9, 2013: in all provinces except Quebec and Alberta, as an officer.

18. The evidence disclosed that at all material times, Dianne Stuart was the primary person who directed and controlled W.H. Stuart’s operations and was the Approved Person with knowledge of and responsibility for W.H. Stuart’s financial affairs and reporting. The evidence also disclosed that she was primarily responsible for the design and operation of the Note Program which is at the heart of Allegation #1.

19. In early May 2013, a hearing panel, as one of its interim orders pursuant to s. 24.3 of MFDA By-law No. 1, prohibited Dianne Stuart from dealing with the public. W.H. Stuart then submitted a notice of termination on her behalf to the National Registration Database stating that

Dianne Stuart was resigning as a dealing representative and as the UDP of W.H. Stuart. In response, the Ontario Securities Commission suspended Dianne Stuart as a registrant.

Howard Stuart

20. From July 10, 1986 to May 15, 2013, Howard Stuart was registered in Ontario as an officer and director of W.H. Stuart. Prior to May 15, 2013, he was also registered as an officer and director of W.H. Stuart in Alberta, British Columbia and Manitoba.

21. On March 26, 2003, Howard Stuart became an Approved Person of W.H. Stuart. He was a dealing representative in Ontario from September 28, 2009 to May 15, 2013.

22. From September 2009 to May 2013, Howard Stuart held the title of President and Chief Executive Officer of W.H. Stuart.

23. Enforcement Counsel conceded that since approximately 2006, Howard Stuart appears to have had limited involvement in the day-to-day management and operations of W.H. Stuart. He did remain a director and held the positions of President and Chief Executive Officer of W.H. Stuart. He also received monthly payments from W.H. Stuart or related companies.

24. Mr. Stuart resides in California.

Other Companies

25. In addition to W.H. Stuart, Dianne Stuart and Howard Stuart set up and supported the operations of several other companies in Canada and the United States, including a Canadian insurance brokerage called W.H. Stuart Insurance Agency Ltd. (“Stuart Insurance”) and a computer software company called S21C Technologies (“S21C”). S21C developed a proprietary back office system used by W.H. Stuart and Stuart Insurance to record client information and transactions. Dianne Stuart and W.H. Stuart used the trade name “W.H. Stuart and Associates”

on letterhead and documents from time to time. “W.H. Stuart and Associates” was a registered trade name of W.H. Stuart.

26. Dianne Stuart and Howard Stuart also financed the start-up of the family’s American companies, including Stuart Securities Corp., Stuart Mutuals, Stuart Financial Corporation and W.H. Stuart Insurance Agencies Inc. These companies were all incorporated in Georgia, U.S.A.

Allegation #1: The Note Program

27. A significant number of clients of W.H. Stuart were educators. Dianne Stuart and Howard Stuart had been teachers themselves and established strong relationships with the education sector. Some of their senior compliance staff previously worked in the education sector as well. A number of retired educators commuted their pensions and placed the proceeds with W.H. Stuart to be invested in mutual funds.

28. Beginning in a period of low interest rates, Dianne Stuart and W.H. Stuart offered clients the opportunity to invest with “W.H. Stuart and Associates” in a “guaranteed investment.” It purportedly guaranteed the principal amount invested and purportedly would pay investors interest (usually specified as 7% per year). This is referred to as the “Note Program.”

29. In total, Dianne Stuart and W.H. Stuart solicited and obtained approximately \$6 million from more than 180 clients for investment in the Note Program. Investors in the Note Program understood, assumed or were led to believe by Dianne Stuart that the Note Program was a legitimate investment that W.H. Stuart was permitted to sell.

30. There was no evidence of any collateral or security of any kind supporting the investments in the Note Program in spite of the representations that it was a “guaranteed” investment. Investors were not told how the money they were investing was to be used, why it was being solicited or about the constraints on W.H. Stuart’s ability to repay investors.

31. The money that Dianne Stuart and W.H. Stuart solicited and obtained from investors in the Note Program should have been deposited in the trust account of W.H. Stuart if the Note Program was legitimate. Instead, Dianne Stuart deposited the investors' monies in other bank accounts that she controlled including bank accounts of related companies. All or substantially all of the monies remained within the possession and control of Dianne Stuart or companies that Dianne Stuart controlled and were used to sustain the operations of W.H. Stuart and related companies, or for the direct or indirect benefit of Dianne Stuart.

32. There was no evidence that any monies solicited from clients who participated in the Note Program were actually invested on their behalf. Dianne Stuart and W.H. Stuart have not repaid any of the monies to investors, except to the extent that they may have used some investors' monies to purportedly make interest payments to other investors. They also repaid a few clients who chose to redeem their investments. All of the monies otherwise remain unaccounted for.

33. Some investors who participated in the Note Program received a document entitled "Investment Agreement" that was usually signed by Dianne Stuart. It purported to set out the terms of their investment, including the following:

- (a) the principal amount invested;
- (b) a representation that the principal amount was guaranteed;
- (c) the annual interest rate (usually 7%);
- (d) the term of the investment, which was a minimum period of 1 year renewable at maturity; and
- (e) a statement to the effect that investors were required to provide advance written notice of a request to redeem their investment (usually specified as between 60 days and three months).

34. Other investors in the Note Program did not receive documents evidencing the terms of their investments, but were either verbally promised, or were led to believe, that they would receive interest payments at the rate of 7% to 10% per year on monies that they held in cash in their investment accounts at W.H. Stuart. These investors were led to believe that their interest payments would be credited to their investment accounts on a regular basis.

35. The above findings were supported by documentation the hearing panel reviewed. The documentation included:

- (a) Notes prepared by Gerald Rumball, a former Approved Person of W.H. Stuart and signed by Dianne Stuart that reflected unsecured loans to or investments with W.H. Stuart in return for fixed rates of return;
- (b) Unsigned notes that also showed unsecured loans to or investments with W.H. Stuart in return for fixed rates of return; and
- (c) Account statements or portfolio summaries of former clients of W.H. Stuart that reflected some of the activity associated with the Note Program.

36. The amounts recorded on both signed and unsigned notes, and the activity shown on portfolio summaries show that many clients invested hundreds of thousands of dollars in the Note Program. These monies often represented all of substantially all of their portfolios and, in many instances, all of their retirement savings, including the proceeds derived from commuting their pensions.

37. During the period 2009 to 2013, Dianne Stuart also arranged for an unregistered individual to contact clients of W.H. Stuart to solicit their participation in the Note Program. He had not fulfilled the proficiency requirements necessary to conduct securities related business and was not subject to the jurisdiction of the MFDA.

38. In September 2013, Dianne Stuart admitted to the Ontario Securities Commission and the MFDA that beginning as early as 2002, she began to borrow money from clients. These monies were solicited for the purpose of addressing financial difficulties including significant litigation

expenses she was then incurring. She acknowledged that she would not have had sufficient funds available to pay back a large number of investors in the Note Program at the same time in the event of a significant spike in redemptions. We observe that these admissions were very different than the representations she had earlier made to the MFDA.

39. We earlier referred to the transfer of client accounts to Keybase. Following that transfer, it became apparent very quickly that there were insufficient funds available to satisfy the liabilities of W.H. Stuart. On September 18, 2013, a bankruptcy order was made against W.H. Stuart and a Trustee in Bankruptcy appointed.

40. Dianne Stuart and W.H. Stuart failed to repay or otherwise account for all or substantially all of the monies (approximately \$6 million) that they solicited from more than 180 clients who invested in the Note Program.

41. The evidence disclosed that IPC implemented a claims process to compensate clients whose losses were attributable to the bankruptcy and insolvency of W.H. Stuart. As of February 4, 2016, IPC had received 239 claims for compensation totaling over \$10 million. Of those numbers, 189 claims seeking compensation of approximately \$8.4 million related to the Note Program. As of the same date, the IPC had paid out over \$6 million in compensation related to the Note Program. This likely underestimates the total losses associated with the Program given certain limits applicable to IPC's coverage.

42. In engaging in the conduct described above, Dianne Stuart and W.H. Stuart:

(a) failed to deal fairly, honestly and in good faith with the clients and engaged in conduct unbecoming a Member and Approved Person, contrary to MFDA Rule 2.1.1; and

(b) engaged in personal financial dealings with the clients which gave rise to a conflict or potential conflict of interest between the interests of Dianne Stuart and W.H. Stuart and the interests of the clients, which they failed to ensure was addressed by the

exercise of responsible business judgment influenced only by the best interests of the clients, contrary to MFDA Rules 2.1.4 and 2.1.1.

Allegation #2: Concealment

43. Dianne Stuart and W.H. Stuart used a variety of techniques to actively conceal the existence of the Note Program from the MFDA and others.

44. Prior to the commencement of MFDA's investigation of the Note Program in January 2012, Dianne Stuart and W.H. Stuart did not record any liabilities associated with the Note Program in W.H. Stuart's books and records, monthly financial reports or annual audited financial statements submitted to the MFDA. No prospectus, offering memorandum or other disclosure document was provided to investors or submitted to any regulator for approval. The Note Program was not described on W.H. Stuart's website or in publications or presentations to investors or Approved Persons. Client statements or portfolio summaries identified Note Program holdings as cash, rather than as an investment product. Dianne Stuart and W.H. Stuart did not wish to take any steps that made it more likely that the Note Program would come to the attention of regulators.

45. Indeed, Dianne Stuart actively deceived the MFDA once its investigation had commenced. Initially, she and W.H. Stuart denied the existence of the Program. They then claimed that it was only offered to a single client for unusual reasons. Dianne Stuart then refused to answer many questions about that client's investment on the basis that the investment was purchased through Stuart Insurance and thus, supposedly beyond MFDA's jurisdiction. In May 2013, Dianne Stuart admitted that the Program had been offered to other clients, but discontinued some time ago. She falsely asserted that she was unaware of any promissory notes that remained outstanding. In July 2013, a former Approved Person of W.H. Stuart admitted to the MFDA that he had facilitated investments in the Note Program by a number of clients. Around the same time, the MFDA received confirmatory reports from former clients. It was only in late 2013 that Ms. Stuart admitted that she had operated the Program until May 2013 when W.H. Stuart's assets had been sold to Keybase. She also admitted that the liabilities associated with the Program went

unrecorded on W.H. Stuart's financial statements. She did not truthfully explain to compliance staff at W.H. Stuart why frequent intercompany transfers were taking place between W.H. Stuart and Stuart Insurance.

46. Clients who participated in the Note Program were provided with electronic access to, or paper copies of, records that purportedly tracked the performance of their investments. The records were false and manipulated, when necessary, by or under the direction of Ms. Stuart. They were separate and distinct from the books and records of W.H. Stuart. Ms. Stuart was able to manipulate the records because she controlled the company that owned W.H. Stuart's back office system, S21C Technologies Ltd ("S21C"). Dianne Stuart took steps to restrict access of regulators and other individuals to data on the back office system and directed several employees of W.H. Stuart and S21C to manipulate access to and content in records on the S21C system in a variety of ways, such as:

- (a) programming the system so that a client, certain authorized employees or Approved Persons of W.H. Stuart could see all of the data associated with the account, but other users such as regulators and auditors could only see data associated with mutual fund holdings;
- (b) separating mutual funds data on the back office system from insurance products and cash holdings data. Only Dianne Stuart was granted access to the cash holdings data;
- (c) the creation of a "Do Not Include" List comprised of accounts that held only cash. Access to these accounts was limited to Dianne Stuart, a S21C employee and the client;
- (d) the creation of "inactive active" accounts that even the client could not see;
- (e) editing and deleting data from reports and other print outs from the back office system of W.H. Stuart prior to authorizing the Chief Compliance Officer to submit the requested data to respond to regulatory inquiries; and
- (f) retaining the ability to access, view and change back office records if she wished to do so without the knowledge, approval or consent of clients or Approved Persons.

47. The evidence disclosed other actions taken by Ms. Stuart to conceal the Note Program from the MFDA and others, including measures to ensure the unavailability of a person with damaging knowledge to MFDA Staff and W.H. Stuart's Chief Compliance Officer, and the alteration of records. These and other sophisticated, deceitful measures undoubtedly delayed the detection of the serious misconduct of Ms. Stuart and W.H. Stuart by the MFDA and others.

48. By engaging in the above conduct, Dianne Stuart and W.H. Stuart actively concealed their activities associated with the Note Program from external auditors, the MFDA and other regulators, and many employees by:

- (a) deliberately not recording transactions and other information about the Note Program in the books and records of W.H. Stuart;
- (b) preparing records of the Note Program that were maintained separately from the records of W.H. Stuart and actively concealed; and
- (c) falsifying, altering, concealing and withholding relevant records and information,

contrary to MFDA Rule 5, MFDA Policy No. 4 and MFDA Rule 2.1.1.

Allegation #3: Misappropriation and failure to account unrelated to the Note Program

49. The evidence disclosed that Dianne Stuart and W.H. Stuart misappropriated and/or failed to account for more than \$800,000 that was invested with or held in accounts at W.H. Stuart unrelated to the Note Program.

50. In April 2013, an employee of W.H. Stuart told the MFDA that she was aware of 40-50 complaints about unauthorized transactions processed in client accounts between 2011 and 2013. Dianne Stuart would generally respond by contacting the client herself to explain that the transactions had been processed in error and that she would take steps to reverse the transactions. The evidence overwhelmingly demonstrated that her explanation was false. The unauthorized activity in the clients' accounts was simply another facet of the large scale deception perpetrated by Dianne Stuart and W.H. Stuart.

51. Although the MFDA ultimately discovered a number of cases of misappropriations of client monies and unauthorized transactions unrelated to the Note Program, three instances figured most prominently in the evidence before us. These involved the investment accounts of clients MD, SC and RS. These clients rarely processed transactions in their accounts. Paperwork containing falsified signatures of the clients was submitted to the fund companies by fax. The paperwork purported to direct the fund companies to liquidate the clients' holdings and forward the proceeds by way of cheques to W.H. Stuart in trust for the clients. The cheques were deposited into bank accounts of Stuart Insurance. Of course, the transactions were not reported to the clients.

52. When these transactions were discovered, Dianne Stuart claimed falsely that they had been processed in error and repurchased for the clients the investments that had been sold without their authorization. The unauthorized redemptions and the repurchases in the client accounts did not appear on the W.H. Stuart trade blotters. The client complaints were not reported to the MFDA on the Member Event Tracking System ("METS") contrary to MFDA Policies 3 and 6. When the MFDA requested account records of the clients, compliance staff at W.H. Stuart advised that there were no records of those client accounts on the mutual fund section of the back office system. The records had been transferred to the insurance side of the back office system. W.H. Stuart took the completely untenable position that those records were therefore not subject to the jurisdiction of the MFDA.

53. The IPC received approximately 38 claims alleging losses resulting from the misappropriation of, or failures to account for, client funds unrelated to the Note Program. The 38 claimants alleged losses totaling approximately \$1.5 million. IPC determined that compensation in the amount of \$826,638.99 was payable to them under its Coverage Policy.

54. By engaging in the above conduct, Dianne Stuart and W.H. Stuart misappropriated or otherwise failed to account for over \$800,000 of client investments and monies from over 30 clients, contrary to MFDA Rules 2.1.1 and 2.3.1.

Allegation #4: Failure to Comply with Interim Orders

55. On April 29, 2013, the MFDA commenced an application pursuant to s. 24.3 of MFDA By-law No. 1 on an *ex parte* basis to obtain interim orders against Dianne Stuart and W.H. Stuart for the purpose of, among other things, suspending the authority of Dianne Stuart to have dealings with the public, engage in complaint handling or play an active role in the banking and financial operations of W.H. Stuart. The application was also designed to avoid further deterioration of W.H. Stuart's financial position and preserve certain documents and records relevant to the matters under investigation. Subsequent appearances took place, with notice to Dianne Stuart and W.H. Stuart, before a hearing panel on three occasions in May 2013. A series of orders were made as a result.

56. The evidence disclosed that Dianne Stuart and W.H. Stuart contravened those orders in a variety of ways. These included:

- (a) the failure of Dianne Stuart to end her involvement with banking in relation to W.H. Stuart and related companies such as Stuart Insurance;
- (b) the failure of Dianne Stuart to stop processing trades through W.H. Stuart's back office system;
- (c) the failure to abide by early warning requirements and restrictions;
- (d) the failure of Dianne Stuart and W.H. Stuart to disclose passwords to MFDA Staff to facilitate their access to electronic banking records of W.H. Stuart and its related companies. Dianne Stuart and W.H. Stuart also failed to produce a complete set of paper banking records as required; and
- (e) the failure to transfer client assets or the proceeds from the sale of client assets to Keybase or to otherwise account for many of those assets.

57. The irresistible inference to be drawn from these contraventions, viewed in the context of all of the evidence, is that Dianne Stuart had no regard for the authority of the regulator, showed no good faith in addressing the difficulties caused by her own conduct, and exhibited no remorse

for her extremely serious misconduct. On the contrary, the contraventions represented further efforts to conceal and prevent access to evidence of that misconduct.

58. By engaging in the above conduct, Dianne Stuart and W.H. Stuart failed to comply with interim orders made by a Hearing Panel of the MFDA, contrary to section 22.1 of MFDA By-law No. 1 and MFDA Rule 2.1.1.

Allegation #5: Financial compliance deficiencies

59. Pursuant to MFDA Rule 3.5.1, W.H. Stuart was required to file financial reports (the “Form 1”) with the MFDA on a monthly basis; and two copies of its audited Form 1 on an annual basis. Between 2004 and 2013, W.H. Stuart failed to disclose any of the liabilities associated with the Note Program on the forms it filed with the MFDA. Nor were the liabilities owed to investors as a result of the Note Program shown on any financial records that were available to regulators or auditors of W.H. Stuart. Indeed, as indicated earlier in these Reasons, steps were taken to prevent disclosure of the Note Program itself, or its nature and extent, to the regulators or auditors of W.H. Stuart.

60. In addition, Dianne Stuart and W.H. Stuart co-mingled client monies with their property and with related companies that Dianne Stuart controlled, failed to maintain the minimum capital in W.H. Stuart, a Level 4 Dealer, as required under the MFDA Rules, and in particular, failed to maintain enough monies in the W.H. Stuart trust account to offset the liabilities associated with the Note Program or the large cash balances in client accounts. It is an understatement to say that the books and records of W.H. Stuart were deficient and non-compliant with MFDA Rules. They were deliberately misleading in furtherance of the misconduct outlined in these Reasons. Concealment of that misconduct also explains why Dianne Stuart and W.H. Stuart failed to put in place adequate internal controls to promote compliance. Dianne Stuart was the individual who bore prime responsibility for all of these contraventions.

61. We find it unnecessary to further detail the financial compliance contraventions by Dianne Stuart and W.H. Stuart. As was in case in relation to Allegations #1 to #4, the evidence of misconduct on the part of Dianne Stuart and W.H. Stuart was overwhelming.

62. By engaging in the above conduct, Dianne Stuart and W.H. Stuart failed to:

- (a) file accurate and complete monthly Form 1's and annual audited Form 1's for W.H. Stuart with the MFDA, contrary to MFDA Rules 3.5.1 and 2.1.1 and MFDA Policy No. 4;
- (b) ensure that W.H. Stuart maintained the minimum capital required of a Level 4 dealer, contrary to MFDA Rule 3.1.1;
- (c) segregate cash and other property of W.H. Stuart's clients from Dianne Stuart's or W.H. Stuart's own property, contrary to MFDA Rules 3.3 and 2.1.1 and MFDA Policy No. 4;
- (d) implement adequate internal controls, contrary to MFDA Rule 2.9; and
- (e) ensure accurate financial records were maintained by W.H. Stuart, contrary to MFDA Rule 5, MFDA Policy No. 4 and MFDA Rule 2.1.1.

Summary respecting Dianne Stuart and W.H. Stuart

63. Dianne Stuart was a directing mind of W.H. Stuart. In fact, she was the primary person who directed and controlled W.H. Stuart's operations at the material time, and was the Approved Person with knowledge of and responsibility for W.H. Stuart's financial affairs and reporting. As such, her misconduct also constitutes misconduct on the part of W.H. Stuart.

64. The evidence revealed that Dianne Stuart and W.H. Stuart engaged in a massive scheme of dishonesty over a period of approximately 10 years or more. It was perpetuated in a variety of ways, including but not limited to the bogus Note Program. At its core was the falsification and concealment of records, and a pattern of deceit. The scheme represented a gross breach of trust and fiduciary responsibility, and resulted in losses in the millions of dollars. The efforts taken to disguise this scheme of dishonesty from the MFDA and other regulators, auditors, investors, and

others were truly staggering in their breadth, duration and level of sophistication. The evidence demonstrated, not merely on a balance of probabilities but overwhelmingly, that Dianne Stuart and W.H. Stuart engaged in the misconduct set out in Allegations #1 to #5.

Allegation #6: Failure to Cooperate (Howard Stuart)

65. As earlier indicated, prior to May 15, 2013, Howard Stuart held the title of President and Chief Executive Officer of W.H. Stuart. He was also an officer and director of W.H. Stuart for an extensive period of time prior to May 15, 2013. He also received substantial monthly payments from W.H. Stuart or related companies.

66. On January 17, 2012, David Liptrott, a manager in the MFDA Case Assessment group of the MFDA Enforcement Department sent a letter to Dino DeRosa, who was then the Chief Compliance Officer of W.H. Stuart, requesting information about the activities of W.H. Stuart, its principals and/or its related or affiliated entities.

67. On February 21, 2012, Mr. DeRosa faxed a response to MFDA Staff that included a written statement dated February 6, 2012 which was addressed to Mr. DeRosa and which responded to the questions raised by MFDA Staff. The statement was purportedly signed by Howard Stuart and Dianne Stuart and appeared to deny the existence of any promissory note, investment certificate, loan arrangement or other type of transaction involving lending arrangements between W.H. Stuart, its principals or its related or affiliated entities entering into lending arrangements with dealer clients or other individuals.

68. On November 21, 2012, Enforcement Counsel, Mr. Feld, sent a letter to counsel for W.H. Stuart, requesting, among other things that by Wednesday, November 28, 2012, Howard Stuart agree to attend an interview with MFDA Enforcement Staff on or before December 12, 2012. The purpose of the interview would be, among other things, to obtain a statement from Howard Stuart regarding the investments and lending arrangements referred to above.

69. By letter dated November 27, 2012, counsel for W.H. Stuart informed Mr. Feld that Howard Stuart had suffered a heart attack and had withdrawn from full time employment. Counsel indicated that Howard Stuart was out of the country and was not expected to return to Toronto for some time. He also stated in the letter that Mr. Stuart had limited day to day involvement with the dealer at that point in time. Counsel offered to inform MFDA Staff when Mr. Stuart was next expected in Toronto. MFDA Staff learned that Mr. Stuart had not resided in Toronto for several years and now resided in in California, U.S.A.

70. In the fall of 2013, Staff of the MFDA and the Ontario Securities Commission conducted a compelled examination of Dianne Stuart pursuant to section 13 of the Ontario *Securities Act*, R.S.O. 1990, c. S.5.

71. On several occasions during the examination, Dianne Stuart indicated that Howard Stuart had knowledge of investments or lending arrangements that have been referred to in these Reasons as the Note Program. She indicated that she and Howard Stuart set up and supported the operations of several other companies besides W.H. Stuart including Stuart Insurance and S21C, that they registered the trade name “W.H. Stuart and Associates”, which was used by W.H. Stuart and Stuart Insurance, and that they had financed the start-up of the family’s American operations, including Stuart Financial Corporation and W.H. Stuart Insurance Agencies Inc., which were companies incorporated in the state of Georgia. She also stated that although Mr. Stuart had limited involvement in the day-to-day management and operations of W.H. Stuart and its affiliates since the two of them separated as husband and wife in approximately 2007, he continued to receive monthly payments of at least \$7,500 from Stuart Insurance up until approximately May 2013.

72. On November 7, 2013, Lara Rowles, a manager with MFDA’s Investigations Group, sent a letter to Howard Stuart at his residential address in California. She requested his attendance at an interview with MFDA Staff to answer questions in connection with the investigation of W.H. Stuart.

73. On November 26, 2013, she received a response, by letter, from Howard Stuart in which he asserted that due to “poor health” he would not be able to travel to attend an interview with MFDA Staff. In his letter, Howard Stuart also requested that MFDA Staff provide him with “some money” as a result of purported financial difficulties that he was experiencing.

74. By letter dated December 11, 2013, Ms. Rowles offered to conduct an electronic interview (via Skype) with Mr. Stuart so that he would not have to travel to Toronto to attend in person. She instructed him to contact her to indicate which date between February 3 and 7, 2014 he would be available to participate in the electronic interview.

75. On December 31, 2013, Ms. Rowles received a second letter from Howard Stuart in which he agreed to participate in an interview provided that MFDA Staff first disclose to him certain information that had been gathered during the investigation. Howard Stuart did not provide a date on which he would agree to be interviewed.

76. By letter dated January 6, 2014, Ms. Rowles reiterated her request to Howard Stuart to advise her which date he would be available to participate in the electronic interview. She also informed him that if he failed to respond to MFDA Staff’s requests, MFDA Staff would consider commencing enforcement proceedings against him for failing to cooperate with the investigation.

77. On January 15, 2014, Ms. Rowles received another letter from Howard Stuart in which he expressed his purported willingness to cooperate with the investigation, but again failed to provide a date on which he agreed to be interviewed.

78. By letter dated January 17, 2014, Ms. Rowles informed Mr. Stuart that MFDA Staff had scheduled his interview to take place on February 7, 2014. She also instructed him to contact her by January 29, 2014 to provide his contact information for purposes of conducting the interview. She reiterated that if he failed to respond to MFDA Staff’s requests, MFDA Staff would commence enforcement proceedings against him for failing to cooperate with the investigation.

79. Howard Stuart did not respond to her letter dated January 17, 2014 letter and did not participate in an interview with MFDA Staff on February 7, 2014.

80. Mr. Stuart was obligated to cooperate with the MFDA in its ongoing investigation of W.H. Stuart and its principals. The MFDA was well within its rights to insist on that cooperation given, among other things, the positions that Mr. Stuart held at the material time with W.H. Stuart and MFDA's undoubted jurisdiction over him. Its right to insist on that cooperation was not dependent on whether Dianne Stuart had or had not accurately described Mr. Stuart's role in the Note Program and related activities in her interview in the fall of 2013.

81. The MFDA was prepared to be accommodating in how, when and where Mr. Stuart would be interviewed, having regard to information conveyed that he had suffered a heart attack and now lived in California. Indeed, the MFDA offered to conduct the interview by Skype, which would allow Mr. Stuart to remain in California. Despite several representations by Mr. Stuart that he was prepared to be interviewed and cooperate with the investigation, he never provided a response to the dates proposed by MFDA staff or for that matter, any response at all to the last correspondence from Ms. Rowles. Ms. Rowles made him fully aware of his obligation to cooperate, and that a failure on his part to cooperate could result in enforcement proceedings.

82. We are satisfied on a balance of probabilities that Mr. Stuart has deliberately chosen not to cooperate with the MFDA's investigation. He was obligated to do so. We have been offered no evidence that provides him with a legal justification or excuse for failing to cooperate.

83. As a result, in part, of Mr. Stuart's lack of cooperation, MFDA Staff has been unable to determine the extent of his involvement and participation in the Note Program, if any, and the misconduct of W.H. Stuart and M. Dianne Stuart.

84. By failing to attend an interview to provide a statement and give information respecting the matters under investigation, Howard Stuart failed to cooperate with an investigation, contrary to section 22.1 of MFDA By-law No. 1 and MFDA Rule 2.1.1.

Findings

85. For these reasons, we are satisfied that all of the allegations contained in the Notice of Hearing have been proven. April 29, 2016 has been scheduled for the continuation of these proceedings. At that time, we will hear submissions on the issue of penalty.

DATED this 25th day of April, 2016.

“Mark J. Sandler”

Mark J. Sandler
Chair

“Kenneth P. Mann”

Kenneth P. Mann
Industry Representative

“Vasant Pachapurlar”

Vasant Pachapurlar
Industry Representative

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