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

IN THE MATTER OF A SETTLEMENT HEARING
PURSUANT TO SECTION 24.4 OF BY-LAW NO. 1 OF
THE MUTUAL FUND DEALERS ASSOCIATION OF CANADA

Re: Sterling Mutuals Inc.

Heard: May 26, 2016, in Toronto, Ontario
Decision and Reasons: June 27, 2016

DECISION AND REASONS

Hearing Panel of the Central Regional Council:

John Lorn McDougall, Q.C.	Chair
Guenther W. K. Kleberg	Industry Representative
Robert J. Wright, C.M., Q.C.	Industry Representative

Appearances:

Shelly Feld	)	Counsel for the Mutual Fund Dealers
	)	Association of Canada
	)	
Lara Jackson	)	Counsel for the Respondent
	)	
	)	

1. By Notice of Settlement Hearing, dated February 29, 2016, a Hearing Panel of the Central Regional Council of the Mutual Fund Dealers Association of Canada ("MFDA") was convened on May 26, 2016 to consider whether, pursuant to Section 24.4 of By-law No. 1 of the MFDA, the Hearing Panel should accept a settlement agreement dated May 26, 2016 ("Settlement Agreement") entered into between Staff of the MFDA and Sterling Mutuals Inc. ("the Respondent").

2. At the outset of the proceedings, Staff advised that the Notice of Settlement Hearing had been prepared and publicized in accordance with Section 24.4 of By-law No. 1 and Rule 15.2(1) of the MFDA Rules of Procedure.

3. We also considered a joint Motion by Staff and the Respondent to move the proceedings "in-camera". This Motion was brought pursuant to Rule 15.2(2) of the MFDA Rules of Procedure, which provides as follows:

> "(2) A Hearing Panel may, on its own initiative or at the request of a party, order that all or part of the settlement hearing be held in the absence of the public, having regard to the principles set out in Rule 1.8".

4. Rule 1.8(2) provides as follows:

> "(2) A Panel may order that all or part of a hearing be heard in the absence of the public where the Panel is of the opinion that intimate financial or personal matters or other matters may be disclosed at the hearing which are of such a nature, having regard to the circumstances, that the desirability of avoiding disclosure thereof in the interests of any person affected or in the public interest outweighs the desirability of adhering to the principle that hearings be open to the public."

5. We granted the Motion on the condition, which was agreeable to both Staff and the Respondent that, should the Hearing Panel accept the Settlement Agreement, we would provide Reasons for our Decision which, along with the Record of the Settlement Hearing, would be available to the public. This is consistent with Rule 15.2(3) of the MFDA Rules of Procedure.

6. After considering the Settlement Agreement, along with the submissions made by counsel for the MFDA which were supported by counsel for the Respondent, the Hearing Panel unanimously accepted the Settlement Agreement and will make an Order to this effect in accordance with these Reasons for Decision.

7. The salient portions of the Settlement Agreement are as follows:

> **II. JOINT SETTLEMENT RECOMMENDATION**
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> 2. Staff conducted an investigation of the Respondent's activities. The investigation disclosed that the Respondent had engaged in activity for which the Respondent could be penalized on the exercise of the discretion of the Hearing Panel pursuant to s. 24.1 of By-law No.1.
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> **…**
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> **IV. AGREED FACTS**
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> **Registration History**
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> 6. Since June 6, 1996, the Respondent has been registered in Ontario and in other Canadian provinces as a Mutual Fund Dealer and became a Member of the MFDA on March 8, 2002.
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> 7. Between 1991 and May 29, 2015, Armstrong & Quaile Associates Inc. ("A&Q") was registered in Ontario and in other Canadian provinces as a Mutual Fund Dealer. A&Q amalgamated with the Respondent on May 29, 2015. A&Q was a Member of the MFDA from December 7, 2001 to May 29, 2015.
>
> **Barry Hunt – A Former Approved Person Of A&Q**
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> 8. Between June 5, 2003 and June 24, 2011, Barry Allan Hunt ("Hunt") was registered in the provinces of Ontario, Alberta and Québec as a mutual fund salesperson / dealing representative with A&Q. He is no longer registered in the securities industry.

The Supervision Of Hunt And The Handling Of The Complaint Against Him

The Conduct Of Hunt

9. Hunt was a respondent to a separate but related disciplinary proceeding (MFDA File No. 201342) that was commenced by Notice of Hearing issued on September 11, 2013 and concluded by reasons for decision dated July 18, 2014. In that proceeding, Hunt signed an agreed statement of facts dated May 2, 2014 in which he admitted that:

1) Between September 12, 2007 and June 24, 2011, he engaged in securities related business that was not carried on for the account or through the facilities of A&Q by selling, recommending, referring or facilitating the sale of investments in real estate outside the Member including:

   (i) a $100,000 real estate investment product to client VM; and
   (ii) investments totaling $660,000 in a real estate development project that he owned and operated to clients VM, LT, BM and 11 other individuals; and
   (iii) investments totaling $60,000 in two housing restoration projects to client VM;

   contrary to MFDA Rules 1.1.1(a) and 2.1.1; and

2) Between September 12, 2007 and June 24, 2011, he engaged in personal financial dealings with clients VM, LT and BM by:

   (i) selling an investment of $60,000 in a property owned by Hunt to each of clients VM, LT and BM; and
   (ii) borrowing $120,000 from client VM;

thereby giving rise to a conflict or potential conflict of interest between his interests and the interests of clients VM, LT and BM which he failed to address 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.

The Handling Of The Complaint Concerning VM's Account

10. In 2003, when he became an Approved Person of A&Q, Hunt disclosed and obtained approval from A&Q to engage in an outside business activity as a licensed real estate broker. He did not disclose to A&Q at any time prior to 2010 that he was engaged in real estate investing or that he solicited money from clients for that purpose.

11. On June 7, 2010, client VM appointed her brother and sister-in-law CS and JW as her powers of attorney.

12. On June 21, 2010, CS and JW met with Hunt to discuss client VM's investments.

13. By letter dated June 22, 2010, CS and JW submitted a complaint to A&Q about loans and investments in real estate that had been solicited from client VM by Hunt. CS and JW submitted an additional letter dated July 15, 2010 restating their concerns and requesting the liquidation of all investments other than mutual funds and segregated funds.

14. A&Q failed to report the complaint of CS and JW to the MFDA or the concerns about possible personal financial dealings and unauthorized outside business activities engaged in by Hunt and did not treat the concerns raised on behalf of client VM as a complaint or respond promptly and fairly to the concerns about Hunt's conduct that were raised in the complaint.

15. A&Q also inappropriately delegated authority to Hunt to respond to and resolve the complaint on his own without the involvement of the dealer.

16. A&Q knew or ought to have known that the participation of the subject of a complaint (in this case Hunt) in the complaint handling process and investigation gave rise to a conflict of interest that could not be resolved in the best interests of the client.

17. By failing to implement a proper complaint handling process and by failing to report the complaint to the MFDA following receipt of the complaint of CS and JW, A&Q contravened MFDA Rules 2.11, 2.1.1 and 2.1.4 and MFDA Policy Nos. 3 and 6.

Failure To Conduct A Reasonable Supervisory Investigation

18. A&Q also failed to undertake a reasonable supervisory investigation after receiving the letters from CS and JW, by among other things, failing to adequately investigate:

(a) what investments client VM had made with or through Hunt that were not carried on for the account of the dealer or processed through the facilities of the dealer;
(b) the range and extent of Hunt's outside business activities;
(c) whether any clients or individuals other than client VM had been solicited by Hunt to engage in personal financial dealings with Hunt or to participate in investments that he facilitated that were not processed through the dealer or with its approval; or
(d) whether any other complaints had been received by Hunt or whether any other legal proceedings had been commenced against him.

19. A&Q also failed to take any reasonable supervisory or disciplinary action to ensure that Hunt ceased to engage in personal financial dealings or to facilitate additional investments that were not for the account of the dealer or processed through the facilities of the dealer.

20. A&Q reported this matter to the MFDA for the first time in March 2011 after CS and JW commenced a lawsuit against Hunt and A&Q on behalf of client VM. Prior to the resolution of the lawsuit that was commenced by CS and JW, A&Q learned that:

(a) two other clients (in addition to client VM) and 11 other individuals who were not clients of A&Q had also been solicited by Hunt to participate in real estate investments;
(b) Hunt had obtained personal loans from two other clients (in addition to client VM); and
(c) Hunt was a defendant to multiple lawsuits that had not been reported to A&Q that had been commenced by plaintiffs that included other clients of A&Q.

21. By failing to conduct a reasonable supervisory investigation after receiving the letter from CS and JW dated June 22, 2010, A&Q contravened MFDA Rules 2.5.1 and 2.1.1 and MFDA Policy Nos. 2 and 3 which may have delayed the discovery of the full scope of the outside business activities and personal financial dealings that Hunt had engaged in.

BO – A Former Approved Person Of A&Q

22. From August 30, 1999 to May 20, 2009 BO was registered in Ontario as a mutual fund salesperson / dealing representative with A&Q and was an Approved Person of A&Q from December 7, 2001 (when A&Q became a Member of the MFDA) until May 2009. He is no longer registered in the securities industry.

The Handling Of The Complaint Of JH & JH

23. By letter sent to A&Q on August 7, 2010, former A&Q clients JH and JH (who are spouses) submitted a complaint concerning the suitability of a leveraged investment strategy that was recommended to them and implemented for them in November 2004 by

BO who was by then a former Approved Person of A&Q. Clients JH and JH claimed that at the time that the leveraged investment strategy was implemented, they were provided with unjustified assurances that they would not incur any losses associated with the strategy if they maintained their investments for at least 10 years.

24. In 2009, clients JH and JH transferred their accounts to a new advisor at another mutual fund dealer. Following the transfer, it was explained to clients JH and JH that they held investments that were not subject to guarantees and they had incurred investment losses and interest charges on the loans associated with the leveraged investment strategy that amounted to more than $45,000 as of June 2009.

25. The Ultimate Designated Person of A&Q (the "UDP of A&Q") reviewed the complaint of clients JH and JH and concluded that in his view the leveraged investment strategy that was implemented in November 2004 was suitable for the clients.

26. In reaching that conclusion, the UDP of A&Q failed to consider the Know-Your-Client ("KYC") information on file for clients JH and JH that had been completed and signed on September 21, 2004, just two months prior to the implementation of the leveraged investment strategy which indicated that the joint income of the clients was less than $25,000 per year. This information was later corroborated by the tax returns of clients JH and JH that show the joint annual income of the clients at that time.

27. The UDP of A&Q justified his decision to dismiss the complaint without compensating the clients by applying KYC information reported on a KYC form that was completed in May 2004 that indicated that the joint annual income of the clients was between $50,000 and $100,000. Tax returns that were subsequently produced by the clients appear to support their claims that the amount of their income was inflated on the May 2004 KYC document. In any event, the May 2004 KYC document was not the most up to date KYC information applicable to the clients at the time that the leveraged investment strategy was implemented.

28. By failing to take into account the most recent KYC information on file for the clients at the time when the leveraging strategy was implemented in November 2004 prior to issuing its substantive response to the complaint submitted by clients JH and JH, A&Q failed to deal fairly and promptly with the client complaint, contrary to MFDA Rules 2.11, 2.1.1, 2.1.4 and MFDA Policy No. 3.

Mazzotta's Branch

29. Since June 2002, Carmine Paul Mazzotta ("Mazzotta") has been registered in the provinces of Ontario, Quebec and British Columbia as a mutual fund salesperson / dealing representative with the Respondent. Mazzotta operates his branch office in Ottawa, Ontario using the approved trade name, the Innovative Financial Group ("Mazzotta's Branch").

30. Since July 2002, David John Ireland ("Ireland") has been registered in the provinces of Ontario, Quebec and British Columbia as a mutual fund salesperson / dealing representative with the Respondent and has always worked at Mazzotta's Branch. He was also the Branch Manager of Mazzotta's Branch from August 11, 2008 to March 14, 2011.

31. Mazzotta and Ireland are respondents to a separate but related disciplinary proceeding (MFDA File No. 201511) that was commenced by the MFDA in November 2015 concerning their conduct following receipt of the complaint of client JN as described below.

32. Between September 28, 2005 and August 29, 2008, CB was registered in the province of Ontario as a mutual fund salesperson with the Respondent who worked at Mazzotta's Branch.

The Leveraged Investment Strategy Recommended By Former Approved Person CB

33. Client JN became a client of the Respondent in or about April 2008. His investment accounts were serviced by Approved Persons of the Respondent who worked at Mazzotta's Branch. Initially, client JN received investment advice from former Approved Person CB. After CB resigned in August 2008, the accounts were transferred to Mazzotta and Ireland who serviced the accounts from August 2008 until February 2013.

34. In May 2008, CB recommended and implemented a leveraged investment strategy for client JN that resulted in client JN and his wife client NG borrowing $175,000 by way of an investment loan from B2B Trust and investing the proceeds in mutual funds in amounts recommended by CB (the "Leveraged Investment Strategy").

Client JN's Complaint

35. By letter dated December 5, 2012, client JN submitted a complaint that was addressed to Mazzotta and copied to the Ultimate Designated Person of the Respondent (the "UDP"). The complaint alleged, among other things, that the Leveraged Investment Strategy that CB had recommended was unsuitable and left client JN with outstanding loans that substantially exceeded the value of the investments that he was advised to purchase with the proceeds of the loans and thereafter, Mazzotta and Ireland failed to take satisfactory steps to reduce the risk of client JN's portfolio or provide advice to facilitate the recovery of the losses that he had incurred.

The Handling Of Client JN's Complaint

36. By letter to client JN dated December 10, 2012, the Chief Compliance Officer of the Respondent (the "CCO") acknowledged receipt of the complaint letter from client JN and advised him that the CCO would investigate it. The letter informed client JN that he could contact the CCO if he wished to inquire about the status of the complaint or had

any questions or concerns. A copy of the MFDA Client Complaint Information Form was enclosed with the letter to client JN.

37. The Respondent informed Mazzotta and Ireland of their concern that Mazzotta and Ireland might be held accountable to compensate client JN for a significant proportion of the losses that he had incurred because the value of client JN's account had declined by a substantial amount during the period when they were servicing his account. In spite of this concern, they authorized Mazzotta and Ireland to contact the complainant and schedule a meeting with him to discuss his complaint without the involvement or participation of any compliance staff of the Respondent.

38. On December 18, 2012, Mazzotta and Ireland reported that the "[m]eeting [with client JN] went well." They informed the UDP and the CCO that client JN only intended to direct his complaint towards the conduct of CB and they promised to deliver a further response shortly.

39. The Respondent took no steps to:

(a) assign responsibility for the handling of client JN's complaint to an impartial and qualified supervisor or compliance staff member of the Respondent;
(b) contact client JN to hear his account of what was discussed during the meeting with Mazzotta and Ireland; or
(c) prevent further direct involvement of Mazzotta and Ireland in the handling of client JN's complaint about their conduct even after being informed that they had discussed the possibility of a withdrawal or revision of the complaint with client JN.

40. On February 14, 2013, client JN contacted the Respondent directly by telephone to request that the Respondent transfer his account to a new advisor because he was no longer comfortable dealing with Mazzotta and Ireland.

41. During the telephone call with client JN on February 14, 2013, the Respondent did not request an explanation from client JN about the meetings and communication that had occurred between client JN, Mazzotta and Ireland.

42. On February 14, 2013, client JN also submitted a complaint to the MFDA with respect to the servicing of his investment account by Mazzotta.

43. Subsequently, client JN alleged to Staff of the MFDA ("Staff") that Mazzotta and Ireland had:

(a) attempted to persuade him to withdraw his complaint against them and direct his concerns solely towards former Approved Person CB and the Respondent;
(b) drafted a revised complaint letter for client JN to sign and submit to the Respondent; and
(c) asked client JN to sign a document that was prepared by Mazzotta's lawyer entitled "Assignment of Claims" that purported to assign to client JN all claims Mazzotta had against CB arising from Mazzotta's business/professional relationship with CB in return for a release of Mazzotta from all claims that client JN had against Mazzotta in relation to his investment losses.

44. Client JN also told Staff that he had consulted with lawyers who informed him that the legal claims that Mazzotta had offered to assign to him were statute barred.

45. On February 26, 2013, Staff scheduled a conference call with the Respondent and informed the Respondent about client JN's complaint to the MFDA.

46. Following the call with Staff, for the first time, the Respondent directed Mazzotta and Ireland to cease further communication with client JN. The Respondent also informed Mazzotta and Ireland that:

(1) their conduct may have breached regulatory requirements and policies and procedures of the Respondent;
(2) pending the completion of the MFDA investigation into their conduct, the Respondent was imposing terms of strict supervision on their trading;
(3) a monthly amount would be deducted from their commissions to offset the costs of the heightened supervision for as long as the strict supervision continued.

47. The Respondent continues to impose strict supervision over the trading of Mazzotta and Ireland and a strict supervision charge of 5% is deducted each month from their gross commissions. No additional action was taken against Mazzotta and Ireland by the Respondent.

48. The Respondent knew or ought to have known that the participation of the subjects of a client complaint (in this case Mazzotta and Ireland) in the complaint handling process gives rise to a conflict of interest that could not be resolved in the best interests of the client.

49. On March 23, 2013, the Respondent sent client JN a substantive response to his complaint that informed client JN that the Respondent had completed its review of the complaint and had concluded that proper risk disclosure was provided to him and that based upon the KYC information on file for client JN the Leveraged Investment Strategy that was recommended to client JN was suitable.

50. Following the receipt of the December 5, 2012 complaint from client JN, the Respondent failed to engage in a proper complaint handling process. The Respondent also failed to conduct a reasonable supervisory investigation of the facts and allegations

raised in the complaint of client JN and failed to ensure that the complaint was handled by qualified supervisory or compliance staff and instead permitted the subjects of the complaint to participate in the handling of the complaint, contrary to MFDA Rules 2.1.1, 2.5, 2.1.4 and 2.11 and MFDA Policy No. 3.

Former Approved Persons SW and BY

51. Between May 20, 2014 and December 31, 2015, SW was registered in the provinces of Saskatchewan, Alberta and British Columbia as a dealing representative with the Respondent. SW is no longer registered in the securities industry in any capacity.

52. Between May 27, 2014 and December 31, 2015, BY was registered in the provinces of Saskatchewan, Alberta, British Columbia and Ontario as a dealing representative with the Respondent. He is no longer registered in the securities industry in any capacity.

The Contractual "Release" From Suitability Obligations

53. Effective May 27, 2014, SW and BY transferred their registration from another Member of the MFDA (their "Former Member") and became Approved Persons of the Respondent. They also arranged for the accounts of many of the clients whose accounts they had serviced for their Former Member to be transferred to the Respondent.

54. In respect of most or all of the client accounts that were transferred into the Respondent to be serviced by SW and BY:

(a) uniform Know-Your-Client ("KYC") information was recorded for the clients that represented their risk tolerance as '100% high risk', their investment knowledge as 'good', their time horizon as 'long' and their investment objective as '100% growth'; and

(b) the investment portfolios were comprised primarily of medium to high risk mutual funds that were heavily concentrated in investments in resources and precious metals such as gold.

55. When the accounts were transferred in, the Respondent failed to exercise due diligence to ensure that the uniform KYC information that was recorded for the clients was accurate or that the assets that were transferred into the new client accounts with the Respondent were suitable for the clients.

56. Shortly after SW and BY became Approved Persons of the Respondent, SW and BY showed the CCO of the Respondent a form entitled "Acknowledgement and Release" that clients of their Former Member had apparently been asked to sign. According to the wording of the form, by signing the document, clients were purportedly indicating that they:

(a) 'acknowledge' the high risk of the investment portfolios that SW and BY had recommended to them; and

(b) 'release' the Member and its Approved Persons from their ordinary obligations to ensure the suitability of the investment recommendations that they made to clients and the orders that they accepted from clients.

57. The Respondent oversaw the amendment of the form for use by SW and BY on behalf of the Respondent and instructed SW and BY to arrange for clients of the Respondent to sign the amended Acknowledgement and Release form if the clients had been advised by SW and BY to invest primarily in mutual funds that were heavily concentrated in resource and precious metals investments such as gold.

58. By instructing former Approved Persons SW and BY to arrange for clients to sign the Acknowledgement and Release form instead of ensuring that accurate KYC information was obtained from the clients and that the investments held in their accounts with the Respondent were suitable, the Respondent contravened its supervisory and

suitability obligations and required clients to sign a document that purported to release the Respondent and the Approved Persons from liability for contraventions of their suitability obligations, contrary to MFDA Rules 2.2.1(a), (b), (c) and (e)(i), 2.1.1, 2.1.4 and 2.5.1 and MFDA Policy No. 2.

59. Sterling hired a new CCO in December 2014.

V. CONTRAVENTIONS

60. As described in paragraphs 14 and 17 of this Settlement Agreement, the Respondent admits that prior to its amalgamation with the Respondent, commencing in June 2010, A&Q failed to report to the MFDA that it had received a client complaint that alleged that an Approved Person, Barry Hunt, had engaged in personal financial dealings with a client and had potentially engaged in unauthorized outside business activities and/or unauthorized securities related business with a client, contrary to MFDA Rules 2.1.1, 2.1.4 and 2.11 and MFDA Policies No. 3 and 6.

61. As described in paragraphs 18-21 of this Settlement Agreement, the Respondent admits that prior to its amalgamation with the Respondent, commencing in June 2010, A&Q failed to conduct a reasonable supervisory investigation with respect to the conduct of an Approved Person, Barry Hunt, after it received a complaint on behalf of client VM alleging that Hunt had engaged in personal financial dealings and had potentially engaged in unauthorized outside business activities and/or securities related business that was not carried on for the account of the Member, contrary to MFDA Rules 2.5.1, 2.1.1 and MFDA Policy No. 2.

62. As described in paragraphs 14-17 of this Settlement Agreement, the Respondent admits that prior to its amalgamation with the Respondent, commencing in June 2010, A&Q failed to ensure that a complaint submitted on behalf of client VM with respect to the conduct of Approved Person, Barry Hunt, was handled promptly and fairly by qualified compliance staff and inappropriately permitted the subject of the complaint to

engage in the complaint handling process without supervision, contrary to MFDA Rules 2.11, 2.1.1 and 2.1.4 and MFDA Policy No. 3.

63. As described in paragraphs 25-28 of this Settlement Agreement, the Respondent admits that prior to its amalgamation with the Respondent, commencing in August 2010, A&Q failed to ensure that a complaint received from clients JH and JH that alleged that unsuitable leveraged investment recommendations had been made to the complainants by BO, a former Approved Person of A&Q, was handled promptly and fairly, contrary to MFDA Rules 2.11, 2.1.1 and 2.1.4 and MFDA Policy No. 3.

64. As described in paragraphs 37-39, 41, 48 and 50 of this Settlement Agreement, the Respondent admits that commencing in December 2012, the Respondent failed to conduct a reasonable supervisory investigation after receiving a complaint from client JN, and failed to ensure that the complaint was handled promptly and fairly by qualified compliance staff and inappropriately permitted the subjects of the complaint to engage in the complaint handling process without supervision, contrary to MFDA Rules 2.5, 2.11, 2.1.4, and 2.1.1, and MFDA Policies No. 2 and 3.

65. As described in paragraphs 54-58 of this Settlement Agreement, the Respondent admits that between May 2014 and March 2015, the Respondent: (a) failed to adequately supervise the conduct of Approved Persons SW and BY to ensure that: (i) accurate KYC information was recorded for each client; and (ii) the investments held in portfolios transferred to the Respondent from another Member and serviced by Approved Persons SW and BY and trade orders accepted for such clients thereafter were suitable for the clients; and (b) directed SW and BY to obtain signed documents from clients that purported to release the Respondent and its Approved Persons from liability for contraventions of their suitability obligations, contrary to MFDA Rules 2.2.1(a), (b), (c) and (e)(i), 2.1.1, 2.1.4 and 2.5.1 and MFDA Policy No. 2.

VI. TERMS OF SETTLEMENT

66. The Respondent agrees to the following terms of settlement:

(a) the Respondent shall pay a fine in the amount of $75,000;

(b) the Respondent shall pay compensation in the amount of $34,000 to former clients JH and JH (which payment has already been made);

(c) the Respondent shall pay costs to the MFDA in the amount of $20,000;

(d) the Respondent shall in the future comply with MFDA Rules 2.1.1, 2.1.4, 2.2.1, 2.5 and 2.11, MFDA Policy Nos. 2, 3 and 6 and the Respondent's policies and procedures concerning complaint handling by, among other things:

(i) ensuring that all information and events that should be reported to the MFDA on the Member Event Tracking System ("METS") are reported in a timely way;

(ii) ensuring that complaints are handled by qualified and impartial supervisory staff or compliance staff;

(iii) prohibiting the subjects of a complaint from taking any role in the complaint handling process that involves contact with the complainant concerning the subject-matter of the complaint;

(iv) ensuring that complaints are handled by the Member promptly and fairly; and

(v) taking reasonable supervisory action upon receipt of a complaint; and

(e) at least one senior officer of the Respondent will attend in person at the Settlement Hearing when this Settlement Agreement is presented to a Hearing Panel

VII. STAFF COMMITMENT

67. If this Settlement Agreement is accepted by the Hearing Panel, Staff will not initiate any proceeding under the By-laws of the MFDA against the Respondent or any of its officers or directors in respect of the facts set out in Part IV and the contraventions described in Part V of this Settlement Agreement, subject to the provisions of Part IX below. Nothing in this Settlement Agreement precludes Staff from investigating or initiating proceedings in respect of any facts and contraventions that are not set out in Parts IV and V of this Settlement Agreement or in respect of conduct that occurred outside the specified date ranges of the facts and contraventions set out in Parts IV and V, whether known or unknown at the time of settlement. Furthermore, nothing in this Settlement Agreement shall relieve the Respondent from fulfilling any continuing regulatory obligations.

IX. FAILURE TO HONOUR SETTLEMENT AGREEMENT

68. If this Settlement Agreement is accepted by the Hearing Panel and, at any subsequent time, the Respondent fails to honour any of the Terms of Settlement set out herein, Staff reserves the right to bring proceedings under section 24.3 of the By-laws of the MFDA against the Respondent or any of its officers or directors based on, but not limited to, the facts set out in Part IV of the Settlement Agreement, as well as the breach of the Settlement Agreement. If such additional enforcement action is taken, the Respondent agrees that such proceeding(s) may be heard and determined by a hearing panel comprised of all or some of the same members of the hearing panel that accepted the Settlement Agreement, if they are available.

Analysis and Decision

8. At the Settlement Hearing held on May 26, 2016, counsel for Staff made extensive submissions as to why this Settlement Agreement should be accepted by the Hearing Panel. Counsel for the Respondent made brief submissions in which she both adopted and supported Staff's submissions. Staff also provided Written Submissions.

9. Staff submitted, and the Hearing Panel agrees, that prior to approving a Settlement Agreement, a Hearing Panel must be satisfied that:

1. The facts admitted to by the Respondent constitute misconduct in contravention of the MFDA By-law No.1 (By-law), MFDA rules or policies or provincial securities legislation; and

2. The penalties contemplated in the Settlement Agreement fall within a reasonable range of appropriateness bearing in mind the nature and extent of the misconduct and all of the circumstances

As will be apparent from what follows, the Hearing Panel is satisfied that the foregoing requirements have been satisfied in this case.

10. It is well established that settlements such as the one before us serve the objective of protecting the public interest. As Mr. Justice Kelleher said in *British Columbia Securities Commission v. Seifert,* [2006] B.C.J. No. 225 at para. 49:

> Settlements assist the Commission to ensure that its overriding objective, the protection of the public, is met. Settlements proscribe activities that are harmful to the public. In so doing, they are effective in accomplishing the purposes of the statute. They provide means of reaching a flexible remedy that is tailored to address the interests of both the Commission and the person under investigation. Enforcement is rarely a concern because the settlement is voluntary.

11. The duty of a Hearing Panel sitting on a Settlement Hearing differs from that of a Hearing Panel at a contested hearing. As was stated in *Re Clark (Re),* [1999]:

> In a contested Hearing, the Hearing Panel attempts to determine the correct penalty. In a Settlement Hearing, the Hearing Panel takes into account the settlement process itself and the fact that the parties have agreed to the penalties set out in the Settlement Agreement. In our view, a Hearing Panel should not interfere lightly in a negotiated settlement and should not reject a Settlement Agreement unless it views the penalty as clearly falling outside a reasonable range of appropriateness. As has been said: "The settlement process is one of negotiation and compromise and the penalty imposed following a settlement will often be less onerous than one imposed following a Hearing where similar findings are made."

12. See also *Re Raymer* [2009] LNCMFDA 15 at para. 4:

> 4. It is generally agreed that hearing panels should not interfere lightly in a negotiated settlement as long as the penalties agreed upon are within a reasonable range of appropriateness given the conduct of the Respondent. (See, for instance, *Re Rodney Jacobson,* June 11, 2007, Prairie Regional Council, No. 200712; *Re Clark,* [1999] I.D.A.C.D. No. 40, and *Re Milewski,* [1999] I.D.A.C.D. No. 17.)

13. In past cases, when determining whether it would be appropriate to accept a proposed settlement, MFDA Hearing Panels have taken into account the following considerations:

(a) whether acceptance of the Settlement Agreement would be in the public interest and whether the penalty imposed will protect investors;
(b) whether the Settlement Agreement is reasonable and proportionate, having regard to the conduct of the Respondent as set out in the Settlement Agreement;
(c) whether the Settlement Agreement addresses the issues of both specific and general deterrence;
(d) whether the proposed settlement will prevent the type of conduct described in the Settlement Agreement from occurring again in the future;
(e) whether the Settlement Agreement will foster confidence in the integrity of the Canadian capital markets;
(f) whether the Settlement Agreement will foster confidence in the integrity of the MFDA; and
(g) whether the Settlement Agreement will foster confidence in the regulatory process itself.

14. Further, in previous cases, Hearing Panels have also taken into account the following additional factors when evaluating whether the penalties proposed in a settlement agreement should be accepted:

(a) The seriousness of the contraventions admitted to by the Respondent;
(b) The Respondent's past conduct, experience in the capital markets and disciplinary history;
(c) Whether the Respondent recognizes that the conduct was improper and has demonstrated remorse;
(d) The harm suffered by investors as a result of the Respondent's conduct;

(e) Whether the settlement agreement addresses both specific and general deterrence and will tend to prevent both the Respondent and others who participate in the capital markets from engaging in similar improper activity in the future;
(f) Whether acceptance of the settlement agreement would be in the public interest as the penalties agreed upon will protect investors and are reasonable and proportionate having regard to the conduct of the Respondent;
(g) Whether the settlement agreement will foster confidence in the integrity of the Canadian capital markets, the MFDA and the regulatory process; and
(h) Previous decisions in similar circumstances.

Complaint Handling

15. In this case, the allegations of misconduct concern primarily complaint handling violations of the Respondent and of A&Q, a former MFDA Member that amalgamated with the Respondent on May 29, 2015. In addition, the proceeding addresses a contravention of the Respondent's obligations to ensure that accurate KYC information is recorded for new clients and that assets transferred into a new account are suitable. A Member cannot contract out of its regulatory obligations by having clients sign a document that purports to release the Member and its Approved Persons from liability for contraventions of their suitability obligations.

16. Prompt and fair complaint handling is a baseline expectation of Members in the industry that is essential for effective supervision and fairness to clients. If complaint handling is not conducted promptly, the potential for effective investigation may be undermined and a complainant may be unfairly deprived of a timely resolution to the complaint. If a complaint is not handled fairly, the process fails investors and is inconsistent with the public interest. Based on their knowledge of the industry and regulatory standards and requirements, their access to information on record about the accounts of clients and the activities of their Approved Persons and in many cases bearing in mind the size and financial resources of Members, Members are in the best position to evaluate the merits of a complaint and have an obligation to do so fairly.

17. The subjects of a complaint are not impartial arbiters of the merits of a complaint. The subject of a complaint has a direct interest in minimizing the significance and negative implications of a complaint and self-interest in the resolution of any factual dispute or

misunderstanding in their own favour. Accordingly, the investigation of a complaint by the subject will ordinarily give rise to a conflict of interest that cannot be resolved in the best interest of the complainant.

18. Furthermore, when subjects of a complaint are involved in complaint handling, they may attempt to resolve the complaint unfairly, negotiate withdrawal or retraction of the complaint and minimize disclosure of the nature and implications of the complaint to compliance staff of the Member and to the regulator.

19. Whether concerns that are brought to light by a complaint are the result of intentional misconduct, negligence, or the failure of the Member or an Approved Person to appreciate and appropriately implement regulatory requirements or the policies and procedures of the Member, the Member's complaint handling process is an important source of information about potential problems that should be addressed. Accordingly, prompt, fair and reasonable complaint handling is a critical part of the compliance process. If it is undertaken properly and fairly, the process should:

(a) result in a transparent, objective, impartial and fair investigation and assessment of the merits of a complaint in accordance with MFDA Rule 2.11 and Parts I and III of MFDA Policy No. 3;
(b) provide the complainant and the subject of the complaint with a clear and balanced explanation of the conclusions reached and the implications of those conclusions for a resolution of the complaint in accordance with Part II of MFDA Policy No. 3;
(c) expose and enable Members and regulators to appropriately address cases of wrongdoing as a result of a reasonable supervisory investigation and disciplinary action in appropriate cases in accordance with Parts III and IV of MFDA Policy No. 3 and MFDA Rule 2.5;
(d) provide an opportunity for Members to promptly and fairly address client harm in accordance with MFDA Rule 2.11 and Part I of MFDA Policy No. 3; and
(e) give rise to improvements in supervisory processes in appropriate cases to ensure that other clients[1] are not similarly adversely affected in accordance with Part III of MFDA Policy No. 3.

[1] Identifying additional instances of similar client harm that have already occurred and preventing future cases of similar conduct and resulting harm.

Suitability of Investments

20. The obligation to exercise due diligence to ensure that investment orders that are accepted, recommendations that are made and investments that are held in client accounts of a Member are suitable for the clients is a core responsibility of any advisor or dealer that services client accounts in the securities industry.

21. In order to fulfill this obligation, Members and Approved Persons are required to obtain accurate and complete KYC information for each of their clients which facilitate an effective trade supervision process because the suitability of each client trade and client holding can be evaluated bearing in mind the KYC information on file for the client. In circumstances where a Member or Approved Person fails to accurately record the KYC information of clients, the ability to evaluate suitability is undermined.

22. It is incompatible with the standard of conduct and contrary to the public interest to contract out of regulatory obligations. Members and Approved Persons have a duty to ensure the suitability of the investments that their clients hold and cannot simply agree to disregard this fundamental obligation.

The Proposed Penalties

23. We have considered the factors that are frequently taken into account by Hearing Panels when assessing appropriateness of a Settlement Agreement and which are listed in paragraphs 13 and 14 above.

24. However, there is more to the analysis of a settlement agreement than simply trying to apply a myriad of factors in a vacuum. Hearing Panels quite properly look to Staff to provide guidance by identifying the important factors in each case and then explaining why it submits they have been satisfied or are consonant with the suggested penalty. In this case, Staff had identified the following factors and has proffered such explanations.

(a) Seriousness of the contraventions;
(b) Past conduct, experience and disciplinary history;
(c) Remorse;
(d) Deterrence;
(e) Public interest and proportionality;
(f) Integrity of the capital markets and the regulatory process;
(g) Previous decisions.

25. In respect of these matters, the Hearing Panel finds:

(a) Seriousness of the Contraventions: The contraventions that the Respondent has admitted to are serious. The Respondent and A&Q failed to ensure that fair, objective and balanced investigations were conducted into client complaints and that those complaints were resolved promptly and fairly in accordance with MFDA Rules 2.1.1, 2.1.4 and 2.11 and MFDA Policies No. 2 and 3. The Respondent also allowed two Approved Persons to record uniform KYC information for each client whose account they serviced and condoned an attempt by those Approved Persons to contract out of their suitability obligations to those clients.

(b) Past Conduct, Experience and Disciplinary History: The Respondent was subject to a previous disciplinary proceeding that resulted in a Settlement Agreement with Staff that was accepted by a Hearing Panel in August 2008 concerning certain compliance deficiencies including the failure of the member to implement an adequate two tier trade supervision process and to conduct and record appropriate evidence of trade supervision. Staff has advised us that the misconduct addressed in the previous disciplinary proceeding is unrelated to the contraventions admitted to in this case.

(c) Remorse: Staff has indicated that it is satisfied that the Respondent has demonstrated remorse, accepted responsibility for its conduct and regrets the contraventions of its regulatory misconduct. The Respondent cooperated with Staff's investigation of its conduct, agreed to pay substantial compensation to

clients JH and JH and entered into this Settlement Agreement which substantially reduced the length and complexity of the disciplinary proceedings that might otherwise have been necessary.

(d) Deterrence: The approval of the Settlement Agreement will result in the Respondent being ordered to pay (a) a fine in the amount of $75,000 and (b) the $34,000 compensation payment to clients JH and JH which we are advised has already been paid and (c) costs to the MFDA in the amount of $20,0000.
Collectively these penalties are substantial and will accomplish the goal of specific and general deterrence by sending a clear message to this Respondent and to other members of the MFDA that the contraventions that arose in this case are serious and the disciplinary consequences of such contraventions are substantial.

(e) Public Interest and Proportionality: Staff submits that it would be in the public interest to accept the Settlement Agreement and the Hearing Panel agrees that it would be. The Settlement Agreement is the result of significant negotiation and conveys clearly that the Respondent's misconduct constituted serious regulatory contraventions that have resulted in significant penalties.

(f) Integrity of the Capital Markets and the Regulatory Process: The Settlement Agreement reveals the extent and nature of the misconduct that the Respondent engaged in. In imposing significant penalties as a consequence, the Settlement Agreement serves to foster confidence in the integrity of the capital markets and the regulatory process.

Settlement Agreement Acceptance

26. As indicated in paragraph 6 above, the Settlement Agreement of May 26, 2016 is hereby accepted.

Penalties Imposed

27. The MFDA Penalty Guidelines are typically referred to by Hearing Panels when determining the appropriate penalties to be imposed in disciplinary proceedings. In Settlement Hearings, the purpose in doing so is for the Hearing panel to satisfy that the penalties agreed to by the parties are within the reasonable range of appropriateness.

28. Having considered the MFDA Penalty Guidelines as they apply to complaint handling, standard of conduct, conflict of interest, supervision and suitability and know your client, the Hearing Panel is satisfied that the recommendations have been complied with or exceeded.

29. In summary, the penalties, which we impose on the Respondent, are the following:

(a) A fine in the amount of $75,000;
(b) Payment of compensation to clients JH and JH in the amount of $34,000;
(c) Costs to the MFDA in the amount of $20,000.

DATED this 27th day of June, 2016.

"John Lorn McDougall"

John Lorn McDougall, Q.C.
Chair

"Guenther W. K. Kleberg"

Guenther W. K. Kleberg
Industry Representative

"Robert J. Wright"

Robert J. Wright, C.M., Q.C.
Industry Representative

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