

Re Royal Mutual Funds Inc.

IN THE MATTER OF

The Mutual Fund Dealer Rules

and

Royal Mutual Funds Inc.

2024 CIRO 77

Canadian Investment Regulatory Organization
Hearing Panel (Ontario District)

Heard: October 15, 2024 in Toronto, Ontario
Reasons for Decision: October 31, 2024

Hearing Panel:

Martin L. Friedland, C.C., K.C., Chair
Linda J. Anderson, Industry Representative
Leo Ciccone, Industry Representative

Appearances:

Alan Melamud, Senior Enforcement Counsel
David Di Paolo, Counsel for the Respondent, Royal Mutual Funds Inc.
Veronica Sjolin, Counsel for the Respondent, Royal Mutual Funds Inc.
David Barbaree, Senior Counsel, Royal Mutual Funds Inc.
Michael Walker, President, Royal Mutual Funds Inc.
Jennifer Wilson, CCO, Royal Mutual Funds Inc.

REASONS FOR DECISION

BACKGROUND

- ¶ 1 On July 29, 2024, the Canadian Investment Regulatory Organization (“CIRO”) issued a Notice of Settlement Hearing, announcing that a settlement hearing would be held in respect of Royal Mutual Funds Inc. (the “Respondent”).
- ¶ 2 Staff of CIRO and the Respondent entered into a Settlement Agreement, dated July 4, 2024 (the “Settlement Agreement”), which is attached to these reasons. The relevant facts are set out in some detail in Part IV of the Settlement Agreement.
- ¶ 3 The Respondent is a Dealer Member of CIRO, registered as a mutual fund dealer under securities legislation in all Canadian provinces and territories. The Respondent has been a Dealer Member of CIRO (formerly, a Member of the Mutual Fund Dealers Association) since October 25, 2001.
- ¶ 4 The question for the Panel is whether we should accept the Settlement Agreement.
- ¶ 5 At the conclusion of the Hearing, the Panel concluded that the Settlement Agreement should be accepted, with reasons to follow.
- ¶ 6 These are our reasons for accepting the Settlement Agreement.

CONTRAVENTIONS

¶ 7 In paragraph 4 of the Settlement Agreement, the Respondent admits the following violations of the Mutual Fund Dealer Rules:

“Between October 2001 and May 2021, the Respondent failed to establish and maintain an adequate system of controls and supervision to ensure requests were submitted for Canada Education Savings Grant payments on behalf of eligible client accounts, contrary to Mutual Fund Dealer Rules 2.5.1 and 2.1.1.”

¶ 8 Member Responsibility Rule 2.5.1 provides: “Each Member is responsible for establishing, implementing and maintaining policies and procedures to ensure the handling of its business is in accordance with the By-laws and Rules and with applicable securities legislation.”

¶ 9 Standard of Conduct Rule 2.1.1. provides, in part: “Each Member and each Approved Person of a Member shall: (a) deal fairly, honestly and in good faith with its clients; (b) observe high standards of ethics and conduct in the transaction of business; [and] not engage in any business conduct or practice which is unbecoming or detrimental to the public interest.”

TERMS OF SETTLEMENT

¶ 10 In paragraph 5 of the Settlement Agreement, Staff of CIRO and the Respondent agree to the following terms of settlement:

- (a) the Respondent shall pay a fine in the amount of \$125,000 on the date the Settlement Agreement is accepted, pursuant to Mutual Fund Dealer Rule 7.4.1.2(b);
- (b) the Respondent shall pay costs in the amount of \$10,000 on the date the Settlement Agreement is accepted, pursuant to Mutual Fund Dealer Rule 7.4.2;
- (c) the Respondent shall in the future comply with Mutual Fund Dealer Rules 2.5.1 and 2.1.1; and
- (d) a senior officer of the Respondent will attend in person on the date set for the Settlement Hearing.

FAILURE OF THE RESPONDENT TO SUBMIT REQUESTS FOR CANADA EDUCATION SAVINGS GRANT PAYMENTS

¶ 11 The Canada Education Savings Grant (“CESG”) is a widely used government program, pursuant to which the federal government of Canada will make monetary contributions to Registered Education Savings Plan (“RESP”) accounts based on the contributions made by the account holders.

¶ 12 The CESG is part of the Canada Education Savings Program that is intended to encourage Canadians to save for post-secondary education, and is administered by Employment and Social Development Canada, which is responsible for delivering and overseeing the CESG.

¶ 13 Under the Canada Education Savings Program, promoters contract with the Minister of Employment and Social Development via a “Promoter Agreement” to deliver the CESG. Royal Bank of Canada is a promoter and among other duties is responsible for submitting applications for the CESG to Employment and Social Development Canada. The Royal Bank of Canada did so on behalf of the Respondent.

¶ 14 The Respondent offered RESP accounts to its clients, pursuant to which they could apply for and receive the CESG. When opening an RESP account, clients would provide the required personal information and, where they wished to do so, execute the necessary forms to apply for the CESG.

¶ 15 In September 2020, Employment and Social Development Canada conducted a review of all promoters where contributions to the accounts had been made but the CESG had not been requested. The review included the RESP accounts of the Respondent’s clients.

¶ 16 On or about May 17, 2021, Employment and Social Development Canada issued a report, advising that after reviewing 30 of the Respondent’s RESP accounts, it had determined that in 16 instances, the CESG had not been requested on behalf of RESP accounts where the clients had provided the required information and executed the necessary documents to apply for the CESG.

¶ 17 Following receipt of the report, the Respondent undertook a review of all RESP accounts opened since 1998 and identified 1,475 RESP accounts that were eligible for the CESG but where it had not been requested.

¶ 18 As stated in paragraph 15 of the Settlement Agreement, the failure to process the applications for the CESG payments generally arose because the Respondent's back-office operational process did not contain a system or procedure to validate whether RESP accounts were incorrectly marked as not applying for the CESG or whether there were changes to a client's CESG application status. In some cases, this resulted in applications for accounts not being submitted notwithstanding that clients had requested that applications be made and the accounts were potentially eligible for CESG payments.

¶ 19 The failure to request the CESG described above, potentially resulted in 1,475 RESP accounts not receiving approximately \$1,045,046 in CESG payments.

¶ 20 The Respondent clearly failed to establish and maintain an adequate system of controls and supervision to ensure that applications for the CESG on behalf of its clients were being submitted.

¶ 21 The Respondent failed to detect that clients were not receiving CESG payments to which they were entitled until the issue was raised by Employment and Social Development Canada, as described above.

REMEDIATION EFFORTS AND CURRENT PRACTICES

¶ 22 Paragraphs 19 to 21 of the Settlement Agreement set out remediation efforts undertaken by the Respondent after the issues described above were identified. The Respondent

- (a) submitted (via its Promoter, RBC) requests for CESG payments to the Canada Educational Savings Program where the missed CESG requests arose in the three preceding years and were therefore still eligible for CESG from the government, resulting in \$295,405 recovered in CESG payments from the government for client RESP accounts;
- (b) credited RESP accounts approximately \$749,641 in compensation for client RESP accounts where the missed CESG payments could no longer be recovered from Canada Educational Savings Program (because the missed CESG requests were older than three years); and
- (c) with respect to the client RESP accounts covered by both (a) and (b) above, credited a further \$293,083 on account of lost growth from not having received the CESG payments earlier when the requests ought to have been made.

¶ 23 In total, the Respondent paid compensation of approximately \$1,042,724 in connection with the 1,475 client RESP accounts. Together with amounts recovered from the Canada Educational Savings Program, the RESP account holders received compensation of \$1,338,129.

¶ 24 As set out in paragraph 21 of the Settlement Agreement, the Respondent also implemented changes to their internal controls, including:

- (a) suspending a certain back-office operational process, which had resulted in RESP accounts being marked as not applying for the CESG, when the RESP account holders had in fact requested to apply for the CESG;
- (b) implementing a weekly review process whenever an RESP account is set on the back-office system to not apply the CESG;
- (c) implementing enhancements to the back-office system used by Approved Persons when entering RESP/CESG information to prevent Approved Person error, including, for example, an additional prompt and warning message if an Approved Person sets the CESG selection to "No"; and
- (d) updating policies and procedures to provide additional clarity to Approved Persons on the process of inputting RESP/CESG information on the back-office system.

ACCEPTANCE OF THE SETTLEMENT AGREEMENT

¶ 25 As stated above, the Panel accepted the terms of the Settlement Agreement. A panel can either accept or reject a settlement agreement. It cannot modify it.

¶ 26 The conduct in the present case was very serious. It involved a large number of investors and went on for a long period of time. A significant sum of money was at stake.

¶ 27 In the Respondent's favour is the fact that it had not previously been subject to a CIRO (or MFDA)

disciplinary proceeding.

¶ 28 The Respondent's remediation efforts and current practices described above are of particular importance in our accepting the Settlement Agreement. The loss to the clients was fully covered.

¶ 29 It is also important to note that the Respondent did not benefit from the misconduct. To the contrary, the Respondent did not receive the benefit of additional commissions that could have been earned on the CESG payments that would have been received by its clients and likely invested.

¶ 30 Further, it was the Respondent that reported the matter to CIRO after it was identified by the government.

¶ 31 The Respondent cooperated with CIRO and by entering into the Settlement Agreement recognized the seriousness of its conduct and saved CIRO the time, resources, and expenses associated with conducting a full hearing on the allegations.

¶ 32 The penalty of \$125,000 is a significant monetary penalty, which provides a large measure of general and specific deterrence to the Respondent and others in the securities industry.

¶ 33 The penalty is not out of line with the four comparable cases cited by counsel and, it should be noted, in all four cases the Respondent would have profited from the transactions. See *Re CIBC World Markets Inc.* 2022 LNIROC 34; *Re Canaccord Genuity Corp* 2021 LNIROC 35; *Re PEAK Securities Inc.* 2020 LNIROC 36; and *Re Raymond James* 2019 LNIROC 8. As stated above, the Respondent did not profit from its conduct.

¶ 34 Hearing panels should respect settlements worked out by the parties. The present Settlement was worked out by experienced counsel. A panel does not know what led to a settlement, what was given up by one party or the other during the negotiations, and what interest each party has in agreeing to resolve the matter. The Panel cannot go beyond the Settlement Agreement. There are almost always facts that play a role in the settlement which are not set out in the Settlement Agreement or brought to the attention of the Panel.

¶ 35 As a panel stated in *Re Keshet* [2014] MFDA File No. 201419 at paragraph 7, to take one of many such cases: "It is well established that hearing panels should not interfere lightly in negotiated settlements and should not reject a settlement agreement unless it views the proposed penalty clearly falling outside a reasonable range of appropriateness." There are many similar statements by Panels, stemming from the leading decision of *Re Milewski* [1999] I.D.A.C.D. No. 17, which stated:

"A District Council considering a settlement agreement will tend not to alter a penalty that it considers to be within a reasonable range, taking into account the settlement process and the fact that the parties have agreed. It will not reject a settlement unless it views the penalty as clearly falling outside a reasonable range of appropriateness."

¶ 36 The penalty and costs agreed to in the present case fall within "a reasonable range of appropriateness."

¶ 37 For the above reasons, the Panel accepted the Settlement Agreement.

Dated at Toronto, Ontario this 31 day of October 2024.

"Martin Friedland"
Martin Friedland K.C., Chair

"Linda J. Anderson"
Linda J. Anderson, Industry Representative

"Leo Ciccone"
Leo Ciccone, Industry Representative

Settlement Agreement

IN THE MATTER OF

The Mutual Fund Dealer Rules

and

Royal Mutual Funds Inc.

SETTLEMENT AGREEMENT

I. INTRODUCTION

¶ 1 The Canadian Investment Regulatory Organization, a consolidation of IIROC and the MFDA ("CIRO") will announce that it proposes to hold a hearing (the "**Settlement Hearing**") to consider whether, pursuant to Mutual Fund Dealer Rule 7.4.4.3, a hearing panel of the Ontario District Committee (the "**Hearing Panel**") of CIRO should accept the settlement agreement (the "**Settlement Agreement**") entered into between Staff of CIRO ("**Staff**") and Royal Mutual Funds Inc. (the "**Respondent**").

¶ 2 Staff and the Respondent consent and agree to the terms of this Settlement Agreement.

¶ 3 Staff and the Respondent jointly recommend that the Hearing Panel accept the Settlement Agreement.

II. CONTRAVENTIONS

¶ 4 The Respondent admits to the following violations of the Mutual Fund Dealer Rules:

Between October 2001 and May 2021, the Respondent failed to establish and maintain an adequate system of controls and supervision to ensure requests were submitted for Canada Education Savings Grant payments on behalf of eligible client accounts, contrary to Mutual Fund Dealer Rules 2.5.1 and 2.1.1.

III. TERMS OF SETTLEMENT

¶ 5 Staff and the Respondent agree and consent to the following terms of settlement:

(a) the Respondent shall pay a fine in the amount of \$125,000 on the date the Settlement Agreement is accepted, pursuant to Mutual Fund Dealer Rule 7.4.1.2(b);

(b) the Respondent shall pay costs in the amount of \$10,000 on the date the Settlement Agreement is accepted, pursuant to Mutual Fund Dealer Rule 7.4.2;

(c) the Respondent shall in the future comply with Mutual Fund Dealer Rules 2.5.1 and 2.1.1; and

(d) a senior officer of the Respondent will attend in person on the date set for the Settlement Hearing.

¶ 6 The Respondent consents to the Hearing Panel making a confidentiality order on the following terms:

If at any time a non-party to this proceeding, with the exception of the bodies set out in Mutual Fund Dealer Rule 6.3, requests production of or access to exhibits in this proceeding that contain personal information as defined by CIRO's Privacy Policy, then the Corporate Secretary's Office, Mutual Fund Dealer Division of CIRO shall not provide copies of or access to the requested exhibits to the non-party without first redacting from them any and all intimate financial and personal information, pursuant to Rules 1.8(2) and (5) of the Mutual Fund Dealer Rules of Procedure.

¶ 7 Staff and the Respondent agree to the settlement on the basis of the facts set out in this Settlement Agreement herein.

IV. AGREED FACTS

Registration History

¶ 8 The Respondent is a Dealer Member of CIRO registered as a mutual fund dealer under securities legislation in all Canadian provinces and territories. The Respondent has been a Dealer Member of CIRO (formerly, a Member of the MFDA) since October 25, 2001.

Failure to Submit Requests for Canada Education Savings Grant Payments

¶ 9 The Canada Education Savings Grant (“**CESG**”) is a government program, pursuant to which the federal government of Canada will make monetary contributions to Registered Education Savings Plan (“**RESP**”) accounts based on the contributions made by the account holders.

¶ 10 The CESG is part of the Canada Education Savings Program (“**CESP**”) that is intended to encourage Canadians to save for post-secondary education, and is administered by Employment and Social Development Canada (“**ESDC**”). The ESDC is responsible for delivering and overseeing the CESG.

¶ 11 Under the CESP, promoters contract with the Minister of Employment and Social Development via a “Promoter Agreement” to deliver the CESG. Royal Bank of Canada (“**RBC**”) is a promoter and among other duties is responsible for submitting applications for the CESG to EDC. RBC did so on behalf of the Respondent.

¶ 12 The Respondent offered RESP accounts to its clients, pursuant to which they could apply for and receive the CESG. When opening an RESP account, clients would provide the required personal information and, where they wished to do so, execute the necessary forms to apply for the CESG. The Respondent’s Approved Persons were required to input the personal information into the Respondent’s back office system and, where clients wished to apply for the CESG, set the CESG selection to “Yes”.

¶ 13 In September 2020, the ESDC conducted a review of all promoters where contributions to the accounts had been made but the CESG had not been requested. The review included RMFI RESP accounts. On or about May 17, 2021, ESDC issued a report, advising that after reviewing 30 RESP accounts, it had determined that in 16 instances, the CESG had not been requested on behalf of RESP accounts where the clients had provided the required information and executed the necessary documents to apply for the CESG.

¶ 14 Following receipt of the report, RMFI undertook a review of all RESP accounts opened since 1998 and identified 1,475 RESP accounts that were eligible for the CESG but where it had not been requested.

¶ 15 The failure to process the applications for the CESG payments generally arose because the Respondent’s back-office operational process did not contain a system or procedure to validate whether RESP accounts were incorrectly marked as not applying for the CESG or whether there were changes to a client’s CESG application status. In some cases, this resulted in applications for accounts not being submitted notwithstanding that clients had requested that applications be made and the accounts were potentially eligible for CESG payments.

¶ 16 The failure to request the CESG described above potentially resulted in 1,475 RESP accounts not receiving approximately \$1,045,046 in CESG payments.¹

¶ 17 The Respondent failed to establish and maintain an adequate system of controls and supervision to ensure that applications for the CESG on behalf of its clients were being submitted.

¶ 18 The Respondent failed to detect that clients were not receiving CESG payments to which they were entitled until the issue was raised by ESDC as described above.

Remediation Efforts and Current Practices

¶ 19 After the issues described above were identified, the Respondent implemented the following remediation efforts:

- (a) submitted (via its Promoter, RBC) requests for CESG payments to the CESP where the missed CESG requests arose in the three preceding years and were therefore still eligible for the CESG from the government, resulting in \$295,405 recovered in CESG payments from the government

¹ Because only the ESDC has discretion to deem accounts eligible for CESG payments, it is not known whether the ESDC would have necessarily done so for all potential 1,475 accounts in this case.

for client RESP accounts;

- (b) credited RESP accounts approximately \$749,641 in compensation for client RESP accounts where the missed CESG payments could no longer be recovered from the CESP (because the missed CESG requests were older than three years); and
- (c) with respect to the client RESP accounts covered by both (a) and (b) above, credited a further \$293,083 on account of lost growth from not having received the CESG payments earlier when the requests ought to have been made.

¶ 20 In total, the Respondent paid compensation of approximately \$1,042,724 in connection with the 1,475 client RESP accounts.²

¶ 21 The Respondent implemented changes to their internal controls, including:

- (a) suspending a certain back-office operational process, which had resulted in RESP accounts being marked as not applying for the CESG when the RESP account holders had in fact requested to apply for the CESG;
- (b) implementing a weekly review process whenever an RESP account is set on the back office system to not apply for the CESG;
- (c) implementing enhancements to the back-office system used by Approved Persons when entering RESP/CESG information to prevent Approved Person error, including, for example, an additional prompt and warning message if an Approved Person sets the CESG selection to “No”; and
- (d) updating policies and procedures to provide additional clarity to Approved Persons on the process of inputting RESP/CESG information on the back office system.

Additional Factors

¶ 22 The Respondent reported the issue described above to CIRO (formerly the MFDA) after ESDC identified it.

¶ 23 By entering into this Settlement Agreement, the Respondent has accepted responsibility for its misconduct and saved CIRO the time, resources, and expenses that would have otherwise been necessary to conduct a contested hearing of the allegations.

V. ADDITIONAL TERMS OF SETTLEMENT

¶ 24 This settlement is agreed upon in accordance with Mutual Fund Dealer Rule 7.4.4 and Rules 14 and 15 of the Mutual Fund Dealer Rules of Procedure.

¶ 25 The Settlement Agreement is subject to acceptance by the Hearing Panel. At or following the conclusion of the Settlement Hearing, the Hearing Panel may either accept or reject the Settlement Agreement. Settlement Hearings are typically held in the absence of the public pursuant to Mutual Fund Dealer Rule 7.3.5 and Rule 15.2(2) of the Mutual Fund Dealer Rules of Procedure. If the Hearing Panel accepts the Settlement Agreement, then the proceeding will become open to the public and a copy of the decision of the Hearing Panel and the Settlement Agreement will be made available at www.mfda.ca.

¶ 26 The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel. Unless otherwise agreed, any monetary penalties and costs imposed upon the Respondent are payable immediately, and any suspensions, revocations, prohibitions, conditions or other terms of the Settlement Agreement shall commence, upon the effective date of the Settlement Agreement.

¶ 27 Staff and the Respondent agree that if this Settlement Agreement is accepted by the Hearing Panel:

- (a) the Settlement Agreement will constitute the entirety of the evidence to be submitted at the settlement hearing, subject to Rule 15.3 of the Mutual Fund Dealer Rules of Procedure;

² Together with the amounts recovered from the CESP, the RESP account holders received compensation of \$1,338,129.

- (b) the Respondent agrees to waive any rights to a full hearing, a review hearing or appeal, including before the Board of Directors of CIRO or any securities commission with jurisdiction in the matter under its enabling legislation, or a judicial review or appeal of the matter before any court of competent jurisdiction;
- (c) except for any proceedings commenced to address an alleged failure to comply with this Settlement Agreement, Staff will not initiate any proceeding under the Mutual Fund Dealer Rules against the Respondent in respect of the contraventions described in this Settlement Agreement. Nothing in this Settlement Agreement precludes Staff from investigating or initiating proceedings in respect of any contraventions that are not set out in this Settlement Agreement, 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;
- (d) the Respondent shall be deemed to have been penalized by the Hearing Panel pursuant to Mutual Fund Dealer 7.4.1.2 for the purpose of giving notice to the public thereof in accordance with Mutual Fund Dealer Rule 7.4.5; and
- (e) neither Staff nor the Respondent will make any public statement inconsistent with this Settlement Agreement. Nothing in this section is intended to restrict the Respondent from making full answer and defence to any civil or other proceedings against the Respondent.

¶ 28 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 Mutual Fund Dealer Rule 7.4.3 against the Respondent or any of its officers or directors based on, but not limited to, the facts set out in this Settlement Agreement, as well as the breach of the Settlement Agreement. If such additional enforcement action is taken, the Respondent agrees that the 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 available.

¶ 29 If, for any reason, this Settlement Agreement is not accepted by the Hearing Panel, each of Staff and the Respondent will be entitled to any available proceedings, remedies and challenges, including proceeding to a disciplinary hearing pursuant to Mutual Fund Dealer Rules 7.3 and 7.4, unaffected by the Settlement Agreement or the settlement negotiations.

¶ 30 The terms of this Settlement Agreement will be treated as confidential by the parties hereto until accepted by the Hearing Panel, and forever if, for any reason whatsoever, this Settlement Agreement is not accepted by the Hearing Panel, except with the written consent of both the Respondent and Staff or as may be required by law. The terms of the Settlement Agreement will be released to the public if and when the Settlement Agreement is accepted by the Hearing Panel.

¶ 31 The Settlement Agreement may be signed in one or more counterparts which together shall constitute a binding agreement. A facsimile or electronic copy of any signature shall be as effective as an original signature.

DATED this 4th day of July, 2024.

“Micheal Walker”
 Royal Mutual Funds Inc.
 Per:

“AS”
 Witness - Signature

AS
 Witness - Print name

“Alan Melamud”
 Staff of the Canadian Investment Regulatory Organization
 Alan Melamud, Senior Enforcement Counsel

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