File No. 200503

MUTUAL FUND DEALERS ASSOCIATION OF CANADA

**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**

DISCIPLINARY HEARING

D E C I S I O N

Re: Arnold Tonnies

Heard: May 16th, 2005

Panel Decision: June 27th, 2005

Hearing Panel of the Prairie Regional Council	**Daniel Ish, Q.C., Chair** **Terry Ford, Industry Representative** **Erwin Granson, Industry Representative**
Appearances:	
For the Mutual Fund Dealers Association of Canada	**Robert DelFrate**
For Arnold Tonnies	**Not in attendance personally or by counsel**

CONTENTS

1. THE ALLEGATIONS

By notice of hearing dated February 10, 2005, the following allegations were made against Arnold Tonnies ("the Respondent"):

(1) In or around July 2002, the Respondent borrowed money from two clients to finance his outside business activity as a cattle farmer, thereby placing his personal interests above those of his clients and giving rise to an actual or potential conflict of interest, contrary to MFDA Rule 2.1.4.

(2) In or around July 2002, the Respondent failed to abide by the policies and procedures set out by the Member regarding conflicts of interest by borrowing money from two clients to finance his outside business activity as a cattle farmer, thereby failing to observe high standards of ethics and conduct in the transaction of business, contrary to MFDA Rule 2.1.1(b).

(3) Commencing in or around December 2003, the Respondent failed to produce for inspection and provide copies of documents requested by the MFDA for the purpose of investigating a complaint made against the Respondent, contrary to s. 22.1 of By-Law No. 1.

2. SERVICE

The Notice of Hearing provided for a first appearance by teleconference before the Hearing Panel at #2330, 355 - 4 Avenue, SW, Calgary, Alberta on Tuesday, March 22, 2005, at 9:00 a.m. At that time, the Respondent did not appear personally and no one appeared as counsel or agent on his behalf.

At the First Appearance Mr. DelFrate, Enforcement Counsel for the MFDA, described the attempts that had been made to that date by the staff of MFDA to serve the

Notice of Hearing on the Respondent. No decision was made on March 22, 2005, as to the adequacy of service. A hearing date was set for May 16, 2005 to deal with the merits of the allegations. Subsequent to the teleconference hearing on March 22, 2005, the MFDA issued a Press Release and posted a copy on its website, advising as to the time and place of the May 16, 2005 hearing.

The Respondent did not appear personally, or by counsel or agent, at the hearing on May 16, 2005. At the commencement of the hearing, Enforcement Counsel made submissions as to the adequacy of service and filed in support of his submissions a copy of the Notice of Hearing dated February 10, 2005 (Exhibit 1), an Affidavit of Service of the Notice of Hearing (Exhibit 2), a copy of a letter dated March 3, 2005 to Mr. Tonnies in care of his solicitor, Glen Forester (Exhibit 3), a letter dated March 30, 2005 to Mr. Forester (Exhibit 5) and a letter dated April 29, 2005 to Mr. Forester (Exhibit 6).

We find that the following steps were taken by the staff of the MFDA to effect Service of Notice of Hearing on the Respondent:

(a) On February 14, 2005, a true copy of the Notice of Hearing, together with a letter addressed to Glen Forester, the Respondent's counsel, and a copy of MFDA's Rules of Procedure were sent by registered and ordinary mail, addressed to Arnold Tonnies, c/o Glenn E. Forrester, MacLaughlin Forrester Heinrichs, #9 Carmel Mall, 224 - First Avenue NE, Swift Current, Saskatchewan, S9H 2B4. The letter advised the Respondent and his counsel that a Disciplinary Hearing had been commenced against the Respondent and set out in detail his rights and obligations in relation to the Disciplinary Hearing.

(b) On February 17, 2005, Canada Post delivered a copy of the Notice of Hearing along with a letter to Mr. Forrester to the address of Mr. Forrester's law office in Swift Current, Saskatchewan.

(c) Following delivery of a copy of the Notice of Hearing and the letter to Mr. Forrester, Mr. Forrester contacted MFDA's enforcement counsel advising him that neither the Respondent nor Mr. Forrester would participate in the first appearance in this Hearing on March 22, 2005.

(d) On March 3, 2005 enforcement counsel wrote to Mr. Forrester, counsel for Mr. Tonnies, advising him that the Notice of Hearing which was sent to him on February 14, 2005 was incorrect in that it indicated the Hearing time to be 10:00

a.m. (Mountain Time) on March 22, 2005. The letter went on to advise Mr. Forrester that the correct date and time for the hearing was Tuesday, March 22, 2005 at 9:00 a.m. (Mountain Time).

(e) As indicated, neither the Respondent nor his counsel appeared on March 22, 2005 and, subsequent to the teleconference hearing, the MFDA issued a Press Release, posted on the MFDA website, advising of the time and place of the May 16, 2005 hearing.

(f) On March 30, 2005 Enforcement Counsel wrote to Mr. Forrester advising him that on March 22, 2005 the first appearance was held by teleconference and that the date for the commencement of the hearing on the merits had been scheduled to take place on Monday, March 16, 2005 at 10:00 a.m. (MST) in the Novara Ballroom at the Delta Regina Hotel, 1919 Saskatchewan Drive, Regina, Saskatchewan.

(g) On April 29, 2005 Enforcement Counsel wrote to Mr. Forrester again advising him that the hearing on the merits in the matter of Arnold Tonnies had been scheduled to take place on Monday, May 16, 2005 at 10:00 a.m. (MST) in Regina (the details of the place of the hearing were given) and provided Mr. Forrester with copy of the Affidavit of Patricia McIlwrick (both of which were entered as exhibits at the hearing on May 16, 2005).

After hearing the submissions of Enforcement Counsel and reviewing the documentary evidence during the course of the hearing on May 16, 2005, this panel was unanimously of the opinion that the delivery and publication of the Notice of Hearing in the manner described above constituted good and sufficient service on the Respondent. We hereby make an Order to this effect pursuant to Rule 4.2(1)(d) of the MFDA Rules of Procedure.

3. MANNER OF PROCEEDING

Rule 13.5 of the MFDA Rules of Procedure states:

Where a Respondent Fails to Attend a Disciplinary Hearing

(1) Where a Respondent, having been served with a Notice of Hearing, fails to attend the hearing of the proceeding on its merits, the Hearing Panel may proceed in accordance Rule 7.3.

Rule 7.3 provides:

Failure to Attend Hearing

(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 section 24.1 and 24.2 respectively by Bylaw No. 1.

Enforcement Counsel advised the Hearing Panel that he wished to proceed with the hearing in the absence of the Respondent but seek to prove the allegations by means of admissible evidence. The Panel agreed with that approach and proceeded to hear the evidence.

4. PRESENTATION OF EVIDENCE

The primary evidence before the Hearing Panel consisted of a 39-paragraph Affadavit of Patricia McIlwrick ("the McIlwrick Affidavit"), an investigator with the Enforcement Department of the Investment Dealers Association of Canada. Accompanying and forming part of the McIlwrick Affidavit was an exhibit book containing 24 exhibits.

The MFDA Rules of Procedure contain provisions dealing with admissibility of evidence generally and sworn statements particularly. Rule 1.6 states:

Admissibility of Evidence

(1) Subject to sub-Rule (3), a panel may admit as evidence any testimony, document or other thing, including hearsay, which it considers to be relevant to the matters before it and is not bound by the technical or legal rules of evidence.

Rule 13.4 states:

> ***Evidence by Sworn Statement***
>
> (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.

Accordingly, we admitted and marked the McIlwrick Affidavit as Exhibit 4(a) since pursuant to the Rules of Procedure it is admissible evidence before us.

Enforcement Counsel advised the Hearing Panel that the clients' names had been removed in the McIlrick Affidavit by MFDA staff and substituted with initials. This was to protect client confidentiality. Counsel advised that this was not possible to do with the book of 24 Exhibits to the McIlrick Affidavit. Therefore he asked that the Hearing Panel treat the exhibit book as a confidential document pursuant to Rule of Procedure 1.8(2) and (5). After considering the submissions of Counsel, the exhibit book was marked as Exhibit 4(b) and, pursuant to a combination of Rule 1.8(2) and (5), it was marked "confidential".

5. THE EVIDENCE

A. General

As indicated, the primary evidence in this matter was the McIlwrick Affidavit and the exhibits attached to it. Clearly some of the evidence relied upon by Ms. McIlwrick in her Affidavit, such as the notes and conversations with the National Compliance Officer of TWC, constitute hearsay evidence for the purposes of this Panel. Although such evidence may be admitted by us pursuant to the Rules, it is important for the Panel to exercise caution when relying upon hearsay evidence on matters that are integral to the allegations before us. Even though in this case none of the evidence was challenged by Mr. Tonnies, as he did not appear either personally or through counsel, the Panel still must be satisfied that the evidence supports the allegations of misconduct made against him.

Arnold Tonnies was registered as Mutual Funds Salesperson with the Saskatchewan Financial Services Commission between 1986 and April 2003. He was also registered as a Non-Resident Salesperson in Alberta and Ontario. Mr. Tonnies worked at Prairie West Financial Services Ltd. in Swift Current, Saskatchewan, a registered branch of TWC. TWC became a member of MFDA on March 8, 2002. Mr. Tonnies was an "Approved Person" as defined in MFDA Bylaw no. 1 and thus is subject to MFDA rules. In addition, Mr. Tonnies also owned and operated a cattle farming business under the name "Tonnies Cattle Company". This business was disclosed to and approved by TWC in March 2002. The disclosure and approval was in accord with TWC's Policies and Procedures Manual and MFDA Rule 1.2.1(d). As a result of the events leading up to the allegations which are the subject of this hearing, Mr. Tonnies was terminated for cause by TWC on April 14, 2003.

B. The Clients - MS and LMS

All of the events surrounding the allegations in this matter pertain to two elderly clients of the Respondent. The clients, MS and LMS, were sisters who were approximately 90 and 94 years of age respectively at the time the events occurred. Both had been clients of Mr. Tonnies for about 13 years. The elder sister, LMS, suffered from Alzheimer's disease and, as a result, MS held a Power of Attorney over LMS's affairs which was dated March 7, 1989. The evidence admitted included an Affidavit of MS and a summary of statements and evidence provided by her, or her agents or counsel. The evidence discloses that in July 2002 Mr. Tonnies approached MS and asked her whether he could borrow $200,000 from LMS. At the time Mr. Tonnies was aware that MS held the Power of Attorney for LMS. In response to Mr. Tonnies' request, MS obtained a certified cheque payable to Arnold Tonnies in the amount of $200,000 drawn on LMS's bank account. The Respondent agreed to pay the entire loan, including interest calculated at 6% per annum on the $200,000, on or before October 31st, 2002. No promissory note was provided by the Respondent to MS and the loan has never been repaid.

A few days later, on or about July 8, 2002, MS redeemed a net amount of $50,000 from a mutual fund that she had on her own behalf with TWC. MS did not receive a cheque, rather the funds were released to Mr. Tonnies and it appears the cheque was cashed by him. MS received a promissory note from the Respondent with respect to the $50,000. The promissory note was only received after the Executors of LMS's estate discovered the $200,000 loan to Mr. Tonnies. Mr. Tonnies subsequently retrieved the promissory note from MS and its current whereabouts are unknown.

In a telephone call on December 15, 2003 Ms. McIlwrick as part of her investigation spoke to Arnold Tonnies. Mr. Tonnies admitted to her that he did borrow the $200,000 and $50,000 from LMS and MS respectively. In her investigation Ms. McIlwrick spoke to and reviewed notes of Brad Nyhus, a National Compliance Officer with TWC. These communications confirm that he had borrowed the money from MLS and MS and had not repaid the loans. The reason for the borrowing was that he was under pressure to pay a bank loan as a result of his cattle business. The loans were used to repay a loan or loans he had with the Bank of Montreal.

Mr. Tonnies ultimately declared bankruptcy, filing an assignment of bankruptcy on April 22, 2003. In the Statement of Affairs sworn by Mr. Tonnies, the estate of LMS is listed as a creditor in the amount of $210,000 and MS is listed as a creditor in the amount of $52,000. The MFDA first became aware of the loans to the Respondent when advised by the Saskatchewan Financial Securities Commission on March 20, 2003. The SFSC had received a complaint against Mr. Tonnies filed by the estate of LMS after it was advised by TWC of the situation and the complaint. The Respondent was placed on full supervision by TWC and, on April l4, 2003, was terminated for cause. The cause cited by TWC for the termination was Mr. Tonnies' breach of his fiduciary duty to his clients by failing to act in their best interest and failing to avoid a personal conflict of interest by borrowing money for his own personal use.

In summary, the evidence discloses that Mr. Tonnies at his request obtained unsecured loans from LMS and MS in the total amount of $250,000 in July 2002. The

first loan was for $200,000 from LMS and was not supported by a promissory note. The second loan was for $50,000 from MS. A promissory note was issued to MS for this loan, but was subsequently retrieved by the Respondent. The proceeds of the loans appear to have been used to pay an outstanding debt to the Bank of Montreal arising from Mr. Tonnies' cattle farming business. The Respondent did not disclose the loans to TWC.

C. Failure to Comply with Policies and Procedures Manual

TWC maintains a policy and procedures manual ("PPM") as required by MFDA Rule 2.1.4. The portions of the PPM that deal with conflicts of interest read as follows:

> ***Conflicts of Interest, MFDA Rule 2.1.4***
>
> TWC is required by MFDA Rule 2.1.4 to establish written policies and procedures to ensure compliance with the MFDA Rules regarding Conflicts of Interests.
>
> General
>
> A conflict of interest is the situation of an Associate whose private interests might benefit from his or her influence over a client.
>
> When faced with a conflict or potential conflict of interest with respect to services provided to a TWC client, the Associate will exercise the business judgement of responsible persons, uninfluenced by considerations other than the best interests of the clients.
>
> Personal Conflicts of Interest
>
> Associates must avoid any situation in which their personal interests conflict or appear to conflict with their duties at TWC. Conflicts of interests may arise in a number of ways and include the following:
> - Inappropriate use of information obtained through other occupations outside of TWC to further Mutual Fund Sales;
> - Promoting investments which the Associate has a personal interest in, such as Limited Partnerships; or asking a client to invest in the Associate's Personal Business;
> - Basing a decision to sell a particular mutual fund or investment based on the compensation whether monetary or non-monetary to the Associate rather than the clients' best interests.
>
> Disclosure
> It is important that disclosure of potential conflicts of interest takes place immediately after becoming aware that there is a potential conflict. Associates must immediately disclose to TWC any conflict or potential conflict of interest by submitting it in writing to the Compliance Manager at Head Office.

> If an Associate is uncertain as to whether a conflict of interest exists, the Associate shall call the Compliance Manager to discuss the matter. The Compliance Manager will determine if a conflict of interest exists and the appropriate means to resolve it.
>
> TWC is required by the MFDA to immediately disclose the conflict of interest to the Associate's client in writing prior to TWC or the Associate conducting business for the client.

On May 15th, 2002 Mr. Tonnies signed a certificate acknowledging that he read and understood the PPM and that he agreed to abide by it.

D. Failure to Produce and Provide Documents

The evidence discloses that notwithstanding numerous efforts by the Investigator, Patricia McIlwrick, Mr. Tonnies failed to provide documents, or copies of documents, to assist the Investigator in her investigation of the complaint made against him. The efforts of the Investigator to obtain documentation from the Respondent included the following:

- On December 1, 2003 the Investigator, by registered letter, requested that the Respondent provide copies of all banking statements for any personal or business accounts in which he had signing authority, or had a direct or indirect control over, between January 1, 2002 and April 30, 2003. The letter requested that Mr. Tonnies provide the material no later than December 19, 2003.
- In a telephone conversation on December 15, 2003, the Respondent requested, and received, from the Investigator an extension of the December 19 deadline to January 16, 2004. In this conversation the Respondent advised the Investigator that the requested documents were with the trustee in bankruptcy and would likely be available by mid-January. The Investigator confirmed the extension to January 16, 2004 by a registered letter dated December 15, 2003.
- The Investigator spoke to Mr. Tonnies on the telephone on January 20, 2004 advising him that the extension date of January 16 had passed and that the requested documents had not been received. Mr. Tonnies advised the investigator that he wished to speak with his lawyer before providing the documents.

- In a registered letter dated January 22, 2004, the Investigator notified the Respondent that he was compelled to provide the requested documents pursuant to s. 23.1 (now s. 22.1) of MFDA Bylaw No. 1. In this letter the Investigator provided a further extension of the time in which to provide the documents to February 3, 2004.
- The Investigator was contacted by telephone on February 3, 2004 by Mr. Glenn Forrester, the Respondent's lawyer. Mr. Forrester advised that in lieu of providing the requested documents, Mr. Tonnies was prepared to provide the MFDA with an undertaking not to deal in mutual funds in the future. He further advised that the requested documents were currently with the Respondent's accountant and thus were unavailable. The Investigator requested that Mr. Forrester reduce his proposal to writing which he did in letter to the MFDA dated February 3, 2004. The letter essentially reiterated the conversation with the Investigator in that it indicated that Mr. Tonnies was prepared to provide the MFDA with an undertaking never to deal or attempt to deal in mutual funds in the future.
- In a registered letter dated March 21, 2004 the Investigator advised Mr. Forrester that an undertaking not to deal in mutual funds was not an acceptable alternative to the production of the requested documents. Mr. Forrester was also advised that the failure of Mr. Tonnies to provide the requested documents may result in disciplinary proceedings for failure to co-operate with the MFDA investigation. Again, the deadline for the production of documents was extended, this time to April 16, 2004
- In a telephone conversation on April 19, 2004, Mr. Forrester advised the investigator that Mr. Tonnies would not be providing the documents because he was voluntarily no longer involved in the mutual funds industry, that he did not intend to return to the industry, and that his current financial situation did not enable him to pay any fine that may be imposed on him by the MFDA.
- In a registered letter dated April 29, 2004, Investigator McIlwrick notified Mr. Forrester that a disciplinary proceeding would be contemplated against

Tonnies for failure to co-operate with the MFDA's investigation contrary to s. 22.1 (previously s. 23.1) of Bylaw No. 1.

The Panel was advised at the hearing on May 16, 2005 that the Respondent had not provided the MFDA with the documentation as requested.

6. ANALYSIS AND DECISION

A. Allegation No. 1 - Borrowing $250,000 from two clients to finance outside business activities

MFDA Rule 2.1.4 provides as follows:

> **Conflicts of Interest**
>
> (a) Each Member and Approved Person and other employee and agent of a Member shall be aware of the possibility of conflicts of interest arising in connection with business conducted by them for a client. In the event that such a conflict or potential conflict of interest arises, the Member shall ensure that it is addressed by the exercise of responsible business judgment influenced only by the best interests of the client and in compliance with Rules 2.1.4(b) and (c).
>
> (b) Any conflict of interest that arises or can reasonably be expected to arise as referred to in Rule 2.1.4(a) shall be immediately disclosed in writing by the Member to the client prior to the Member, or any person acting on its behalf in connection with its business, conducting business for the client.
>
> (c) Each Member shall develop and maintain written policies and procedures to ensure compliance with Rules 2.1.4(a) and (b).

Rule 2.1.4 (a) requires that each Member and Approved Person of the MFDA shall be aware of the possibility of conflict of interest arising in connection with business conducted by them for a client. In the event that such conflict or potential conflict of interest arises, a Member or Approved Person must "ensure that it is addressed by the exercise of responsible business judgment influenced only by the best interests of the client". The phrase "responsible business judgment", which is contained in the Rule, is not defined by the Rules. However, a reasonable interpretation would suggest that it requires the exercise of care and diligence in the circumstances to address the conflict or

potential conflict of interest always subject to being in the best interest of the client. The exercise of responsible business judgment may therefore vary depending on the nature of the conflict of interest and the characteristics of the client. In cases involving a significant and actual conflict of interest, the exercise of responsible business judgment may require a blanket prohibition on, or refusal to proceed with, the type of transaction giving rise to the conflict. This may be especially so when the client, or clients, are somewhat vulnerable, perhaps because of age, as is the situation before us. In contrast, cases involving a potential conflict of interest of a relatively minor nature, the exercise of responsible business judgment may require only that the client is directed to obtain independent advice before proceeding with the proposed transaction. Again, the sophistication and the characteristics of the client may very well be significant factors.

Rule 2.1.4(b) requires any conflict of interest to be disclosed in writing to the client prior to the Member (or any person acting on its behalf, ie. an Approved Person) conducting business with the client. Further, the rules make clear that an Approved Person must conduct himself or herself in a manner consistent with and in furtherance with the bylaws and rules. Rule 1.1.2 provides that each Approved Person shall comply with the bylaws and rules "… as they relate to the Member or such Approved Person."

Upon a careful review of the evidence in this matter, we conclude that the Respondent, Arnold Tonnies, failed to meet his obligations as an Approved Person under Rule 2.1.4. Also, by his conduct, he prevented TWC from satisfying its obligations under this rule. Mr. Tonnies approach MS asking for a loan of $200,000 utilizing her Power of Attorney over the affairs of her sister, LMS. Further, he then orchestrated MS to redeem $50,000 from her mutual fund holdings and to provide these funds to him as a loan. The Respondent did not disclose either to MS or LMS in writing or verbally that these loans gave rise to an actual or potential conflict of interest. Clearly, it was more than a potential conflict of interest, it was an actual conflict of interest. Specifically, there is no evidence to support the proposition that the Respondent disclosed the use to which the borrowed funds were to be put or the risk inherent in transferring money from secure mutual funds to an investment in his own cattle farming operation. Therefore, we find,

on the basis of clear and cogent evidence, that Mr. Tonnies failed to exercise responsible business judgment taking into account only the best interests of his clients. Rather, his judgment seemed to be influenced by his own personal interests. Further, there is no evidence to suggest that the Respondent advised MS to obtain independent advice, on her own behalf or on behalf of LMS, before proceeding with either loan. To exacerbate the situation, the Respondent did not provide any security for the loans, in the one case only provided a promissory note which, it appears, he later retrieved.

There is no evidence that Mr. Tonnies took any steps to protect the interests of his clients. He did not disclose the existence of these loans to TWC and, as a result, TWC was unable to intercede in any respect. Had notice been given to TWC, TWC may have ensured that the client receive written notice of the conflict of interest as required by the rules. Also TWC would have been in a position to assess whether the transaction represented an exercise of responsible business judgment.

Mr. DelFrate, counsel for MFDA, provided the Panel with a book of authorities making reference to numerous court cases and decisions of regulatory tribunals relating to persons in situations similar to Mr. Tonnies. The Panel found these cases quite helpful in assessing the application of the rules to the evidence in the present case. Quite aside from a specific rule to address the situation, the cases make clear that financial counselors are required to exercise reasonable precautions to ensure that any transaction performed on behalf of a client is to the benefit of and in the best interests of the client (*Re Thompson,* [2004] I.D.A.C.D. No. 49, at para. 47). This obvious proposition has been supported by the courts and goes to the very essence and nature of the relationship between a financial counselor and client.

This Panel is unanimous in finding that the Respondent clearly violated Rule 2.1.4. He approached vulnerable clients and solicited significant funds (a total of $250,000) from them as a loan, which was never repaid, for his personal business interest. The loans were used to pay off the debt he had with the Bank of Montreal. We find that in July 2002 the Respondent failed to act with integrity and in good faith and did

not adhere to the needs of his clients. More specifically, he breached Rule 2.4.1 by being in a clear conflict of interest with his clients and failing to exercise "responsible business judgment influenced only by the best interests of the client". It would be difficult to find a more clear case of a Member or Approved Person placing his own personal financial interests before the interests of his client. In addition, all the facts support the proposition that he preyed on their vulnerability, their age, and their lack of sophistication. It is clear that such conduct is a breach of the rules and cannot be condoned. Previous cases have held such conduct to be of a very serious nature (see *Re Wong* (1994), 3 A.S.C.S. 1574 at para. 21).

B. Allegation No. 2: Failing to Observe High Standards of Ethics and Conduct in the Transaction of Business

MFDA Rule 2.1 provides as follows:

> 2.1.1 Standard of Conduct. Each Member and each Approved Person of a Member shall: …
>
> (b) observe high standards of ethics and conduct in the transaction of business.

The phrase "high standards of ethics" is not clearly defined in the Rules. However, in addition to the Hearing Panel's specialized knowledge, considerable guidance can be found to give meaning to this phrase both in decisions of the courts, administrative tribunals and TWC's Policies and Procedures Manual which applied to the Respondent in this case. As previously indicated, the Respondent acknowledged that he read the PPM and agreed to abide by it. The PPM specifically references MFDA Rule 2.1.4 dealing with conflict of interest and provides examples of conduct that would constitute a conflict of interest which would fall within that Rule. The PPM states in part:

> Conflicts of interest may arise in a number of ways including the following:
>
> - Promoting investments which the Associate has a personal interest in, such as Limited Partnerships; or asking a client to invest in an Associate's Personal Business.

It is clear that the Respondent solicited and accepted loans from his clients to fund his personal business activities despite the specific admonition in the PPM. The borrowing from clients MS and LMS occurred in July 2002, merely two months after Mr. Tonnies signed an acknowledgement indicating that he read the PPM and agreed to abide by it. The direction in the PPM can be used as a standard of ethics and conduct against which we can measure the activities of Mr. Tonnies. It is clear that he breached the internal standards of TWC.

The British Columbia Securities Commission has held that registrants are obliged to follow their member firms' business procedures for dealing with clients. In *Re Cartaway Resources Corp.,* [2000] B.C.S.C.D. No. 92, the Commission found that the member firms' business procedures, as reflected in its Guidelines for Business Conduct, established that the member "had a legal duty to act with the 'highest standard of ethical business conduct' towards clients, shareholders and the public" (para. 228). The Commission went on to state:

> The Guidelines stated that every employee was to avoid any activity, interest or association which might interfere or even appear to interfere with the independent exercise of judgment in the best interest of [the member firm] its shareholders, clients and the public. All outside business connections were required to be reported so that they could be scrutinized and continuously monitored for potential conflicts. To the extent that employees were engaged in outside activities, they were required to ensure their activities were not in conflict or competition with their duties and responsibilities. (para. 228)

Identical comments can be made with respect to the PPM in this case as were made with respect to the Guidelines in the *Cartaway* case. Moreover, the standards outlined in the PPM are reasonable ones given the nature of the activity, namely advising and counseling individuals with respect to investment decisions.

Superior courts in Canada have also dealt with the issue of ethics and standards in the role of self-governing professions. The courts have made clear that members of these professions are uniquely and best qualified to establish the standards of professional conduct. Thus, a hearing panel of three, two of whom are members of the profession,

possesses a specialized knowledge with respect to ethics and standards that can be applied in a particular case. In *Re Milstein and Ontario College of Pharmacy, et al.* (1977), 72 D.L.R. (3d) 202, Cory J. of the Ontario High Court confirmed this principle and went on to say:

> Members of the profession can best determine whether the conduct of a fellow member has fallen below the requisite standards and determine the consequences. The peers of the professional person are deemed to have and, indeed, they must have special knowledge, training and skills that particularly adapts them to formulate their own professional standards and to judge the conduct of a member of their profession. No other body could appreciate as well the problems and frustrations that beset a fellow member." (at p. 234)

Finally, the courts have made clear that the absence of a definition of misconduct does not prevent a disciplinary tribunal from considering whether there has been misconduct in a particular case. In *Re Matthews and Board of Directors of Physiotherapy* (1987), 61 O.R. (2d) 475, the Ontario Court of Appeal stated:

> The absence of such a definition requires the board to judge the appellant by the objective standards of his own profession. Although these standards are unwritten, they are nonetheless real and it is within the jurisdiction of the appellant's professional brethren who constitute the board to determine in the particular case if he has fallen below that standard. (at p. 475)

Similarly, in *Ripley and the Investment Dealers Assoc. (Business Conduct Committee)*, [1990] N.S.J. No. 295, the Nova Scotia Supreme Court stated:

> I agree with the respondent's statement that to require that evidence be given in proof of such issues as basic ethics and honesty would be an affront to the common sense, experience and intelligence of the members of every professional Disciplinary Committee.

It is the unanimous finding of this Panel that the Respondent, Arnold Tonnies, failed to "observe high standards of ethics and conduct in the transaction of business" as required by MFDA Rule 2.1.1(b). Mr. Tonnies breached TWC's Policies and Procedures Manual requirement relating to conflicts of interest, specifically by receiving from clients LMS and MS money for the purpose of paying off a loan with respect to his own cattle business. Moreover, he failed to disclose the conflict of interest to TWC contrary to the

PPM. Indeed, he did not even discuss the matter with the Compliance Manager to determine whether the arrangement with a client constituted a conflict of interest. We unanimously find that Allegation No. 2, set out in the Notice of Hearing, has been proved.

C. Allegation 3: Failure to Produce and Provide Documents

Section 22.1 of MFDA Bylaw No. 1, under the heading, Investigatory Powers, states:

> 22.1 For the purpose of any examination or investigation pursuant to this By-law, a Member, Approved Person of a Member or other person under the jurisdiction of the Corporation pursuant to the by-laws or the Rules may be required by the Corporation:
>
> (a) to submit a report in writing with regard to any matter involved in any such investigation;
>
> (b) to produce for inspection and provide copies of the books, records and accounts of such person relevant to the matters being investigated;
>
> (c) to attend and give information respecting to any such matters; and
>
> (d) to make any of the above information available through any directors, officers, employees, agents and other persons under the direction or control of the Member, Approved Person or other person under the jurisdiction of the Corporation;
>
> and the Member or person shall be obliged to submit such report, to permit such inspection, provide such copies and to attend, accordingly. Any Member or person subject to an investigation conducted pursuant to this By-law may be invited to make submission by statement in writing, by producing for inspection books, records and accounts and by attending before the persons conducting the investigation. The person conducting the investigation may, in his or her discretion, require that any statement given by any Member or person in the course of an investigation be recorded by means of an electronic recording device or otherwise and may require that any statement be given under oath.

The courts have made clear that there is a general duty upon all members of self-regulated professions to co-operate with their governing bodies (see *Artinian v. The College of Physicians of Ontario* (1990), 73 O.R. (2d) 704 (Div. Ct.) and *Kaburda v.*

College of Dental Surgeons of British Columbia, [2001] B.C.J. No. 2161 (B.C.S.C.). Section 22 of M.F.D.A. Bylaw No. 1 codifies this obligation by requiring Approved Persons to submit reports, to produce for inspection and provide copies of relevant documents, and to attend and give information during investigations conducted by the MFDA. Failure to co-operate is serious misconduct in that it subverts the ability of the MFDA to perform regulatory functions. The responsibility to regulate mutual fund sales has been granted to the MFDA, as similar regulatory powers fall upon other professional bodies, and that responsibility can only be carried out if the MFDA has the authority to investigate, which includes the ability to obtain relevant documentation from Members and Approved Persons.

The evidence in the present case clearly establishes that the Respondent failed to produce and provide documents after being requested to do so on numerous occasions by MFDA's Investigator. As set out above, the Investigator gave the Respondent every opportunity by allowing numerous extensions of the time for the production of the documents, yet none were produced. Ultimately, the Investigator was advised by the Respondent's lawyer that none would be produced. We unanimously find that allegation No. 3, set out in the Notice of Hearing, has been proved.

7. PENALTY

MFDA Bylaw No. 1, s. 24 sets out the disciplinary power of Hearing Panels. With respect to Approved Persons, which applies to the Respondent in this case, the bylaw states:

> **24. DISCIPLINE POWERS**
>
> 24.1 **Power of Hearing Panels to Discipline**
>
> 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:

(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 specified period and upon such terms as the Hearing Panel may determine;

(d) revocation of the authority of such person to conduct securities related business;

(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.

The courts, and other tribunals, have set out a number of factors to be taken into account in determining penalties to be imposed under provisions similar to s. 24 of Bylaw No. 1. In determining an appropriate penalty, the Supreme Court of Canada has indicated that tribunals must keep in mind the primary goal of securities regulation which is the protection of the investing public (see *Pezim v. British Columbia (Superintendent of Brokers,* [1994] 2 S.C.R. 557.) The Court also has indicated that sanctions imposed in the securities regulatory context should be protective and preventative, intended to be

exercised to prevent likely future harm to the capital markets (see *Committee for Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission),* [2001] 2 S.C.R. 132).

The Ontario Securities Commission has set out succinctly its role, not dissimilar to the role of this Panel, in determining penalty in *Re Mithras Management Ltd. et al.* (1990), 13 O.S.C.B. 1600. The Commission stated at 1610:

> … [T]he role of this Commission is to protect the public interest by removing from the capital markets - wholly or partially, permanently or temporarily as the circumstances may warrant - those whose conduct in the past leads us to conclude that their conduct in the future may well be detrimental to the integrity of those capital markets. We are not here to punish past conduct; that is the role of the courts, particularly under section 118 of the Act. We are here to restrain, as best we can future conduct that is likely to be prejudicial to the public interest in having capital markets that are both fair and efficient.

Several previous decisions of industry tribunals, including an MFDA tribunal (*Re Parkinson*, [2005] MFDA Case No. 200501), have found the following factors should be taken into account in determining the appropriate sanctions to impose:

(a) the protection of the investing public;

(b) the integrity of the securities market;

(c) specific and general deterrents;

(d) the protection of the governing body's membership; and

(e) the protection of the integrity of the governing body's enforcement processes.

Moreover, the Supreme Court of Canada in the *Cartaway* decision, *supra,* has indicated that general deterrence is an appropriate consideration in making orders that are both protective and preventative. At para. 61 of that case, the Court stated:

> In a word, a general deterrent is preventative. It is therefore reasonable to consider general deterrence as a factor, albeit not the only one, in imposing a sanction under s. 162. The respective importance of general deterrence as a factor will vary according to the breach of the Act and the circumstances of the person charged with breaching the Act.

Previous tribunals have set out a number of additional factors that should be considered in determining penalty. They include:

- The seriousness of the allegations proved against the respondent;
- The respondent's past conduct, including prior sanctions;
- The respondent's experience in the capital markets;
- The level of the respondent's activity in the capital markets;
- Whether the respondent recognizes the seriousness of the improper activity;
- The harm suffered by investors as a result of the respondent's activities;
- The benefits received by the respondent as a result of the improper activity;
- The risk to investors and the capital markets in the jurisdiction, were the respondent to continue to operate in capital markets in the jurisdiction;
- The damage caused to the integrity of the capital markets in the jurisdiction by the respondent's improper activities;
- The need to deter not only those involved in the case being considered, but also any others who participate in the capital markets, from engaging in similar improper activity;
- The need to alert others to the consequences of inappropriate activities to those who are permitted to participate in the capital markets; and
- Previous decisions made in similar circumstances.

See *Belteco Holdings Inc.* (1998), 21 O.S.C.B. 7743; *M.C.J.C. Holdings and Michael Cowpland* (2002), 25 O.S.C.B. 1133; and *Lamoureux (Re),* [2002] A.S.C.D. No. 125.

Counsel for the MFDA urged the Panel to impose penalties the cumulative effect of which would be at the high end of the scale. He proposed that the Panel impose a permanent prohibition on the authority of the Respondent to conduct securities-related business. Also, he asked the Panel to consider a fine in the following amounts:

- Allegation No. 1 - $300,000
- Allegation No. 2 - $50,000
- Allegation No. 3 - $50,000

In addition he asked that the Panel award costs of $7,500.

Counsel argued that a permanent prohibition and a global fine of this magnitude, amounting to $400,000 in total, reflects the seriousness of the Respondent's conduct and

is in keeping with the purpose of the MFDA to enhance investor protection and strengthen public confidence in the Canadian mutual fund industry by ensuring high standards of conduct by its Members and Approved Persons. Further, it was argued that the proposed sanctions will prevent future misconduct by the Respondent, deter others from engaging in similar misconduct, improve overall compliance by mutual fund industry participants, and foster public confidence in the securities industry. In addition, it was argued that these sanctions reflect the goals and purposes of securities regulation as we have outlined above.

Numerous cases were cited to the Panel as a guide to appropriate penalties that should be considered. In the *Re Wong* case (1994), ASCS 2053, an Alberta mutual funds salesperson advised his clients to redeem their mutual fund investments to invest in a scheme whereby interest in Egyptian Arabian horses was acquired. The clients, like in the present case, were vulnerable and unsophisticated investors, who trusted his advice. The Alberta Securities Commission found that Mr. Wong was in a conflict of interest with his clients in that he failed to advise them that he had a personal interest in the venture. The penalty imposed by the Commission was to remove Mr. Wong from the securities industry by issuing a 20-year cease trade order and denying him the benefit of certain exceptions in the Alberta Securities Act and Regulations. The Commission further ordered that he immediately resign from any positions he held as director or officer of an issuer and that he be prohibited from holding such positions for 20 years. He was also ordered to pay costs of $5,000.

In *Re Monterossa,* [2002] BCSECCOM 567, the British Columbia Securities Commission made a finding of misconduct against a mutual funds person who borrowed $73,000 from his clients to help support family members in El Salvador and to assist himself in meeting his monthly expenses. The B.C. Commission held that by borrowing money from his client, Monterossa failed to deal fairly, honestly, and in good faith with his clients. The Commission ordered that for a period of 10 years from the date that all outstanding debts to former clients had been repaid that he not engage in any investment

related activities, that he be denied exceptions under the Securities Act and he not act as an officer or director of an issuer.

With respect to the *Parkinson* case, *supra,* an MFDA Panel imposed a fine in the amount of $250,000 after finding a breach of the rules with respect to unbecoming and detrimental conduct involving $314,000 not repaid to clients. In addition, a further fine in the amount of $75,000 was imposed Parkinson for providing false account statements and order forms to clients and a fine of $50,000 was imposed with respect to the third finding that the respondent engaged in business conduct which was unbecoming and detrimental to the public interest by abandoning his business as an Approved Person without notice to his clients or to the Member. The total fine imposed in *Parkinson* amounted to $375,000 in addition to costs of $7,500 and a permanent prohibition of the authority of Parkinson to conduct a securities-related business in any capacity.

In determining the appropriate penalties to impose, it is appropriate to take into account mitigating and aggravating factors. Unfortunately, because Mr. Tonnies did not appear either personally or by counsel, the Panel was denied the benefit of hearing evidence with respect to any mitigating factors, therefore we are limited to the evidence which was admitted in the Hearing in Mr. Tonnies' absence. As a result, the only mitigating factor that we are aware of is that this is the first time that there has been any disciplinary action taken against Mr.Tonnies.

On the aggravating side, we considered the following:

1) The Respondent has not made any restitution to either of his former clients;
2) There was no evidence before us of any remorse on the part of the Respondent; and
3) The Respondent's improper activities caused, in our view, serious damage to the integrity of the capital markets in Saskatchewan and elsewhere in Canada.

After carefully considering the evidence, the submissions of counsel for the MFDA, and the previous authorities with respect to penalty (which include the factors that should be taken into account), we order that the Respondent, Mr. Tonnies, be permanently prohibited from conducting any securities related business in any capacity. Also, we are of the view that the following fines are the appropriate ones for each of the three allegations which we have found to be substantiated:

Allegation No. 1 - a fine of $250,000.

Allegation No. 2 - a fine of $50,000. In imposing a fine with respect to allegation 2, we are mindful of the fine which we impose with respect to allegation 1 as well as the overall totality of the fines. The consequences of the conduct of the Respondent we have found to exist with respect to allegation No. 1 and allegation No. 2 are very similar and should be considered together in determining the overall fine.

With respect to our finding in response to allegation No.3, two decisions from the Investment Dealers Association of Canada were cited to us where fines were imposed on individuals who refused or failed to attend and give information with respect to an investigation, conduct that which we found to be established against the Respondent in the present case. In *Re Crittall,* [2004] I.D.A.C.D. No. 51, the I.D.A. Panel imposed a fine of $50,000. That fine seems to have been mitigated by some concern the panel had with respect to medical difficulties that the respondent was experiencing which may have precluded her participation. In *Re White*, [2003] I.D.A.C.D. No. 28, Mr. White was ordered to pay a fine of $50,000, in addition to a permanent prohibition and $9,200 in costs. In the *White* decision three other cases were cited, *Re Rob, Re Stauffer* and *Re Katz*, in which panels imposed a penalty of $50,000 and costs for a violation of the rule requiring participation and co-operation.

With respect to the substantiated allegation No. 3, we order a fine of $50,000.

Finally, we further order costs to be paid in the amount $7,500.

8. SUMMARY

In summary, we find that the three allegations set out in the Notice of Hearing have been proved and we order:

(1) A permanent prohibition of the Respondent to conduct securities-related business in any capacity;
(2) A fine in the amount of $250,000 which respect to allegation No. 1;
(3) A fine in the amount of $50,000 which respect to allegation No. 2;
(4) A fine in the amount of $50,000 which respect to allegation No. 3; and
(5) Costs in the amount of $7,500.

Dated this 27th day of June, 2005.

"Daniel Ish"
Daniel Ish, Q.C., Chair

"Terry Ford"
Terry Ford, Industry Representative

"Erwin Granson"
Erwin Granson, Industry Representative

Doc # 61551