

Re Scotia Securities Inc.

IN THE MATTER OF:

The Mutual Fund Dealers Association of Canada

and

Scotia Securities Inc.

2023 CIRO 15

Canadian Investment Regulatory Organization
Hearing Panel (Ontario District)

Heard: December 21, 2022, by electronic hearing in Toronto, Ontario

Decision: December 21, 2022

Reasons for Decision: October 12, 2023

Hearing Panel:

Thomas J. Lockwood, K.C, Chair

Guenther W.K. Kleberg, Industry Representative

Kenneth P. Mann, Industry Representative

Appearances:

Shelly Feld, Director, Chief of Litigation

Paul Blasiak, Senior Enforcement Counsel for the Mutual Fund Dealers Association of Canada

David DiPaolo and Laura Poppel, Counsel for the Respondent

Neal Weston and Brent Curry, Respondent's Representatives

REASONS FOR DECISION

I. INTRODUCTION

¶ 1 By Notice of Settlement Hearing, dated December 19, 2022, the Mutual Fund Dealers Association of Canada ("MFDA") gave notice that an electronic hearing would be held before a hearing panel of the Central Regional Council of the MFDA ("Hearing Panel") on December 22, 2022, to consider whether, pursuant to Section 24.4 of MFDA By-law No. 1, the Hearing Panel should accept the settlement agreement ("Settlement Agreement") entered into between Staff of the MFDA and Scotia Securities Inc. ("Respondent").

¶ 2 On December 19, 2022, the MFDA issued a News Release giving public notice of the Settlement Hearing scheduled for December 21, 2022.

¶ 3 On December 21, 2022, the Hearing Panel was formally presented with the executed Settlement Agreement. This Settlement Agreement had been prepared in accordance with Section 24.4 of MFDA By-law No. 1, with the exception that the Notice of Settlement Hearing did not comply with the time provisions set out in Rule 15.2(1) of the MFDA Rules of Procedure.

¶ 4 Rule 15.2(1) provides as follows:

"15.2 Notice and Public Access

- (1) Except where a settlement is reached after the commencement of the hearing of a proceeding on its merits, a Hearing Panel shall not consider a Settlement Agreement unless at least 10 days' notice of the settlement hearing has been given by the Corporation in the

same manner as a notice of penalty pursuant to section 24.5 (Publication of Notice and Penalties) of MFDA By-law No. 1 specifying:

- (a) the date, time and place of the settlement hearing; and
- (b) the purpose of the settlement hearing with sufficient information to identify the Member or person involved and the general nature of the allegations which are the subject matter of the settlement.”

¶ 5 At the opening of the Settlement Hearing, MFDA Staff and the Respondent made a joint written and oral request that the Hearing Panel exercise its discretion pursuant to Rules 1.5 and 2.2(1)(a) of the MFDA Rules of Procedure to abridge the ordinary requirement set out in Rule 15.2 that a Settlement Hearing be heard only upon 10 days’ notice to the public. We were also mindful of the General Principles set out in Rule 1.3 of the MFDA Rules of Procedure.

¶ 6 Rules 1.3(1), 1.5(1)(b) and 2.2(1)(a) of the Rules of Procedure provide as follows:

1.3 General Principles

- (1) These Rules shall be liberally construed to secure the most expeditious and cost-effective determination of every proceeding on its merits consistent with the requirements of fairness.

1.5 General Powers of a Panel

- (1) A Panel may:
 - (b) waive or vary any of these Rules at any time, on such terms as it considers appropriate.

2.2 Extension or Abridgment of Time

- (1) The time for the performance of any obligation under these Rules may be extended or abridged:
 - (a) by a Panel, at any time on such terms as it considers appropriate;

¶ 7 The joint submission included that it is in the public interest that this Settlement Hearing be conducted in an expeditious manner and there would be no prejudice caused to members of the public if this request was granted because Settlement Hearings are held *in camera* and, therefore, even if the ordinary notice period was provided, members of the public would be excluded from the proceeding unless and until a Settlement Agreement is accepted by the Hearing Panel.

¶ 8 It was also submitted that this type of relief has been granted in previous disciplinary proceedings. The cases to which we were referred to include the following:

Sun Life Financial Services (Canada) Inc. (Re), [2018] Hearing Panel of the Central Regional Council, MFDA File No. 201775, Panel Decision dated March 5, 2018.

Quadrus Investments Services Ltd. (Re), [2022] Hearing Panel of the Central Regional Council, MFDA File No. 202166, Panel Decision dated January 20, 2022.

Investia Financial Services Inc. (Re), [2019] Hearing Panel of the Central Regional Council, MFDA File No. 201881, Panel Decision dated January 22, 2019.

¶ 9 After considering both the written and oral submissions of the parties, as well as the appropriate legislative provisions and the applicable case law, the Hearing Panel was, unanimously, of the view that this matter should proceed and that we would exercise our discretion to abridge the 10 day notice period in Rule 15.2.

¶ 10 The Hearing Panel then granted the joint request of the parties to move the proceedings “in camera” so that the Settlement Agreement could be considered in the absence of the public. This procedure is consistent with Rule 15.2(2).

¶ 11 The Hearing Panel then considered the provisions of the Settlement Agreement. After hearing submissions, both as to the applicable law and as to why this particular Settlement Agreement met the appropriate criteria, the Hearing Panel retired to consider whether we were in a position to accept the Settlement Agreement on the basis of the material before us.

¶ 12 After carefully considering the Settlement Agreement and the submissions of the parties, the Hearing Panel unanimously accepted the Settlement Agreement. We made an Order to this effect on December 21, 2022. At that time, we advised that written Reasons would follow. These are those Reasons.

II. SETTLEMENT AGREEMENT

¶ 13 The salient portions of the Settlement Agreement are as follows:

1. “II. CONTRAVENTIONS

4. The Respondent admits to the following violations of the By-laws, Rules or Policies of the MFDA:
 - a) Prior to April 2020, the Respondent failed to implement adequate policies and procedures and an adequate system of controls and supervision to ensure that its Approved Persons processed certain transactions as switches, rather than as redemptions and purchases, which resulted in the Approved Persons receiving increased performance credits which counted toward their sales targets, contrary to MFDA Rules 2.5.1 and 2.1.1 and MFDA Policy No. 2;
 - b) Prior to January 2021, the Respondent failed to implement adequate policies and procedures and an adequate system of controls and supervision to prevent its Approved Persons from establishing and subsequently cancelling pre-authorized contribution plans without adequate evidence of client authorization, which resulted in some of the Approved Persons receiving increased performance credits which counted toward their sales targets, contrary to MFDA Rules 2.5.1 and 2.1.1 and MFDA Policy No. 2;
 - c) Prior to July 2021, the Respondent failed to implement adequate policies and procedures and an adequate system of controls and supervision to prevent its Approved Persons from manually adjusting their sales results, which resulted in some of the Approved Persons receiving increased performance credits which counted toward their sales targets, contrary to MFDA Rules 2.5.1 and 2.1.1;
 - d) Between March 2020 and July 2020, at the onset of the COVID-19 pandemic, the Respondent failed to implement adequate policies and procedures and an adequate system of controls and supervision to ensure that it provided redemption cheques to clients in a timely manner, contrary to MFDA Rules 2.5.1 and 2.1.1;
 - e) Prior to April 13, 2021, the Respondent failed to implement adequate policies and procedures and an adequate system of controls and supervision to ensure that clients did not purchase certain mutual funds in non-registered accounts which, according to the funds' simplified prospectuses and fund facts documents, were not suitable to be held in such accounts, contrary to MFDA Rules 2.2.1, 2.5.1 and 2.1.1; and
 - f) Between November 24, 2021 and February 9, 2022, the Respondent failed to ensure that some client account transfer requests that were sent to one of its fax servers were processed in a timely manner, contrary to MFDA Rules 2.5.1 and 2.1.1.

III. TERMS OF SETTLEMENT

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

- a) the Respondent shall pay a fine in the amount of \$1,000,000 in certified funds upon acceptance of the Settlement Agreement, pursuant to s. 24.1.2(b) of MFDA By-law No.1;

- b) the Respondent shall pay costs in the amount of \$75,000 in certified funds upon acceptance of the Settlement Agreement, pursuant to s. 24.2 of MFDA By-law No.1;
- c) the Respondent shall in the future comply with MFDA Rules 2.5.1, 2.2.1, 2.1.1 and MFDA Policy No. 2; and
- d) a senior officer of the Respondent who is authorized to appear on behalf of the Respondent will attend by videoconference on the date set for the Settlement Hearing.

...

IV. AGREED FACTS

Registration History

¶ 15 The Respondent is registered in all provinces and territories in Canada as a mutual fund dealer and has been a Member of the MFDA since November 2001. At the material times described below, there were approximately 5,500 Approved Persons registered with the Respondent.

¶ 16 The Respondent's head office is located in Toronto, Ontario.

Overview

¶ 17 As described in this Settlement Agreement, the Respondent failed to implement and maintain adequate policies and procedures and an adequate system of controls and supervision to ensure that the handling of its business is in accordance with the MFDA's By-law, Rules and Policies.

¶ 18 The Respondent self-identified the extent of each of the contraventions.

¶ 19 As a result of contraventions #1-3 described in further detail below, some Approved Persons registered with the Respondent received performance credits from the Respondent which they were not otherwise entitled to receive. The performance credits counted toward the Approved Persons' sales targets. If an Approved Person achieved their sales target, he or she would be eligible to receive increased compensation from the Respondent.

¶ 20 As described below, the Respondent has and is developing substantial widespread process and governance enhancements to prevent contraventions similar to those addressed in the Settlement Agreement from occurring in the future and to ensure sufficient training of its Approved Persons (the "Control Remediation").

¶ 21 In addition to the Control Remediation, the Respondent has also developed a comprehensive remediation plan to identify all clients who may have been adversely impacted by the contraventions described herein. The scope of that remediation is particularized below (the "Client Remediation"). The Respondent's general approach to Client Remediation has been to provide remediation for all transactions that fit within certain criteria in order to ensure the broadest approach to addressing potential client harm.

Contravention #1 – Processing Transactions as Redemptions and Purchases Rather than as Switches

Background

¶ 22 At all material times, the Respondent did not award performance credits to its Approved Persons for transactions processed as switches.¹

¶ 23 When a transaction is processed as a redemption and purchase, rather than as a switch, the client is exposed to the risk of a change in value of the client's investments while the client is out of the market between the time of redemption and the time when the purchase trade is placed.

¶ 24 In 2019, the Respondent became aware that one of its Approved Persons had processed transactions in client accounts as redemptions and purchases, rather than as switches, and had received performance credits from the Respondent for the transactions. Had the Approved Person processed the transactions as switches, he would not have been eligible to receive any performance credits from the Respondent.

¹ A switch is a type of trade whereby a client's investments are transferred from one mutual fund to another, and the client's assets remain invested while the trade settles.

¶ 25 The Respondent then commenced an internal investigation to determine whether other Approved Persons had engaged in similar conduct.

The Respondent's Investigation

¶ 26 During the Respondent's internal investigation, the Respondent identified additional Approved Persons who processed redemptions and purchases in a short time frame as opposed to switches. The Respondent conducted a thorough and in-depth investigation of those Approved Persons including reviewing relevant documents and interviewing the Approved Persons and their supervisors, where appropriate.

¶ 27 The investigation revealed that:

- a) between November 1, 2017 to January 31, 2020, 46 Approved Persons registered with the Respondent processed approximately 757 transactions as redemptions and purchases rather than switches, which resulted in the Approved Persons receiving increased performance credits;
- b) some transactions were processed as redemptions and purchases pursuant to the instructions of the client, and therefore, the Approved Persons properly received performance credits for the transaction;
- c) a small number of the Approved Persons processed transactions as redemptions and purchases rather than as switches for the purpose of increasing their performance credits;
- d) the predominant response from the Approved Persons as to why they were engaging in the practice was that they misunderstood the procedures for when transactions ought to be processed as switches; and
- e) some clients suffered losses as a result of the delay caused by processing these transactions as redemptions and purchases rather than as switches (conversely, some clients also benefitted from gains).

¶ 28 Based on the findings described above, the Respondent admits that deficiencies existed in its policies and procedures and controls relating to transactions that ought to be processed as switches, including:

- a) the Respondent did not adequately train its Approved Persons to ensure that they understood that certain transactions ought to be processed as switches so that clients are not exposed to the risk of market loss while the trade settles; and
- b) the Respondent awarded performance credits to its Approved Persons when they processed transactions as redemptions followed by purchases, thereby incentivizing Approved Persons to process transactions as redemptions and purchases, rather than as switches, without implementing adequate controls and supervision to ensure that the transactions were processed in the best interests of the clients.

Approved Person Discipline

¶ 29 Of the 46 Approved Persons referred to in paragraph 19(a) above, 8 had resigned prior to the investigation. The Respondent determined that the remaining 38 Approved Persons had engaged in conduct warranting internal discipline, as they were determined to have breached the Respondent's Code of Conduct (a policy which outlines the Respondent's ethical standards and values to abide by).

¶ 30 The Respondent developed a matrix for the discipline of Approved Persons under investigation. This matrix provided for three levels of discipline which depended upon the severity of the misconduct:

- a) **Misconduct:** This level of discipline was imposed when there was a low level of misconduct (e.g. an honest misunderstanding or mistaken belief of the appropriate procedure for processing the transaction). The Approved Persons received a Written Warning and were required to successfully complete the IFSE Institute (the educational arm of Investment Funds Institute of Canada ("IFIC"))'s Ethics and Professional Conduct Course within six months;

- b) **Serious Misconduct:** This level of discipline was imposed when there was a moderate level of misconduct (e.g. some level of understanding of the appropriate procedure, but no clear intention to process the transaction in a certain manner for the purposes of increasing sales credit, and provided reasonable explanations for some transactions). The Approved Persons received a Final Warning for Serious Misconduct, were required to successfully complete IFIC's Ethics and Professional Conduct Course within six months, were placed under strict supervision for 1 year, and received a financial penalty; or
- c) **Egregious Misconduct:** This level of discipline was imposed when there was a high level of **misconduct** (e.g. initiated transactions for the purposes of increasing sales credit). These Approved Persons received Termination of Employment for Cause.

¶ 31 Of the 38 Approved Persons who were determined to have engaged in conduct warranting internal discipline for processing transactions as redemptions and purchases as opposed to switches, the discipline breakdown was as follows:

- a) 22 Approved Persons were determined to have engaged in Misconduct;
- b) 14 Approved Persons were determined to have engaged in Serious Misconduct; and
- c) 2 Approved Persons rose to the level of Egregious Conduct and were therefore terminated.

¶ 32 The Respondent has provided the results of its investigation to Staff. Staff will independently determine any enforcement action that will be taken against Approved Persons who engaged in such conduct.

Control Remediation

Procedure and Training Enhancements

¶ 33 Upon discovery of the issue, the Respondent established and implemented an ongoing educational campaign to ensure that all Approved Persons are aware of the circumstances in which it would be appropriate to process transactions by way of switch as opposed to a redemption and purchase. Among other things, on July 26, 2019, the Respondent sent a communication to all Approved Persons advising them when it is appropriate to execute transactions by way of switch.

¶ 34 In early 2020, the Respondent sent a communication to all Approved Persons which stated that if any performance credit was received for transactions processed as redemptions and purchases that should have instead been processed as a switch, it would be reversed effective from November 1, 2019.

¶ 35 In July 2019, the Respondent posted a communication on its internal website with respect to when it is appropriate to conduct transactions by way of switch as opposed to a redemption and purchase. In March 2020, the Respondent updated its training materials to particularize the circumstances in which transactions are to be processed by way of switch. In January 2022, additional training was prepared for Approved Persons respecting when a transaction should be processed by way of a switch, as opposed to a redemption and purchase.

System Enhancements

¶ 36 In addition, the Respondent took the following steps:

- a) In April 2020, the Respondent made a system enhancement to prevent its Approved Persons from receiving any performance credit in circumstances where a redemption and subsequent purchase occurred within 30 days;
- b) In May 2020, the Respondent reversed any performance credit applied since November 1, 2019 (FY20) which had been advanced to an Approved Person for a redemption and subsequent purchase which occurred within 30 days; and
- c) In April 2021, the Respondent implemented a system enhancement to improve record keeping and provide an automated system prompt which reminds Approved Persons that when a client intends to redeem or purchase a fund in the same fund family, and in the same currency, the transaction must be executed by way of switch.

Client Remediation

¶ 37 In order to ensure that clients did not suffer a loss as a result of transactions processed as redemptions and purchases in circumstances where they should have been processed by way of switch, the Respondent engaged Deloitte LLP (“Deloitte”) to assist it with assessing which clients were impacted and to determine the quantum of loss. When assessing impact to clients, the Respondent and Deloitte reviewed transactions that occurred during a 6 year period between June 1, 2014 and May 31, 2020. In doing so, the Respondent and Deloitte did not determine whether or not the client had instructed the Approved Person to proceed with the transaction in this manner, but rather assumed that a transaction processed by way of a redemption and purchase when it could have been processed by way of switch, was in scope for remediation with certain reasonable assumptions to account for client choice. As a result of this review, 9,982 clients have received remediation totaling \$3,747,242.92.²

Contravention #2 – Cancelled PACs

Background

¶ 38 A pre-authorized contribution plan (“PAC”) is a type of plan whereby an Approved Person arranges for withdrawals to be made from a client’s bank or similar account at regular intervals (e.g. bi-weekly or monthly) in order to purchase one or more pre-selected mutual funds in the client’s investment account.

¶ 39 In August 2018, two clients (spouses) complained to the Respondent that an Approved Person registered with the Respondent had, without the clients’ knowledge or authorization, established PACs in their accounts and then cancelled the PACs prior to when the first contribution was scheduled to be processed.

¶ 40 After receiving the complaint described above, the Respondent commenced an internal investigation to determine the extent to which its Approved Persons had established and cancelled PACs without client authorization, and whether the rationale for this activity may have been to generate performance credits from the Respondent which the Approved Persons were not otherwise entitled to receive.

The Respondent’s Investigation

¶ 41 During the Respondent’s internal investigation, the Respondent identified Approved Persons who had a high number of PACs that were set up but cancelled prior to the first contribution. In relation to those Approved Persons, the Respondent manually reviewed a sample of the identified transactions in order to determine whether or not there was adequate evidence that the Approved Person secured client authorization in relation to both setting up the PAC and the cancellation of the PAC.

¶ 42 The Respondent also reviewed any client complaints received during the six years preceding the investigation that concerned potentially unauthorized PACs.

¶ 43 Similar to contravention #1, the Respondent reviewed documents related to these transactions and interviewed Approved Persons where it appeared that they may not have had sufficient client authorization to set up a PAC.

¶ 44 The Respondent’s internal investigation revealed that:

- a) between November 1, 2017 to October 31, 2020, approximately 2,421 PACs were set up and subsequently cancelled. For the sample reviewed, in the large majority of those instances there was no documentary evidence of client authorization for the PAC set up and/or cancellation. Approved Persons involved in these transactions received performance credits when they set up the PACs even though, in most instances, the PACs were cancelled prior to when the first contribution was scheduled to be processed;
- b) upon further investigation, some PACs were set up and subsequently cancelled pursuant to the instructions of the client;

² A charitable donation will be made for those clients who would have been entitled to a payment of \$25 or less (3,024 clients for a total of \$28,791.90). The details of that charitable donation are particularized herein.

- c) 19 of the Approved Persons set up and subsequently cancelled PACs without client authorization specifically for the purpose of increasing their performance credits;
- d) the majority of Approved Persons failed to record adequate evidence of client authorization for the PAC set up and/or cancellation; and
- e) 56 Approved Persons were determined to have engaged in conduct warranting discipline.

¶ 45 Based on the findings described above, the Respondent admits that deficiencies existed in its policies and procedures and controls relating to establishing PACs for clients, including:

- a) the Respondent awarded performance credits to Approved Persons who set up a PAC or increased the contribution amount of a PAC, even if the PAC was subsequently cancelled without any contributions having been processed, without implementing adequate controls and supervision to ensure that the PACs were set up and cancelled in the best interests of the clients; and
- b) when an Approved Person cancelled a PAC, the Respondent did not require the Approved Person to document the reason for the PAC cancellation.

Approved Person Discipline

¶ 46 127 Approved Persons registered with the Respondent were identified for further investigation in relation to this issue. Of the 127 Approved Persons, 31 had resigned prior to the investigation. Of the 96 remaining Approved Persons that were investigated, 56 Approved Persons were determined to have engaged in conduct warranting internal discipline, as they were determined to have breached the Respondent's Code of Conduct.

¶ 47 As described above in paragraph 22, the Respondent developed a discipline matrix for the discipline of Approved Persons under investigation.

¶ 48 The discipline breakdown for the 56 Approved Persons referenced above was as follows:

- a) 25 were determined to have engaged in Misconduct;
- b) 17 were determined to have engaged in Serious Misconduct; and
- c) 14 were determined to have engaged in Egregious Misconduct and were therefore terminated.

¶ 49 The Respondent has provided the results of its investigation to Staff. Staff will independently determine any enforcement action that will be taken against Approved Persons who engaged in such conduct.

Control Remediation

¶ 50 The Respondent took the following steps to prevent this issue from occurring in the future:

- a) in April 2020, the Respondent sent a communication to all of its Approved Persons which stated that any performance credit received for PACs cancelled prior to the first contribution will be reversed effective from November 1, 2019;
- b) in October 2020, the Respondent sent a communication to all of its Approved Persons that effective November 1, 2020, performance credits for PACs will only be granted when the initial contribution is activated within 90 calendar days of the PAC set-up/increase date;
- c) the Respondent reversed all performance credits for all PACs in FY2020 (starting November 1, 2019) that were either: (1) set up and cancelled prior to first contribution; or (2) were set up to start more than 90 days in the future;
- d) in January 2021, the Respondent made a system enhancement to only provide performance credits where the first PAC payment occurred within 90 days of set up/increase;
- e) as of May 2021, the Respondent had reversed all performance credits for all PACs in FY2021 (first quarter) that were either: (1) set up and cancelled prior to first contribution; or (2) were set up greater than 90 days in the future;

- f) in June 2021, the Respondent implemented enhanced record keeping requirements related to non-face to face trading instructions, including the set up of PACs and all these trades are subject to review by Tier 1 Supervision;
- g) as of November 2021, the Respondent enhanced its system to require Approved Persons to document on their internal system a reason for PAC cancellation and the cancellation date. This field has been retained in the Respondent's database and monitoring of the reasons was developed and implemented in 2022;
- h) in November 2021, the Respondent provided training for Approved Persons regarding the requirement to take more detailed notes of telephone instructions; and
- i) in January 2022, the Respondent provided training for Approved Persons regarding best practices for PAC transactions, including guidance regarding recording the reasons for PAC cancellation and PAC cancellation date.

Client Remediation

¶ 51 In order to ensure that clients did not suffer a loss as a result of transactions in which the Approved Person did not have sufficient evidence of client authorization to set up a PAC, the Respondent engaged Deloitte to assist it with assessing which clients were impacted and to determine the quantum of loss. When assessing the impact to clients, the Respondent and Deloitte reviewed transactions that occurred during the 6 year period between November 1, 2014 to October 31, 2020. In so doing, the Respondent and Deloitte did not determine whether or not the client had instructed the Approved Person to proceed with the transaction, but rather assumed that, in the absence of adequate evidence of client authorization, the client should be remediated for any losses suffered. A small number of these transactions led to a client loss because the PAC was not cancelled prior to the client's first contribution and the market decreased after purchase. As a result of this review, 7 clients have received remediation totaling \$426.64.³

Contravention #3 – Adjustments to Sales Results

Background

¶ 52 In July 2019, the Respondent detected that one of its Approved Persons had manually adjusted his sales results on the Respondent's sales tracking system in some instances in order to receive performance credits that he was not otherwise entitled to receive.

¶ 53 The Respondent then commenced an internal investigation to determine whether other Approved Persons had engaged in similar conduct.

The Respondent's Investigation

¶ 54 During the Respondent's internal investigation, the Respondent identified 73 Approved Persons, which included 8 Branch Managers, who appeared to have engaged, or who supervised Approved Persons who engaged, in similar conduct during the period November 1, 2017 to October 31, 2020. However, 13 of these Approved Persons or Branch Managers had resigned prior to the investigation.

¶ 55 Of the remaining 60 Approved Persons or Branch Managers who had not resigned prior to the investigation, those who engaged (or supervised an Approved Person who engaged) in manual self-adjustments in FY2018 and FY2019, or who engaged (or supervised an Approved Person who engaged) in manual self-adjustments after the Respondent issued a communication in FY2020 to Approved Persons which cautioned against making manual self-adjustments, were interviewed. The remaining Approved Persons or Branch Managers who made (or supervised an Approved Person who made) manual self-adjustments in FY2020, but prior to the communication, were not interviewed, and instead completed questionnaires.

¶ 56 The Respondent's internal investigation revealed that the 65 Approved Persons performed a total of

³ A charitable donation will be made for those clients who would have been entitled to a payment of \$25 or less (224 accounts for a total of \$674.26). The details of the donation are particularized herein.

approximately 8,734 manual sales adjustments. However, the Respondent was unable to reasonably determine the number of these manual sales adjustments that were adjusted for legitimate and appropriate reasons, as compared to those that were adjusted to receive performance credits that the Approved Person was not otherwise entitled to receive.

¶ 57 Based on the findings described above, the Respondent admits that deficiencies existed in its policies and procedures and controls relating to sales adjustments made by Approved Persons, insofar as the Respondent permitted its Approved Persons to manually adjust their sales results on the Respondent's sales tracking system without receiving prior managerial approval, thereby failing to prevent Approved Persons from adjusting their sales results for the sole purpose of receiving increased performance credits.

Approved Person Discipline

¶ 58 The Respondent determined that the 60 Approved Persons and Branch Managers who had not resigned prior to the investigation had engaged in conduct warranting internal discipline, as they were determined to have breached the Respondent's Code of Conduct.

¶ 59 As described above in paragraph 22, the Respondent developed a discipline matrix for the discipline of Approved Persons under investigation.

¶ 60 The discipline breakdown for the 60 Approved Persons and Branch Managers referenced above was as follows:

- a) 14 were determined to have engaged in Misconduct;
- b) 28 were determined to have engaged in Serious Misconduct; and
- c) 18 were determined to have engaged in Egregious Misconduct and were therefore terminated.

¶ 61 Respondent has provided the results of its investigation to Staff. Staff will independently determine any enforcement action that will be taken against Approved Persons who engaged in such conduct.

Control Remediation

¶ 62 In September 2020, the Respondent introduced a pilot project in Atlantic Canada to centralize the approval of manual adjustments and the full country was moved to a centralized approval model by the end of July 2021. The network is concurrently being monitored to identify any transactions taking place outside of the centralized approval model.

¶ 63 The Respondent implemented a system enhancement to its sales tracking software on April 17, 2022 which removed the ability for Approved Persons to make manual adjustments in branches.

¶ 64 There was no client loss or impact in respect of this contravention.

Contravention #4 – Delays in Issuing Redemption Cheques to Clients

Background

¶ 65 In or around the fall of 2020, the Respondent received client complaints concerning the fact that clients were not receiving redemption cheques in a timely manner.

¶ 66 After receiving the complaints, the Respondent commenced an internal investigation. The investigation revealed that the delays occurred primarily between May and July 2020, and were due to a temporary business process that the Respondent implemented in response to the onset of the COVID-19 pandemic and the switch from in-office to remote work for the department responsible for mailing cheques.

¶ 67 As a temporary measure, the mailing of cheques was assigned to another operations department that continued to work onsite. This switch resulted in delays, which were not reported to the original department in a timely manner. The delivery of cheques by Canada Post during this period may have also contributed to the delay in clients receiving cheques.

¶ 68 Upon identification of the issue in July 2020, the Respondent immediately reverted to its original

processes and restored responsibility for mailing cheques to clients to the department that had been responsible for that function prior to the pandemic. The Respondent was thereby able to correct the delays in mailing out cheques quickly.

Client Remediation

¶ 69 The Respondent conducted an analysis to determine how many cheques may have been impacted by delays causing a client loss.

¶ 70 The Respondent determined that approximately 1,331 cheques were not cashed within 30 calendar days of issuance and therefore may have caused the client who received the cheque to incur a loss (i.e., if the client invested the funds into another investment product late and the market had appreciated during the period of the delay). The Respondent determined that it would compensate all clients who cashed their cheques more than 30 calendar days following issuance, with an amount representing the potential loss of opportunity for those clients. In doing so, the Respondent did not determine whether or not the cheques cashed more than 30 calendar days following issuance were a result of delays in the Respondent's internal process, Canada Post, or by the client but rather assumed that in the absence of evidence of the cause of the delay that the client should be remediated for any losses suffered.

¶ 71 As a result of this review, 827 accounts have received remediation totaling \$740,145.⁴

Control Remediation

¶ 72 In August 2021, the Respondent launched an external electronic payment clearing service to enable the electronic processing of transfers out to participating financial institutions, rather than relying on physical cheque issuance, which eliminates the need for the vast majority of physical cheques that the Respondent issues to other financial institutions.

¶ 73 In November 2021, the Respondent implemented additional procedures for cheques processed outside of the above referenced system to ensure that the cheques were being transferred in a timely manner.

Contravention #5 – Purchases of Funds in Non-Registered Accounts

Background

¶ 74 At all material times, the Respondent offered the Scotia NASDAQ Index Fund, Scotia CanAM Index Fund and Scotia International Equity Index Fund (the "Funds") for sale to its clients.

¶ 75 At all material times, the Funds' simplified prospectuses and fund facts documents stated that the Funds were not suitable to be purchased in non-registered accounts because their distributions were considered income, which is taxed at a higher rate than capital gains when received outside of a registered account.

¶ 76 On April 13, 2021, as a result of client complaints, it came to the Respondent's attention that some of the Respondent's clients had purchased units of the Funds in their non-registered accounts.

¶ 77 The Respondent then commenced an internal investigation to determine the extent of the issue.

The Respondent's Investigation

¶ 78 The Respondent's internal investigation revealed that:

- a) between January 1, 2015 and March 31, 2021, 2,943 clients of the Respondent purchased units of the Funds in their non-registered accounts; and
- b) the Respondent's system did not have a sufficient monitoring system in place in order to identify that the purchases of the Funds in non-registered accounts were unsuitable according to the Funds' simplified prospectuses and fund facts documents.

¶ 79 Based on the findings that were made at the conclusion of its investigation as described above, the

⁴ A charitable donation will be made for those clients who would have been entitled to \$25 or less (59 accounts for a payment of \$379.52). The details of that charitable donation are particularized herein.

Respondent admits that it failed to put in place adequate controls to ensure that the Funds were not purchased in non-registered accounts, in accordance with the Funds' simplified prospectuses and fund facts documents.

Client Remediation

¶ 80 By virtue of the Funds' distributions being treated as income as opposed to capital gains for Funds held in non-registered accounts, the Respondent will pay compensation to all clients who purchased these affected Funds in their non-registered accounts between January 1, 2015 to December 31, 2021 and received a distribution as income. Specifically, the Respondent will pay compensation to each client to compensate them based upon an assumed tax rate for taxes that would not otherwise have been payable had the returns been treated as capital gains. Clients will be informed that they are eligible to submit complaints to the Respondent if they believe that the compensation is insufficient to account for their loss.

¶ 81 The Respondent will pay a total of at least \$6 million in compensation to clients.

Control Remediation

¶ 82 The Funds have now been restructured, on notice to holders of the Funds, such that one of the Funds was merged into a different Fund, and the investment objectives of the other two Funds were amended. As a result of the restructuring, there is no longer a restriction in the Funds' simplified prospectuses and fund facts documents that they cannot be purchased in non-registered accounts.

Contravention #6 – Failure to Process Fax Transfer Requests in a Timely Manner

¶ 83 The Respondent utilizes computer fax servers to process certain transfer requests received from clients by fax.

¶ 84 On November 24, 2021, the Respondent had a third party vendor make a software update to some of its fax servers. Unbeknownst to the Respondent at the time, the third party vendor failed to make the software update to one of the fax servers (the "Fax Server").

¶ 85 As a result, between November 24, 2021 and February 9, 2022, the Respondent failed to process approximately 2,077 non-ATON (manual) transfer requests that were sent to the Fax Server in respect of 1,744 clients.

¶ 86 On February 9, 2022, the Respondent discovered that the third party had failed to make the software update to the Fax Server as described above, and the Respondent arranged for the software update to be immediately made to the Fax Server.

¶ 87 The Respondent then immediately took steps to process the transfer requests that had been sent to the Fax Server between November 24, 2021 and February 9, 2022.

¶ 88 The Respondent was able to retrieve and process the transfer requests that had been sent to the Fax Server between December 2, 2021 and February 9, 2022.

¶ 89 The Respondent was not able to retrieve the transfer requests that had been sent to the Fax Server between November 24, 2021 and December 1, 2021. However, the Respondent contacted several financial institutions that had sent a large number of transfer requests to the Fax Server, and the Respondent concluded that almost all of the transfer requests had been processed (i.e. by virtue of being sent to another fax server or being re-sent to the Fax Server after December 1, 2021).

Client Remediation

¶ 90 The Respondent conducted a review to identify all clients who were affected by the delay in processing transfer requests to the Fax Server. As a result of this review, approximately 1,702 clients will receive remediation totaling at least \$350,000. Clients will be informed that they are eligible to submit complaints to the Respondent if they believe that the compensation is insufficient to account for their loss.

Additional Factors

Proactive and Exceptional Cooperation

¶ 91 The Respondent conducted an extensive review of the contraventions described above and provided the

MFDA with regular progress updates. Voluntarily and at its own initiative, the Respondent developed the Control and Client Remediation in respect of all of the foregoing contraventions. The Respondent conducted investigations of all Approved Persons who were identified during its internal investigations and reported the results of those investigations to Staff.

¶ 92 The Respondent engaged legal counsel and Deloitte to ensure that its investigation was thorough and all appropriate client remediation was considered and effected. The Respondent promptly shared the detailed findings of the review with Staff and otherwise fully cooperated with Staff's regulatory investigation.

¶ 93 Staff has considered this proactive and exceptional cooperation as a factor in agreeing to the sanction set out above.

¶ 94 By entering into this Settlement Agreement and conducting its own investigation, including a fulsome remediation plan, the Respondent has saved the MFDA the time, resources, and expenses associated with conducting a contested hearing on the allegations.

Governance Remediation

¶ 95 In 2021, the Respondent expanded the composition of its internal governance committee by adding additional leadership from key stakeholder groups supporting the Respondent to strengthen the coordination and oversight processes.

¶ 96 The Respondent completed a review of the governance over trade processing, including a review of the organizational structure, roles and responsibilities, issues management and reporting, and has submitted a report to its internal governance committee that has identified any additional risks and opportunities for control enhancements. This report has also been submitted to the Respondent's board. The Respondent will continue to monitor these issues and provide regular status updates to the Respondent's internal governance committee.

Donation to the Canadian Foundation for Economic Education

¶ 97 As referenced above, the Respondent will be making a charitable donation to the Canadian Foundation for Economic Education, a not-for-profit institution, in respect of client remediation amounts that are less than \$25."

V. THE LAW

¶ 98 The impugned conduct of the Respondent involved an alleged breach of the following MFDA Rules and Policy:

a) Rule 2.1.1 states as follows:

"2.1.1 Standard of Conduct.

Each Member and each Approved Person of a Member shall:

- i) deal fairly, honestly and in good faith with its clients;
- ii) observe high standards of ethics and conduct in the transaction of business;
- iii) not engage in any business conduct or practice which is unbecoming or detrimental to the public interest; and
- iv) be of such character and business repute and have such experience and training as is consistent with the standards described in this Rule 2.1.1, or as may be prescribed by the Corporation."

b) Rule 2.2.1 states, in part, as follows:

"2.2.1 "Know Your Client"

Each Member and Approved Person shall use due diligence:

- i) to learn the essential facts relative to each client and to each order or account accepted;

- ii) to ensure that the acceptance of any order for any account is within the bounds of good business practice;
 - iii) to ensure that each order accepted or recommendation made, including recommendations to borrow to invest, for any account of a client is suitable for the client based on the essential facts relative to the client and any investments within the account;”
- c) Rule 2.5.1 states as follows:
- “2.5.1 Member Responsibilities
- 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, Rules and Policies and with applicable securities legislation.”
- d) Policy No. 2 establishes minimum industry standards for account supervision. The Policy requires each Member to, among other things, “establish policies and procedures to identify trends or patterns that may be of concern.”

¶ 99 We found that the following contraventions were established:

Contravention #1 – Processing Transactions as Redemptions and Purchases Rather than as Switches

¶ 100 In the Settlement Agreement, the Respondent admitted that between November 1, 2017 and January 31, 2020, 46 Approved Persons, registered with the Respondent, processed approximately 757 transactions as redemptions and purchases, rather than as switches, which resulted in the Approved Persons receiving increased performance credits.

¶ 101 While some of these transactions were legitimately done pursuant to the instructions of the clients, and others were done for the specific purpose of increasing the Approved Person’s performance credit, the predominant response from the Approved Persons was that they misunderstood the procedures for when transactions ought to be processed as switches.

¶ 102 When a transaction is processed as a redemption and purchase, rather than as a switch, the client is exposed to the risk of a change in value of the client’s investment while the client is out of the market between the time of the redemption and the time when the purchase trade is made.

¶ 103 As stated by the Hearing Panel in *Hale (Re)* with regard to an Approved Person who processed transactions as redemptions and purchases rather than as switches:

“Using responsible business judgment, the Respondent ought to have recognized that he was exposing his clients to a risk of loss from a possible change in the value of their funds while the trade settled and the clients’ assets were not invested.”

Hale (Re), [2020] Hearing Panel of the Prairie Regional Council, MFDA File No. 202046, Panel Decision dated March 9, 2021, at para. 28.

¶ 104 As detailed in paragraphs 11, 14 and 20 of the Settlement Agreement, the Respondent awarded performance credits to its Approved Persons when they processed transactions as redemptions followed by purchases. It did not award performance credits for transactions processed as switches. The performance credits counted towards the Approved Person’s sales targets. If an Approved Person achieved the sales target, he or she would be eligible to receive increased compensation from the Respondent.

¶ 105 The Respondent’s system had the effect of incentivizing Approved Persons to process transactions in a manner that was not in the best interests of the clients.

¶ 106 Previous MFDA Hearing Panels have held that when an Approved Person processes transactions as redemptions and purchases, rather than as switches, in order to ensure that the transactions count toward the Approved Person’s sales targets, the Approved Person has breached the standard of conduct set out in Rule 2.1.1, and has entered into a conflict of interest with the relevant client(s).

Hale (Re), *supra*.

Leonard (Re), [2020] Hearing Panel of the Central Regional Council, MFDA File No. 201919, Panel Decision dated October 2, 2020.

Eng (Re), [2022] Hearing Panel of the Central Regional Council, MFDA File No. 202205, Panel Decision dated June 29, 2022.

¶ 107 The Respondent admits that it failed to implement adequate policies and procedures and an adequate system of controls and supervision to ensure that its Approved Persons processed certain transactions as switches, rather than as redemptions and purchases, which resulted in the Approved Persons receiving increased performance credits which counted toward their sales targets, contrary to MFDA Rules 2.5.1 and 2.1.1 and MFDA Policy No. 2.

¶ 108 The Respondent also admitted that it did not adequately train its Approved Persons to ensure that they understood that certain transactions ought to be processed as switches so that clients are not exposed to the risk of market loss while the trade settles.

Contravention #2 – Cancelled PACs

¶ 109 In the Settlement Agreement, the Respondent admitted that between November 1, 2017 and October 31, 2020, approximately 2,421 pre-authorized contribution plans (“PACs”) were set up and subsequently cancelled. A PAC is a type of plan whereby an Approved Person arranges for withdrawals to be made from a client’s bank or similar account at regular intervals (eg. bi-weekly or monthly) in order to purchase one or more pre-selected mutual funds in the client’s investment account.

¶ 110 While some of these transactions were legitimately done pursuant to the instructions of the clients, and others were done for the specific purpose of increasing the Approved Person’s performance credit, in the large majority of cases there was no documentary evidence that client authorization was obtained for the PAC set up and/or cancellation.

¶ 111 Approved Persons received performance credits when they set up the PAC even if the PAC was cancelled prior to when the first contribution was scheduled to be processed. The Respondent did not require the Approved Person to document the reason for the PAC cancellation.

¶ 112 As with all mutual fund trades, a PAC transaction must always be completed at the direction or with the authorization of the client.

Subzwari (Re), [2022] Hearing Panel of the Central Regional Council, MFDA File No. 202159, Panel Decision dated May 10, 2022, at para. 12.

¶ 113 Previous MFDA Hearing Panels have held that creating and cancelling PAC transactions in client accounts, without the clients’ knowledge or approval and for the purpose of meeting sales goals, is a contravention of the standard of conduct set out in MFDA Rule 2.1.1.

Subzwari (Re), *supra*, at para. 16.

Pattenden (Re), [2014] Hearing Panel of the Prairie Regional Council, MFDA File No. 201354, Panel Decision dated August 18, 2014.

¶ 114 As stated by the Hearing Panel in *Subzwari (Re)*:

“By establishing false PACs in the accounts of clients, and subsequently cancelling the PACs in order to obtain credit towards achieving sales targets, the Respondent failed to deal fairly, honestly and in good faith with clients, failed to observe high standards of conduct in the transaction of business and engaged in conduct which is unbecoming and detrimental to the public interest.”

Subzwari (Re), *supra*, at para. 18.

¶ 115 The processing of unauthorized PAC transactions is serious misconduct as it results in the potential for client loss, client abuse and loss of investor confidence in the capital markets.

¶ 116 When an Approved Person obtains the client’s authorization to process a PAC transaction, it is essential for the Member to take proper steps to ensure that the Approved Person maintains adequate evidence of the

client's authorization. Otherwise, the Member cannot confirm that the client was aware of and had, in fact, provided authorization to proceed with the transaction.

¶ 117 As stated by the Hearing Panel in *Garries (Re)*:

“The failure by an Approved Person to document a client's authorization of a trade may give rise to ramifications that are similar to those that result from the use of pre-signed account forms. Such ramifications include the destruction of the audit trail and the frustration of the Member's ability to respond to inquiries and complaints from clients concerning the propriety of trading activity in their accounts.”

Garries (Re), [2016] Hearing Panel of the Prairie Regional Council, MFDA File No. 201605, Panel Decision dated November 14, 2016, at para. 54.

¶ 118 The Respondent admits that it failed to implement adequate policies and procedures and an adequate system of controls and supervision to prevent its Approved Persons from establishing and subsequently cancelling PACs without adequate evidence of client authorization, which resulted in some of the Approved Persons receiving increased performance credits which counted towards their sales targets, contrary to MFDA Rules 2.5.1 and 2.1.1 and MFDA Policy No. 2.

Contravention #3 – Adjustment to Sales Results

¶ 119 In the Settlement Agreement, the Respondent admitted that 60 of its Approved Persons performed a total of approximately 8,734 manual sales adjustments. However, the Respondent was unable to determine the number of these manual sales adjustments that were adjusted for legitimate purposes as compared to those that were adjusted to receive performance credits that the Approved Person was not otherwise entitled to receive.

¶ 120 There was no client loss or impact in respect of this contravention.

¶ 121 When an Approved Person manually adjusts his or her sales targets for the sole purpose of meeting these targets, he or she engages in dishonest conduct, which damages the reputation of the mutual fund industry.

¶ 122 The Respondent admitted that deficiencies existed in the policies and procedures and controls relating to sales adjustments made by Approved Persons, insofar as the Respondent permitted its Approved Persons to manually adjust their sales results on the Respondent's sales tracking system without receiving prior managerial approval, thereby failing to prevent Approved Persons from adjusting their sales results for the sole purpose of receiving general performance credits. The Respondent admitted that this failure to implement adequate policies and procedures and an adequate system of controls and supervision was contrary to MFDA Rules 2.5.1 and 2.1.1.

Contravention #4 – Delays in Issuing Redemption Cheques to Clients

¶ 123 In the Settlement Agreement, the Respondent admitted that there was a delay in providing redemption cheques to clients. This occurred primarily between May and July 2020.

¶ 124 The delays were due to a temporary business practice that the Respondent implemented in response to the onset of the COVID-19 pandemic and the switch from in-office to remote work for the department responsible for mailing cheques. As a temporary measure, the mailing of cheques was assigned to another operations department that continued to work onsite. This switch resulted in delays which were not reported to the original department in a timely manner.

¶ 125 Upon identification of the issue in July 2020, the Respondent immediately reverted to the original processes and restored responsibility for mailing cheques to clients to the department that had been responsible for that function prior to the pandemic.

¶ 126 Previous MFDA Hearing Panels have held that the failure to process transactions in a timely manner constitutes regulatory misconduct.

ASL Direct Inc. and Leemhuis (Re), [2011] Hearing Panel of the Central Regional Council, MFDA File No. 200832, Panel Decision dated February 8, 2011.

Savoy (Re), [2017] Hearing Panel of the Atlantic Regional Council, MFDA File No. 2016108, Panel Decision dated November 20, 2017.

Bolt (Re), [2013] Hearing Panel of the Central Regional Council, MFDA File No. 201305, Panel Decision dated October 11, 2013.

¶ 127 The Respondent admits that, at the onset of the COVID-19 pandemic, it failed to implement adequate policies and procedures and an adequate system of controls and supervision to ensure that it provided redemption cheques to clients in a timely manner, contrary to MFDA Rules 2.5.1 and 2.1.1.

Contravention #5 – Purchases of Funds in Non-Registered Accounts

¶ 128 The Respondent offered the Scotia NASDAQ Index Fund, Scotia CanAM Index Fund and Scotia International Equity Index Fund (the “Funds”) for sale to its clients.

¶ 129 The Funds’ simplified prospectuses and fund facts documents stated that the Funds were not suitable to be purchased in non-registered accounts because their distributions were considered income, which is taxed at a higher rate than capital gains when received outside of a registered account.

¶ 130 In the Settlement Agreement, the Respondent admitted that between January 1, 2015 and March 31, 2021, 2,943 clients of the Respondent purchased units of the Funds in their non-registered accounts.

¶ 131 Previous MFDA Hearing Panels have held that when a Member fails to implement adequate policies and procedures and adequate controls and supervision to ensure that investments held in client accounts are suitable for the clients, the conduct is contrary to MFDA Rules, including Rule 2.2.1.

Sun Life Financial Services (Canada) Inc. (Re), *supra*.

HollisWealth Advisory Services Inc. (Re), [2015] Hearing Panel of the Central Regional Council, MFDA File No. 201532, Panel Decision dated December 8, 2015.

Investia Financial Services Inc. & FundEX Investments Inc. [2012] Hearing Panel of the Central Regional Council, MFDA File No. 200932 and 201031, Panel Decision dated March 26, 2012.

¶ 132 The Respondent admits that it failed to implement adequate policies and procedures and an adequate system of controls and supervision to ensure that clients did not purchase certain mutual funds in non-registered accounts which, according to the funds’ simplified prospectuses and fund facts documents, were not suitable to be held in such accounts, contrary to MFDA Rules 2.2.1, 2.5.1 and 2.1.1.

Contravention #6 – Failure to Process Fax Transfer Requests in a Timely Manner

¶ 133 In the Settlement Agreement, the Respondent admitted that it utilizes computer fax servers to process certain transfer requests from clients by fax.

¶ 134 On November 21, 2021, the Respondent had a third party vendor make a software update to some of its fax servers. Unbeknownst to the Respondent at the time, the third party vendor failed to make the software update to one of the fax servers. As a result, between November 2021 and February 9, 2022, the Respondent failed to process approximately 2,077 non-ATON (manual) transfer requests that were sent to this fax server in respect to 1,744 clients.

¶ 135 As outlined above in paragraph 42, the failure to process transactions in a timely manner constitutes regulatory misconduct as it exposes clients to the risk of financial loss.

¶ 136 Consequently, the failure by the Respondent to ensure that some client account transfer requests that were sent to one of its fax servers were processed in a timely manner, constituted conduct that was contrary to MFDA Rules 2.5.1 and 2.1.1.

VI. PRINCIPLES AND FACTORS REGARDING THE ACCEPTANCE OF SETTLEMENT AGREEMENTS

¶ 137 Investor protection is the primary goal of securities regulation. Settlements play an important and necessary role in meeting this objective.

Pezim v. British Columbia (Superintendent of Brokers), [1994] 2 S.C.R. 557 at paras. 59 and 68.

¶ 138 In our view, the role of a Hearing Panel in a Settlement Hearing is not the same as its role in making a penalty determination after a contested Hearing. 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.

¶ 139 Previous MFDA Hearing Panels have determined the factors which should be considered in determining whether a Settlement Agreement should be accepted. These include the following:

- (i) Whether acceptance of the Settlement Agreement would be in the public interest and whether the penalty imposed will protect investors;
- (ii) Whether the Settlement Agreement is reasonable and proportionate, having regard to the conduct of the Respondent as set out in the Settlement Agreement;
- (iii) Whether the Settlement Agreement addresses the issues of both specific and general deterrence;
- (iv) Whether the proposed settlement will prevent the type of conduct described in the Settlement Agreement from occurring again in the future;
- (v) Whether the Settlement Agreement will foster confidence in the integrity of the Canadian capital markets;
- (vi) Whether the Settlement Agreement will foster confidence in the integrity of the MFDA;
- (vii) Whether the Settlement Agreement will foster confidence in the regulatory process itself.

Jacobson (Re), [2007], Hearing Panel of the Prairie Regional Council, MFDA File No. 200712, Reasons for Decision, dated July 13, 2007, at para. 68.

¶ 140 Previous Hearing Panels have also identified a number of additional factors which should be considered when determining whether the penalty sought to be imposed is appropriate. These include:

- a) The seriousness of the allegations proved against the Respondent;
- b) The Respondent's past conduct, including prior sanctions;
- c) The Respondent's experience in the capital markets;
- d) The level of the Respondent's activity in the capital markets;
- e) Whether the Respondent recognizes the seriousness of the improper activity;
- f) The harm suffered by investors as a result of the Respondent's activities;
- g) The benefits received by the Respondent as a result of the improper activity;
- h) The risk to investors and the capital markets in the jurisdiction, were the Respondent to continue to operate in capital markets in the jurisdiction;
- i) The damage caused to the integrity of the capital markets in the jurisdiction by the Respondent's improper activities;
- j) 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;
- k) The need to alert others to the consequences of inappropriate activities to those who are permitted to participate in capital markets; and
- l) Previous decisions made in similar circumstances.

Headley [Re], 2006, Hearing Panel of the Central Regional Council, MFDA File No. 200509, Reasons for Decision dated February 21, 2006 at para. 85.

¶ 141 When determining whether a penalty agreed upon by the parties is appropriate, the Hearing Panel may also consider the MFDA's Sanction Guidelines ("Guidelines") which came in to effect on November 15, 2018. The Guidelines are not mandatory or binding on the Hearing Panel, but provide a summary of the key factors upon which discretion can be exercised consistently and fairly. Many of the same factors that are listed above, which have been considered in previous decisions of MFDA Hearing Panels, are also reflected and described in the Guidelines.

VII. CONSIDERATIONS IN THE PRESENT CASE

¶ 142 Staff made very detailed written and oral submissions as to how these principles and factors applied to the case before us. These included the following:

Nature of the Misconduct

¶ 143 We agree with the submissions of Staff that the contraventions in this matter are serious. The misconduct reflects wide-ranging deficiencies in the Respondent's business and trade processing practices.

¶ 144 Many of the contraventions persisted for a significant period of time and exposed a large number of clients to the risk of financial loss. As a result, a substantial fine is warranted.

The Respondent's Recognition of the Seriousness of the Misconduct

¶ 145 By entering into the Settlement Agreement and conducting its own investigation, self-reporting its misconduct to the MFDA and voluntarily implementing a fulsome remediation plan to compensate clients for losses that they may have incurred as a consequence of the Respondent's misconduct, the Respondent has saved the MFDA the time, resources, and expenses associated with conducting a contested hearing on the allegations and has demonstrated remorse and recognition of the seriousness of its misconduct.

¶ 146 After discovery of the problems, the Respondent conducted an extensive review of all of the contraventions and provided the MFDA with regular progress updates. The Respondent remediated clients and developed enhancements to its control systems in order to prevent a reoccurrence. The Respondent also conducted investigations of all Approved Persons who were identified during the initial investigations and reported the results of those investigations to MFDA Staff.

¶ 147 The Settlement Agreement provides exhaustive details of the control enhancements implemented by the Respondent. These included:

- (i) Contravention #1
See paragraphs 27 and 28.
- (ii) Contravention #2
See paragraph 42.
- (iii) Contravention #3
See paragraphs 54 and 55.
- (iv) Contravention #4
See paragraphs 64 and 65.
- (v) Contravention #5
See paragraph 74.
- (vi) Contravention #6
See paragraph 78.

Client Harm

¶ 148 Other than Contravention #3, for which there was no client impact, each of the contraventions exposed a substantial number of clients to the risk of financial loss.

¶ 149 The Respondent has paid or will pay client remediation in the total amount of at least \$10.8 million.

¶ 150 The Settlement Agreement provides details of both the methodology employed, as well as the amounts paid or to be paid in respect of each of the contraventions. These included:

(i) Contravention #1

9,982 clients have received remediation totaling \$3,747,242.92 as a result of the review described in paragraph 29 of the Settlement Agreement.

(ii) Contravention #2

7 clients have received remediation totaling \$426.64 as a result of the review described in paragraph 43 of the Settlement Agreement.

(iii) Contravention #4

827 accounts have received remediation totaling \$740,145 as a result of the review described in paragraph 62 of the Settlement Agreement.

(iv) Contravention #5

At least \$6 million in compensation as a result of the process described in paragraph 72 of the Settlement Agreement.

(v) Contravention #6

Approximately 1,702 clients will receive remediation totaling at least \$350,000 as a result of the review described in paragraph 82 of the Settlement Agreement.

¶ 151 In addition to the above-described remediation amounts, the Respondent will make a charitable donation for these clients who would have been entitled to a payment of \$25 or less.

Approved Person Discipline

¶ 152 As outlined in the Settlement Agreement, the Respondent developed a matrix for the discipline of Approved Persons under investigation. This matrix provided for three levels of discipline which depended upon the severity of the misconduct:

Misconduct: This level of discipline was imposed when there was a low level of misconduct (e.g. an honest misunderstanding or mistaken belief of the appropriate procedure for processing the transaction). The Approved Persons received a Written Warning and were required to successfully complete the IFSE Institute (the educational arm of Investment Funds Institute of Canada (“IFIC”))’s Ethics and Professional Conduct Course within six months;

Serious Misconduct: This level of discipline was imposed when there was a moderate level of misconduct (e.g. some level of understanding of the appropriate procedure, but no clear intention to process the transaction in a certain manner for the purposes of increasing sales credit, and provided reasonable explanations for some transactions). The Approved Persons received a Final Warning for Serious Misconduct, were required to successfully complete IFIC’s Ethics and Professional Conduct Course within six months, were placed under strict supervision for 1 year, and received a financial penalty; or

Egregious Misconduct: This level of discipline was imposed when there was a high level of **misconduct** (e.g. initiated transactions for the purpose of increasing sales credit). These Approved Persons received Termination of Employment for Cause.

Results of the Application of the Discipline Matrix

¶ 153 The Settlement Agreement provides details of the results of the application of the discipline matrix.

(i) Contravention #1

Of the 46 Approved Persons referred to in paragraph 19(a) of the Settlement Agreement, 8 had resigned prior to the investigation. Of the remaining 38 Approved Persons, 22 were determined to have engaged in misconduct, 14 were determined to have engaged in serious misconduct and 2 were determined to have engaged in egregious misconduct and were terminated.

(ii) **Contravention #2**

127 Approved Persons were identified for further investigation with respect to this issue. 31 had resigned prior to the investigation. Of the remaining 96, 56 were determined to have engaged in conduct warranting discipline. Of these, 25 were determined to have engaged in misconduct, 17 were determined to have engaged in serious misconduct and 14 were determined to have engaged in egregious misconduct and were terminated.

(iii) **Contravention #3**

73 Approved Persons, which included 8 Branch Managers, were identified for further investigation with respect to this issue. 13 of these Approved Persons or Branch Managers resigned prior to the investigation. Of the remaining 60 Approved Persons or Branch Managers, 14 were determined to have engaged in misconduct, 28 were determined to have engaged in serious misconduct and 18 were determined to have engaged in egregious misconduct and were terminated.

¶ 154 Owing to the wide-spread nature of the Contraventions, and the length of time during which the Contraventions occurred, the Hearing Panel raised the issue of what, if any, disciplinary action had been taken by the Respondent regarding the failure to properly supervise by personnel above the Branch Manager level. We were advised that the Respondent will undertake an internal investigation and will share the results of that investigation with the MFDA. We trust that such an investigation will be robust and thorough.

(d) Deterrence

¶ 155 Deterrence is intended to capture both specific deterrence of the wrongdoer, as well as general deterrence of other participants in the capital markets, in order to protect investors.

¶ 156 In our view, the fine of \$1,000,000 and costs of \$75,000 will send a clear message to the Respondent, as well as other industry Members, that the contraventions which arose in this case are serious and that the disciplinary consequences are substantial.

¶ 157 We believe that the penalties imposed will enhance investor protection and strengthen public confidence in the Canadian mutual fund industry by ensuring high standards of conduct by Members and improving overall compliance by mutual fund industry participants.

(e) Previous Decisions Made in Similar Circumstances

¶ 158 Staff provided the Hearing Panel with a detailed chart seeking to show that the proposed resolution is within the reasonable range of appropriateness with regard to other decisions made by MFDA Hearing Panels in similar circumstances.

¶ 159 The following cases were discussed:

- a) TD Waterhouse Canada Inc. (Re), 2008 IIROC 7.
- b) Sun Life Financial Services (Canada) Inc. (Re), [2018] Hearing Panel of the Central Regional Council, MFDA File No. 201775, Panel Decision dated March 5, 2018.
- c) Quadrus Investments Services Ltd. (Re), [2022] Hearing Panel of the Central Regional Council, MFDA File No. 202166, Panel Decision dated January 20, 2022.
- d) Scotia Capital (Re), 2015 IIROC 27.
- e) Credential Asset Management Inc. (Re), [2022] Hearing Panel of the Pacific Regional Council, MFDA File No. 202160, Panel Decision dated March 9, 2022.
- f) HollisWealth Advisory Services Inc. (Re), [2015] Hearing Panel of the Central Regional Council, MFDA File No. 201532, Panel Decision dated December 8, 2015.

- g) Portfolio Strategies Corporation (Re), [2020] Hearing Panel of the Prairie Regional Council, MFDA File No. 202032, Panel Decision dated November 30, 2020.
- h) Investia Financial Services Inc. & FundEX Investments Inc. (Re), [2012] Hearing Panel of the Central Regional Council, MFDA File No. 200932 and 201031, Panel Decision dated March 26, 2012.

VIII. DECISION

¶ 160 After a thorough review of the factors by which we should be guided, and the facts of this case, as reflected in the Settlement Agreement, we were, unanimously, of the view that this Settlement Agreement was reasonable and in the public interest and should be accepted by the Hearing Panel. We so informed the parties at the conclusion of the Settlement Hearing.

IX. ORDER

¶ 161 After accepting the Settlement Agreement, we made the following Order:

- a) The Respondent shall pay a fine in the amount of \$1,000,000 in certified funds upon acceptance of the Settlement Agreement, pursuant to s. 24.1.2(b) of MFDA By-law No.1;
- b) The Respondent shall pay costs in the amount of \$75,000 in certified funds upon acceptance of the Settlement Agreement, pursuant to s. 24.2 of MFDA By-law No.1;
- c) The Respondent shall in the future comply with MFDA Rules 2.5.1, 2.2.1, 2.1.1 and MFDA Policy No. 2; and
- d) If at any time a non-party to this proceeding, with the exception of the bodies set out in section 23 of MFDA By-law No. 1, requests production of or access to exhibits in this proceeding that contain personal information as defined by the MFDA Privacy Policy, then the MFDA Corporate Secretary shall not provide copies of or access to the requested exhibits to the non-party without first redacting from them any and all personal information, pursuant to Rules 1.8(2) and (5) of the MFDA *Rules of Procedure*.

Dated this 12 day of October, 2023.

Thomas J. Lockwood, K.C.

Guenther W.K. Kleberg

Kenneth P. Mann

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