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

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

Re: Equity Associates Inc.

Heard: April 13, 2015, in Toronto, Ontario
Reasons for Decision: May 27, 2015

REASONS FOR DECISION

Hearing Panel of the Central Regional Council:

The Hon. P. T. Galligan, Q.C.	Chair
Kenneth Mann	Industry Representative
Leo M. Hill	Industry Representative

Appearances:

Shelly Feld	)))	For the Mutual Fund Dealers Association of Canada
Christopher Caruana	)))	For the Respondent

1. The Staff of the Mutual Fund Dealers Association ("MFDA") and the Respondent entered into a settlement agreement which they had negotiated pursuant to s. 24.4.1 of MFDA By-law No. 1. They submitted the settlement agreement (the "Settlement Agreement") to this Hearing Panel, pursuant to Rule of Procedure 15.1, for approval or rejection. After considering the settlement agreement, the other material filed and upon hearing the submissions made by Enforcement Counsel and by counsel for the Respondent, we issued an order accepting the settlement agreement. These are our reasons for making that order.

PRELIMINARY MATTER

2. The Notice required by Rule 15 of MFDA Rules of Procedure was not given within the ten days required by that rule. Enforcement Counsel satisfied us that all persons who had a direct interest in the proceeding had been made aware of the Settlement Hearing and that the required notice had now been given. In the exercise of our powers under Rule 2.2, we abridged the time required so that the Settlement Hearing could proceed.

THE CONTRAVENTIONS

3. **Allegation #1**: On or about July 4, 2008, the Respondent opened two new joint accounts for clients DH and EH without ensuring that:

(a) it obtained a New Account Application Form ("NAAF") or other form documenting the know-your-client ("KYC") information for each of the joint accounts in a manner which conformed with the requirements of MFDA Rule[1] 2.2.1, contrary to MFDA Rules 2.2.2 and 2.1.1; and

(b) a designated trading partner, director or officer, approved the opening of the new joint accounts prior to or promptly after the completion of the initial transactions in the accounts, contrary to MFDA Rules 2.2.3 and 2.1.1..

[1] Note: The MFDA By-law, Rules and Policies have been amended from time to time. All references to the MFDA By-law, Rules and Policies in this Notice of Hearing rely on the wording of the applicable By-law provision, Rule or Policy at the time when the alleged misconduct occurred.

Allegation #2: Between July 4, 2008 and April 27, 2009, the Respondent failed to ensure that it learned the essential facts relative to two new joint accounts that were opened for clients DH and EH and failed to ensure that the orders that were accepted and the investment recommendations that were made in respect of the joint accounts of clients DH and EH were suitable for clients DH and EH, in keeping with their investment objectives, and within the bounds of good business practice, contrary to MFDA Rules 2.2.1 and 2.1.1.

Allegation #3: Commencing July 2009, the Respondent failed to ensure that a complaint from clients DH and EH concerning the losses that they sustained in their joint accounts was handled promptly and fairly, contrary to MFDA Rules 2.1.1 and 2.11 and MFDA Policy No. 3

TERMS OF SETTLEMENT

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

   (a) the Respondent shall pay a fine in the amount of $40,000;

   (b) the Respondent has made a payment of $50,000 to clients DH and EH as part of the terms of settlement of a civil claim against the Respondent by clients DH and EH;

   (c) the Respondent shall pay costs to the MFDA in the amount of $10,000;

   (d) the Respondent shall in the future comply with MFDA Rules 2.2.1, 2.2.2, 2.2.3, 2.11 and MFDA Policy No. 3 and the Respondent shall uphold the standard of conduct in the industry in accordance with MFDA Rule 2.1.1 by among other things:

      i. exercising due diligence to learn the essential facts relative to each client and each order and account accepted;

      ii. ensuring that the Respondent has obtained a New Account Application form and documented Know-Your-Client information for each new

account of a client and that a designated trading partner, director, officer or branch manager has approved the opening of new accounts and is supervising account activity in each new account prior to or within one day of the initial transaction date in each new account;

iii. ensuring that investment recommendations that are made and orders that are accepted for any account are suitable for the client and within the bounds of good business practice; and

iv. by handling complaints promptly and fairly; and

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

THE CIRCUMSTANCES

5. The circumstances are set out in detail in Part IV of the Settlement Agreement. It is attached as Appendix "A" to these Reasons for Decision. The following is a brief summary of the circumstances.

6. In June 2008, DH and EH, a married couple, had each had personal accounts with the Respondent for a number of years. The investments which they had in those accounts were for the purpose of supplementing their retirement incomes. During the previous spring they had entered into an agreement to purchase a new home which was to be constructed. They intended to sell their existing home and use the proceeds to pay for the new one.

7. In June 2008 they sold their home but the new home was not yet ready. The completion of the new home was delayed and the date of completion was at that time uncertain. The clients met with Mr. Fried and instructed him to invest the funds from the sale of their home in a joint account in funds which could be redeemed on short notice once the closing date for the purchase was finally determined. They instructed that the investment had to be safe and liquid.

8. Mr. Fried did not obtain a new NAAF or new KYC forms for the new joint account. He

invested the clients' funds in investments which were not suited to their new requirements for safe short-term liquid funds. Between June 2008 and the completion of the new home in March 2009 the clients sustained losses of approximately $75,000 on their investment.

Opening the new joint accounts

9. The Respondent opened two new joint accounts without ensuring that new NAAFs or other documents showing KYC information had been obtained, and without ensuring that a designated person approved the opening of the new accounts

Lack of knowledge of the facts relating to the new accounts

10. The Respondent's failure to know the relevant facts about the accounts deprived it of the ability to ensure that the investments were suitable for the investment objectives of the new investment.

Mishandling of the clients' complaint

11. We are advised that this is the first disciplinary process undertaken pursuant to a Member under Rule 2.11. Because of its importance as a precedent we think it is appropriate to set out the position taken by Enforcement Counsel at paragraphs 29 to 31 of his written submissions:

> 29. On July 17, 2009, the Respondent received a complaint letter from clients EH and DH concerning losses in their joint accounts (SA para. 85) but the Respondent failed to deal with the complaint promptly or fairly, contrary to MFDA Rules 2.1.1 and 2.11 and MFDA Policy No. 3.
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> 30. The Respondent failed to prepare a substantive response to the complaint until March 2010, more than 8 months after the complaint was received. (SA paras. 90 and 97).
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> 31. In its substantive response, the Respondent dismissed the complaint of EH

and DH in its entirety. The grounds for doing so were unreasonable, as the Respondent based its decision on considerations including the following:

(a) the Respondent applied the KYC information recorded for the individual accounts of EH and DH to conclude that the investments purchased in the joint accounts; were suitable (in spite of the fact that the KYC information applicable to the new joint accounts was completely different than the KYC information applicable to the individual accounts of EH and DH);

(b) due to deficiencies in its own procedures, the Respondent did not have any record of the KYC information applicable to the joint accounts that were the subject matter of the complaints of EH and DH;

(c) the Respondent applied the weighted average methodology that the Respondent had agreed to discontinue using prior to the opening of the joint accounts of EH and DH to conclude that the purchases in the joint accounts were suitable;

(d) (d) the Respondent accepted uncorroborated assertions of [Fried] disputing some of the grounds for the complaint as a basis for dismissing the complaint and failed to take into account documentary evidence that appeared to support the merits of the client complaint;

(e) the Respondent ignored its own conclusion that the trades in the new joint accounts were processed using photocopied blank signed forms and therefore, there was no evidence that the clients had authorized the trades or the risk level of the portfolio; and

(f) if the Respondent had used the method for assessing suitability that it had in place at the time that it provided its substantive response to clients EH and DH, it should have concluded that the investments in the joint accounts were unsuitable.

(SA paras. 91-92)

We accept that position.

SERIOUSNESS OF THE CONTRAVENTIONS

12. Allegations #1 and #2 relate to a Member's obligation to supervise Approved Persons for whom it is responsible and to assess the suitability of investments which were recommended to clients. It is reasonable to infer that if those duties had been fulfilled the clients' losses might have been avoided entirely or at least significantly lessened.

13. Allegation #3 relates to a Member's obligation to deal with a client's complaints promptly and fairly. We consider the Respondent's failure to fulfil that obligation to be a serious matter. Its misconduct made it necessary for the clients to institute an action in the law courts.

CIRCUMSTANCES OF MITIGATION

14. In determining an appropriate remedy it is always necessary to consider mitigating circumstances. The circumstances of mitigation which we take into account are:

a) The Respondent has no prior disciplinary history in the financial services industry.
b) It has cooperated fully with Staff and has admitted its contraventions. That shows remorse and an intention to fully comply with what is expected of a Member.
c) It has put in place systems which will protect against the repetition of these contraventions.
d) It has settled the lawsuit and has paid compensation to the clients.

THE DUTY OF A HEARING PANEL AT A SETTLEMENT HEARING

15. It is well settled that our task is not to decide whether, in this case, we would have arrived at the same decision as that reached by the parties in their settlement agreement. Rather, our duty is to determine whether the penalty is a reasonable one and whether it meets the objectives of the disciplinary process which are to maintain the integrity of the Investment Services Industry and

to protect the public. In *Re Professional Investments (Kingston) Inc.*, [2009] LNCMFDA 9 at paragraph 13 the following appears:

> 13. In a contested Hearing, the Hearing Panel attempts to determine the correct penalty. In a Settlement Hearing, the Hearing Panel takes into account the settlement process itself and the fact that the parties have agreed to the penalties set out in the Settlement Agreement. In our view, a Hearing Panel should not interfere lightly in a negotiated settlement and should not reject a Settlement Agreement unless it views the penalty as clearly falling outside a reasonable range of appropriateness. As has been said: "The settlement process is one of negotiation and compromise and the penalty imposed following a settlement will often be less onerous than one imposed following a Hearing where similar findings are made."
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> Re: Clark (Re), [1999] I.D.A.C.D. No. 40 at page 3.

16. See also *Re Raymer*, [2009] LNCMFDA 15 at paragraph 4:

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

17. The courts have addressed the importance of settlements and have approved of their place in the disciplinary process. See *B.C. Securities Commission v. Seifert*, [2006] BCJ No. 225, where the following appears at p. 49:

> Settlements assist the Commission to ensure that its overriding objective, the protection of the public, is met. Settlements proscribe activities that are harmful to the public. In so doing, they are effective in accomplishing the purposes of the statute. They provide means of reaching a flexible remedy that is tailored to address the interests of both the Commission and the person under investigation. Enforcement is rarely a concern because the settlement is voluntary. A person who is the subject of an investigation retains the option of refusing to settle and proceeding to a hearing. Settlements are also efficient. Both parties can forego the time and expense of a hearing…

18. Finally we refer to the comments of an IIROC Hearing Panel in the recent case of *Re Vorstadt*, [2012] IIROC at p. 4:

> Before leaving this case we wish to stress the importance of respect for the settlement process. Settlement leads to fair, efficient and economical resolution of disciplinary matters. The settlement process should be encouraged and supported. In *Re Clarke*, [1999] I.D.A.C.D. No. 40, the Hearing Panel stated, at p. 3:
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> > The panel must be cognizant of the importance of the settlement process and should not interfere lightly in a negotiated settlement. [Emphasis added.]
>
> We subscribe to that view.

GUIDELINES AND OTHER DECISIONS

19. In determining whether a settlement is a reasonable one, a hearing panel is entitled to look at regulatory guidelines and other decisions. Guidelines are not binding upon a hearing panel and it cannot derogate from its responsibility to decide what might be an appropriate penalty in a given case. However guidelines are useful in that they show what penalties members of the industry consider to be generally appropriate. We have considered the guidelines for deficient supervision, lack of suitability and complaint handling. The fine suggested in this case is very much in line with those guidelines.

20. Decisions in other cases can often be of some assistance in helping to indicate what might be a reasonable range of penalties. It is always necessary to be cautious about relying too heavily on decisions in other cases because no two cases are ever the same. Counsel drew our attention to five previous decisions in somewhat similar circumstances. We have decided that there is no need to review any of those decisions in detail. The penalties suggested in this case fall within a broad range encompassed by those other decisions.

IMPACT OF THE PENALTY

21. Monetary penalties are imposed to act as specific and general deterrence. The penalty imposed is sufficient to act as a specific deterrent to this Respondent and should be sufficient to alert all Members and Approved Persons that similar conduct will attract significant consequences.

DECISION

22. At the conclusion of the hearing we withdrew from the hearing room. We considered the circumstances of this case and reached the conclusion that the settlement was a reasonable one. Therefore we accepted it.

DATED this 27th day of May, 2015.

"P. T. Galligan"

The Hon. P. T. Galligan, Q.C.
Chair

"Kenneth P. Mann"

Kenneth P. Mann
Industry Representative

"Leo M. Hill"

Leo M. Hill
Industry Representative

APPENDIX "A"

IV. AGREED FACTS

Registration History

The Respondent

6. The Respondent is presently registered as a mutual fund dealer in all Canadian provinces except Saskatchewan and as an Exempt Market Dealer in Newfoundland and Labrador and in Ontario.

7. At all material times pertaining to events described in this Settlement Agreement, the Respondent has been registered in Ontario as a mutual fund dealer and as a limited market dealer. [2]

8. The Respondent has been a Member of the MFDA since March 4, 2003.

Approved Person Mervyn Fried

9. From November 24, 2004 to September 27, 2010, Mervyn Fried ("Fried") was registered in Ontario as a mutual fund salesperson[3] with the Respondent. The Respondent terminated Fried following an internal investigation that the Respondent conducted which led it to conclude that contrary to the policies and procedures of the Respondent and MFDA Rules and without the knowledge or authorization of the Respondent, Fried charged clients, including clients DH and EH (who are described below), fees in addition to the commissions that he received from the Respondent relating to services that constituted securities related business that Fried had provided to clients on behalf of the Respondent.

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[2] The registration category "Limited Market Dealer" was changed to "Exempt Market Dealer" after National Instrument 33-102 came into force on September 28, 2009.

[3] Dealing Representative after September 28, 2009.

10. The MFDA commenced a disciplinary proceeding against Fried by Notice of Hearing issued December 16, 2013 (MFDA Case File No. 201242) alleging that Fried had contravened MFDA Rules by, among other things, making unsuitable investment recommendations in the joint accounts of clients DH and EH which resulted in significant losses, processing trades in the joint account using blank trade order entry forms signed by clients DH and EH, and charging clients DH and EH fees for services without the Respondent's authorization.

11. On October 15, 2014, Staff and Fried entered into a Settlement Agreement that was accepted by order of a Hearing Panel of the MFDA on the same day. The Respondent acknowledges and does not object to the possibility that this Settlement Agreement may be considered by all or some of the members of the Hearing Panel that accepted the settlement agreement in the Fried proceeding.

The March 2008 compliance examination of Equity

12. Staff of the MFDA ("Staff") periodically conducts examinations of MFDA Members to assess their degree of compliance with MFDA By-laws, Rules and Policies with a view to, among other things, identifying regulatory deficiencies that may need to be addressed.

13. By letter dated March 14, 2008, Staff provided the Respondent with the results of its 2008 compliance examination of the Respondent in the form of the 2008 Compliance Examination Report of the Respondent (the "2008 Compliance Examination Report"). The report identified deficiencies in the Respondent's policies and procedures that required the Respondent's immediate attention, including the following:

(a) the Respondent was not ensuring that clients who opened more than one investment account with the Respondent completed a new NAAF or KYC document for each account;
(b) the Respondent was using a weighted-average methodology for reviewing and approving the suitability of trades that did not adequately ensure that trading activity in a client's

account was suitable for the client based on the KYC information on record for the client; and

(c) the Respondent had not implemented a satisfactory process to ensure that each NAAF was reviewed and approved prior to the new account being opened and did not sufficiently document any NAAF approval process that was completed.

14. The March 14, 2008 letter required the Respondent to respond in writing on or before April 7, 2008 describing the steps that it had taken, or intended to take, to address the deficiencies identified in the 2008 Compliance Examination Report.

15. Also in March 2008, as a result of Staff's concerns about the nature and extent of the compliance deficiencies identified in the 2008 Compliance Examination Report, MFDA Compliance Staff referred the 2008 Compliance Examination Report to MFDA Enforcement Staff for possible disciplinary action.

16. In June 2008, the Respondent submitted a response to Staff of the MFDA Compliance Department, setting out a proposed timetable for the implementation of various steps that would be taken during the next year in order to rectify the compliance deficiencies that had been identified by Staff in the 2008 Compliance Examination Report. The Respondent then proceeded to implement the required changes in accordance with the proposed timetable.

17. The Respondent also entered into an Agreement and Undertaking dated June 23, 2008 with Staff of the MFDA Enforcement Department pursuant to which the Respondent was required to implement enhanced policies and procedures to address certain deficiencies in its account supervision process and to cease use of the weighted average methodology for evaluating the suitability of investment recommendations to clients (the "Agreement and Undertaking").

18. Although the timetable that the Respondent proposed for rectification of compliance deficiencies identified in the 2008 Compliance Examination Report contemplated the implementation of changes over a one year period, that schedule did not relieve the Respondent

of regulatory liability arising from such deficiencies in the event that such deficiencies impacted clients prior to, during or after the implementation of changes aimed at resolving the deficiencies identified during the 2008 compliance examination process.

February 2005 - Clients DH & EH Transfer Their Investments To The Respondent

19. DH and EH are spouses. In 2004, they required investment advice and were referred to Fried by their son-in-law. At this time, Fried was an Approved Person at a different Member. (He did not become an Approved Person of the Respondent until November 24, 2004.)

20. DH was born in 1945. He had retired from his job in the fuel-purchasing department at Ontario Hydro in 2003. Prior to his dealings with Fried, DH investments consisted of some Guaranteed Investment Certificates ("GICs") and an RRSP account in which he held some mutual funds that had been purchased at another dealer during the 1990s.

21. EH was born in 1940. In 2004, when she met Fried, she was still working as a real estate agent but she was approaching retirement. She held some investments in an RRSP account at another dealer.

22. In April 2004, client EH opened a new RRSP account and a new open (i.e. non-registered) account in her own name at the mutual fund dealer where Fried was registered at the time.

23. In November 2004, Fried transferred his registration to and became an Approved Person of the Respondent.

24. In February 2005, client DH opened an RRSP account and an open account with the Respondent and transferred the investments that he held at another dealer to the Respondent. Client EH also transferred her RRSP account and her open account from Fried's former dealer to the Respondent.

25. At all material times thereafter, Fried was the mutual fund salesperson at the Respondent who was responsible for servicing the accounts of clients DH and EH.

26. The investments that clients DH and EH held in their individual accounts at the Respondent were intended to supplement their future retirement income.

27. Client DH completed a NAAF for each of the individual accounts (the RRSP account and the Open Account) that he opened with the Respondent, as did client EH. The KYC section of the NAAFs recorded that:

(a) clients DH and EH each had a "novice" level of investment knowledge (the lowest category on the form);
(b) their investment objectives were "growth" and "income";
(c) client DH and EH each had a "medium high" risk tolerance; and
(d) client DH's time horizon for his accounts was 10+ years while client EH's was 6-9 years.

28. At all material times, clients DH and EH relied upon and deferred substantially or entirely to Fried for investment recommendations and advice.

Spring 2008 – Clients DH And EH Invest The Proceeds From The Sale Of Their House

29. In May 2007, clients DH and EH entered into an agreement of purchase and sale with respect to the construction of a new home in Innisfil, Ontario for a total price of $240,350. Clients DH and EH paid a deposit in the amount of $5,000, leaving a balance due on closing of $235,350, plus any adjustments, taxes, fees and other costs due on closing. In August 2007, clients DH and EH instructed Fried to change their mailing address on file with the Respondent.

30. Clients DH and EH also anticipated that they would require money for other expenses that they expected to incur at or around the time of closing, including lifestyle-related expenses.

31. The agreement granted the developer considerable flexibility with respect to moving up or pushing back the closing date of their new home on limited notice. The closing date was initially projected to be July 23, 2008.

32. The Respondent states that Fried did not advise any compliance staff of the Respondent of the agreement of purchase and sale for the new home, its closing date or the requirements for funding other expenses.

June 2008 – Clients DH And EH Instruct Fried To Open A New Joint Account

33. In June 2008, clients DH and EH sold their Newmarket home in order to ensure that they would have sufficient monies available to pay the balance due on closing for their new home and to pay for the other expenses they intended to incur at or around the time of closing.

34. On June 26, 2008, 3 days after the Respondent had entered into the Agreement and Undertaking with Staff, clients DH and EH met with Fried to discuss the possibility of investing $270,000 from the proceeds of the sale of their home until the construction of their new home was completed. On the basis of discussions that occurred and information that was conveyed to Fried during the June 26, 2008 meeting, Fried knew or ought to have known, among other things, that:

(a) the projected closing date for the new house had been pushed back to November 26, 2008, five months from the date of their meeting;
(b) DH and EH would need the entire amount of the sale proceeds ($268,000) that they were investing with the Respondent to pay the balance due on closing and to cover their other anticipated expenses; and
(c) they would need to be able to redeem the investments purchased with the sale proceeds on short notice when the closing date on the new house was determined.

35. At the conclusion of the June 26th meeting, clients DH and EH instructed Fried to open a new joint account for them in which they would hold the investments to be purchased with the

proceeds from the sale of their home. They instructed Fried not to deposit any of the house sale proceeds in any of the existing accounts that they had previously opened in their individual names.

36. In accordance with Fried's instructions, clients DH and EH provided Fried with three cheques at the June 26, 2008 meeting:

(a) one cheque in the amount of $200,000 payable to the Respondent which was labelled 'House Sale 1' on the memo line;
(b) one cheque in the amount of $68,000 payable to the Respondent which was labelled 'House Sale 2' on the memo line; and
(c) one cheque in the amount of $2,680 that was payable to Fried personally which was labelled 'Fees' on the memo line.

37. DH and EH do not recall Fried explaining to them that he intended to open two joint accounts on their behalf or any other reason why he asked that the sale proceeds be divided into two separate cheques of $200,000 and $68,000, nor do they recall Fried explaining why he had requested that clients DH and EH provide him with an additional cheque for fees in the amount of $2,680 payable to him personally.

38. Fried did not complete, nor did he ask clients DH and EH to complete, sign and date a NAAF or any new KYC forms in respect of the new joint accounts that he opened in their joint names after the June 26, 2008 meeting.

39. According to Fried, he consulted with the Respondent and was told that the Respondent did not require its Approved Persons to obtain a NAAF or KYC form prior to opening one or more new accounts for an existing client of the Respondent. As a result, Fried mistakenly believed that he could rely on the KYC information that had previously been recorded for individual accounts of DH and EH that had been opened prior to June 2008 and that he did not have an obligation to complete a NAAF or KYC form for the new joint accounts that he opened for DH and EH for the investment of the proceeds from the sale of their home that he opened

after the June 26, 2008 meeting. The opening of new accounts without a NAAF or KYC form in respect of the new account, even for an existing client of the Respondent, contravened MFDA Rules.

40. Fried also did not prepare or maintain any notes of KYC information applicable to the investment of the sale proceeds from their home in the new joint accounts with the Respondent that he subsequently opened for clients DH and EH including in particular their investment objectives, risk tolerance and investment time horizon.

41. During the June 26th meeting, Fried did obtain the signatures of clients DH and EH on blank trade order entry forms that he subsequently used to process trades with the monies that they had provided to him.

42. On July 4, 2008, Fried arranged for two (rather than one) new joint accounts to be opened at the Respondent in the names of clients DH and EH.

43. The Respondent did not ensure that it obtained a NAAF from clients DH and EH that documented their KYC information in respect of either one of the two new joint accounts prior to opening the two new joint accounts.

44. On July 4, 2008, Fried arranged for the $68,000 cheque from clients DH and EH to be deposited in one of the two new joint accounts that had been opened (the "Small Joint Account") and for the $200,000 cheque to be deposited in the other new joint account (the "Large Joint Account").

45. Fried cashed the third cheque for $2,680 for his own use and benefit. As noted in more detail below, this fee was repaid to clients DH and EH by the Respondent[4] after the Respondent discovered (as a result of the complaint submitted by clients DH and EH) that this fee for

[4] The Respondent compensated clients DH and EH for the unauthorized fee that Fried had charged and then deducted that amount from commissions payable by the Respondent to Fried.

services had been charged to DH and EH by Fried without the knowledge or authorization of the Respondent.

46. Fried made one or more photocopies of a blank order entry form that had been signed by clients DH and EH and filled in forms to purchase 7 mutual funds in the Small Joint Account and 16 mutual funds in the Large Joint Account.

47. Fried wrote in the date "July 4, 2008" next to the signatures of clients DH and EH on the blank, pre-signed or photocopied order entry forms even though the clients had not met with Fried or signed the forms on that day.

Fried Selects The Investments In The Joint Accounts

48. When clients DH and EH left their June 26th meeting with Fried, they understood that Fried would, in accordance with their instructions, open a new account in their joint names and invest the proceeds from the sale of their Newmarket home in a manner that would preserve the principal and enable them to access the money on short notice whenever the sale of their new home in Innisfil was scheduled to close.

49. Although Fried believes that he discussed with clients DH and EH, the nature of the mutual funds that he intended to purchase in their new joint accounts on a high level, clients DH and EH do not recall such a discussion. The only investment proposal that clients DH and EH recall Fried discussing at the June 26, 2008 meeting was a limited partnership product that Fried believed would offer clients DH and EH favourable tax advantages. Clients DH and EH declined this recommendation because they did not think that they understood the features of the product and they feared that it would not be consistent with their need for a secure and accessible (liquid) investment.

50. Fried selected the mutual funds that were purchased in the new joints accounts of clients DH and EH and used the blank order entry forms that the clients signed at the June 26, 2008 meeting, or photocopies of the forms, to process the purchase transactions in the new joint

accounts on July 4, 2008. Fried thereby engaged in discretionary trading contrary to MFDA Rules 2.3.1, 2.1.1 and the terms of his registration as a mutual fund salesperson whether or not he was authorized to do so do so by the client, either expressly or by acquiescence.

51. Fried did not select mutual funds in the joint accounts of clients DH and EH that would ensure the preservation of the clients' capital. He invested the majority of the house sale proceeds in mutual funds with risk ratings of moderate, moderate to high, and high, all of which had an historical volatility which would not ensure preservation of capital.

52. Fried allocated the $68,000 deposited in the Small Joint Account approximately as follows:

- 37% (i.e.; $25,000) in 2 equity mutual funds with a low to moderate risk level;
- 26% in 2 equity mutual funds with a moderate risk level;
- 22% in 2 equity mutual funds with a moderate to high risk level; and
- 15% in 1 equity mutual fund with a high risk level.

53. Fried allocated the $200,000 deposited in the Large Joint Account approximately as follows:

- 5% (i.e.; $10,000) in 1 equity mutual fund with a low to moderate risk level;
- 57% in 9 equity mutual funds with a moderate risk level;
- 20% in 3 equity mutual funds with a moderate to high risk level; and
- 17% in 3 equity mutual funds with a high risk level.

54. In total, in spite of the intentions of clients DH and EH, Fried invested approximately $223,000 (or 83%) of the total $268,000 in sale proceeds in mutual funds with a "moderate" risk rating or higher and $45,000 (or 17%) of the $268,000 in mutual funds with a "high" risk rating.

55. Fried purchased all of the mutual funds on a "front end zero" basis, meaning that he did not receive a sales commission on the purchase of the funds, nor would the clients be subject to a

deferred sales charge upon redemption. Fried was entitled to receive a trailing commission of approximately 1% per year on the value of the clients' holdings for the duration of the period that they owned the mutual funds and Fried continued to be the Approved Person responsible for servicing their accounts.

56. Clients DH and EH were not aware that following the June 26, 2008 meeting,

(a) Fried and the Respondent opened two new joint accounts in their names rather than one; and

(b) the majority of the money that they needed for their house closing was invested in equity mutual funds with risk ratings of moderate or higher and therefore the principal amount that they had invested might not be available to pay the costs that they would be accountable for upon the closing of their new home .

April 2009 – Clients DH And EH Sustain Significant Losses In Their Joint Accounts

57. Between June 2008 and March 2009, clients DH and EH kept Fried apprised of changes to the projected closing date of their new home, which was delayed by the developer on multiple occasions. During the same period, Fried advised the clients on multiple occasions that they did not need to worry about their investments. In spite of the general market downturn that was being widely reported in the news, Fried believed that the investments that had been purchased in the joint accounts of DH and EH on July 4, 2008 would be fine.

58. Although clients DH and EH do not recall any discussions with Fried about the actual value of the investments held in their joint accounts prior to the redemption of their investments in April 2009, Fried assumed that the clients were receiving account statements from the Respondent and were aware of the value of the investments held in their joint accounts.

59. Clients DH and EH left on a trip to Europe in March 2009. Prior to their departure, they asked Fried to redeem the investments in their joint account and transfer the redemption proceeds

to their bank account so that they would have the monies available to pay the closing costs for the new house purchase in April 2009.

60. Fried recommended that clients DH and EH keep their money invested until they returned from their trip. Clients DH and EH accepted Fried's recommendation to remain invested. DH and EH recall telling Fried that they would provide him with instructions during their trip when the redemption proceeds were required.

61. On Tuesday, April 14th and Friday, April 17, 2009, clients DH and EH sent e-mails to Fried to request the transfer of the proceeds from the redemption of their investments to their bank account by Monday, April 20, 2009.

62. On Monday, April 20, 2009, Fried responded to clients DH and EH and informed them that he believed it was an inopportune time to liquidate their investments. Fried recommended that clients DH and EH redeem only a portion of the investments.

63. Clients DH and EH instructed Fried to redeem all of the money in the joint accounts in order to meet their obligations on the scheduled date of closing of their new home.

64. Due to delays associated with liquidating their investments, clients DH and EH ended up borrowing the money that they required to pay the balance of their closing costs and the other expenses that they had anticipated they would incur at or around the time of closing by borrowing the required money from a line of credit.

65. As of April 29, 2009, the day of the house closing, clients DH and EH had received deposits in their bank account comprising the proceeds of the redemptions of the investments in the joint accounts. The redemption proceeds amounted to $193,573.39 of the $270,680[5] that they had provided to the Respondent at the meeting on June 26, 2008. From June 26, 2008 to

[5] Clients DH and EH had $270,680 available to invest with Fried at the time of the June 26, 2008 meeting. As it turned out, Fried directed clients DH and EH to provide him with three cheques including one in the amount of $2,680 which was payable to Fried personally in respect of fees that he charged at the time of their investment. Accordingly, Fried only invested $268,000 on behalf of the clients.

April 29, 2009, a period of approximately 10 months, the value of the clients' investments had declined by more than $75,000 (approximately 28%).

66. As a consequence, the value of the redemption proceeds was insufficient for clients DH and EH to repay the full amount that they had borrowed from their line of credit or to pay the other expenses that they had originally intended to incur at or around the time of closing.

Contravention #1 – Failure to properly open joint account

(a) Failure to obtain NAAF and document client's KYC information

67. At all material times, MFDA Rule 2.2.2[6] required that a NAAF must be completed for each new client account and, where that NAAF did not include KYC information, that such information be documented on a separate KYC form. MFDA Rule 2.2.2 further provided that the completed NAAF, or NAAF and KYC form as the case may be, must be dated and signed by the client and conform to the requirements of MFDA Rule 2.2.1.

68. At all material times, MFDA Rule 2.2.1 required that each Member and Approved Person must, among other things, learn the essential facts relative to each client and each order or account accepted, and ensure that each order accepted or recommendation made is suitable for the client, in keeping with the client's investment objectives, and within the bounds of good business practice.

69. As described above, the March 2008 Compliance Examination Report had identified, among other deficiencies, that the Respondent was not ensuring that clients who opened more than one account completed a separate NAAF (or NAAF and KYC form) documenting their KYC information in respect of each account. This deficiency was one of the deficiencies that the Respondent had agreed to address after receiving the 2008 Compliance Examination Report.

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[6] Note: The MFDA By-law, Rules and Policies have been amended from time to time. All references to the MFDA By-law, Rules and Policies in this Settlement Agreement rely on the wording of the applicable By-law provision, Rule or Policy at the time of the occurrence of the contraventions described herein.

70. Following Fried's meeting with clients DH and EH on June 26, 2008, the Respondent opened, or allowed Fried to open, the two new joint accounts for clients DH and EH without obtaining a NAAF (or NAAF and KYC form) signed and dated by clients DH and EH documenting their KYC information in respect of the new joint accounts.

71. The Respondent mistakenly believed that because clients DH and EH had signed KYC update forms for their individual accounts two months prior to opening the new joint accounts, it was unnecessary to obtain NAAFs and completed KYC forms for the new accounts that were being opened in their joint names. At all material times, Fried was aware, and the Respondent ought to have been aware if the Respondent had ensured that a NAAF documenting the KYC information for the new joint accounts was obtained from clients DH and EH, that the new joint accounts opened for clients DH and EH were subject to a risk tolerance level, investment objectives and an investment time horizon that was materially different from the KYC information that the Respondent had on file in respect of the individual accounts of clients DH and EH (as described in paragraph 27 above).

72. In contrast to the KYC information on file with the Respondent for client DH's and client EH's individual accounts, clients DH and EH were opening the joint account for the specific purpose of investing the proceeds from the sale of their home for a short duration pending the closing of their new home. Their investment time horizon for the joint account was very short[7]; their investment objective was capital preservation (as they needed the money that they were investing to pay the closing costs of their new home), they emphasized their need for liquidity (as they needed to be able to access the full amount of their capital on short notice whenever the closing of their new home was scheduled) and in light of their need for all of the money that they invested, their investment risk tolerance was very low.

73. The Respondent admits that by failing to ensure that it obtained a NAAF including records of KYC information that was signed and dated by clients DH and EH in respect of two new joint accounts that were opened on July 4, 2008 for clients DH and EH, the Respondent

[7] The duration of the closing period turned out to be approximately ten months (from June 26, 2008 to April 29, 2009) but was initially contemplated to be only approximately five months (from June 26, 2008 to November 26, 2008).

failed to use due diligence to learn the essential facts relative to the new joint accounts and, as described in greater detail in Contravention #2 below, the Respondent failed to ensure that it had in its possession, the relevant KYC information that was required to properly supervise the trading activity in the new joint accounts.

74. The Respondent admits that by engaging in the conduct described above, the Respondent failed to obtain a NAAF including records of KYC information applicable to the new joint accounts in a manner which conformed to the requirements of MFDA Rule 2.2.1, contrary to MFDA Rules 2.2.2 and 2.1.1.

(b) Failure to properly approve opening of new joint accounts

75. At all material times, MFDA Rule 2.2.3 provided that each member shall designate a trading partner, director or officer, or in the case of a branch office, a branch manager reporting directly to a trading partner, director or officer, who shall be responsible for approval of the opening of new accounts and the supervision of account activity. Pursuant to Rule 2.2.3, the designated person is required to approve the opening of the new account prior to or promptly after the initial transaction in the account and a record of such approval is to be maintained.

76. The Respondent admits that in circumstances where there was no separate KYC information documented for two new joint accounts, a designated individual ought to have made the following inquiries of Fried and, if necessary, of clients DH and EH directly, prior to approving the opening of the joint accounts:

(a) whether the investment objectives, time horizon and risk tolerance for the two new joint accounts differed from the KYC information documented for the clients' individual accounts; and
(b) if the information did differ, whether the investment objectives, time horizon and risk tolerance was the same for each of the new joint accounts, bearing in mind that:

(i) clients DH and EH were simultaneously opening two new joint accounts instead of one; and

(ii) clients DH and EH were contributing $68,000 to one of the joint accounts and $200,000 to the other.

77. The Respondent admits that it did not ensure that a designated representative approved the opening of the two new joint accounts prior to or promptly after the initial transactions in the accounts and maintained a record of such approval, contrary to MFDA Rule 2.2.3.

Contravention #2: Suitability of trades in the joint accounts

78. As described above, clients DH and EH communicated the relevant KYC and other information in respect of the joint account to Fried at their June 26, 2008 meeting but Fried did not document the information on a NAAF or KYC form(s) or otherwise communicate it to the Respondent. As a result, that information was not available to the Respondent for the purposes of supervising trading activity in the joint accounts at the time of account opening or at any time thereafter.

79. The mutual funds selected and purchased by Fried in the joint accounts were not suitable for clients DH and EH having regard to, among other considerations:

(a) their investment time horizon for the joint account, which was initially contemplated to be approximately 5 months and, in any event, was not going to exceed the length of time required to close the purchase of their new home, which they were anticipating could occur at any time on a month-to-month basis;

(b) their investment objectives for the joint account, which was preservation of capital above all else, and liquidity (i.e. the ability to quickly access the full amount of their capital);

(c) their risk tolerance for the joint account, which was very low to nil given their insistence that they required the entirety of the sale proceeds to pay the balance due on closing for their new home and other expenses; and

(d) their personal and financial circumstances, including the fact that both clients DH and EH were seniors, retired and had limited assets and limited or no employment income to recover from any loss of capital in the joint accounts.

80. Having regard to all of the circumstances, the purchase of mutual funds of any type in the joint accounts other than money market mutual funds was presumptively unsuitable for clients DH and EH in light of their investment objective to preserve capital above all else, their very short investment time horizon, and their very low to nil investment risk tolerance.

81. As a result of the Respondent's failure to ensure that it obtained NAAFs that properly documented the clients' KYC information for each of the new joint accounts prior to opening the new accounts or at any time thereafter, the Respondent never had available to it the information it required to properly supervise the suitability of the trading activity in the joint accounts.

82. Furthermore, even if the Respondent had relied on the documented KYC information on file for the individual accounts of clients DH and EH to supervise the trading activity in the joint accounts,[8] the Respondent ought to have queried at least those investments processed by Fried in the joint accounts in that related to the purchase of high risk mutual funds.

83. The Respondent admits that by engaging in the conduct described above, the Respondent failed to properly supervise the trading activity in the joint accounts, contrary to MFDA Rules 2.2.1, 2.5 and 2.1.1, and MFDA Policy No. 2.

Contravention #3: Failure to handle client DH and EH's complaint promptly and fairly

84. By letter dated June 8, 2009, clients DH and EH submitted a complaint to the Respondent regarding the decline in value of the investments in their joint account(s) and requested compensation for their losses.

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[8]There is no evidence that the Respondent supervised or queried any of the trading activity in the joint accounts.

85. On July 17, 2009, client DH called Equity and was informed that the Respondent had not received the complaint letter.[9] Client DH faxed the complaint letter to the Respondent later that afternoon.

86. Commencing July 2009, the Chief Compliance Officer of the Respondent (the "CCO") spoke with clients DH and EH on a few occasions and exchanged a few letters with clients DH and EH with respect to their complaint.

87. During a telephone call in December 2009, the CCO informed client DH that he anticipated that the Respondent's substantive response to the complaint would be completed by January 11, 2010.

88. In February 2010, clients DH and EH still had not received a substantive response to their complaint. As a result, client DH sent a follow-up letter to the Respondent to inquire about the status of their complaint.

89. The CCO called client DH in February 2010 following receipt of his follow-up letter. During the call, the CCO learned for the first time that the clients had provided Fried with a cheque in the amount of $2,680 payable to him personally at the June 26, 2008 meeting. Prior to the call, the Respondent was unaware that Fried had been charging clients fees apparently in relation to securities related business that he engaged in on behalf of the Member even though such fees had not been processed through the books and records of the Respondent.

90. By letter dated September 25, 2009 (which was actually sent to clients DH and EH on March 8, 2010 as reflected on the second page of the letter), the Respondent provided clients DH and EH with its substantive response to their complaint. The Respondent dismissed the suitability portion of their complaint in its entirety without any offer of compensation for their losses.

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[9] Fried`s website referenced an out of date address for the Respondent`s Head Office. Consequently, when the clients placed a follow up call to the Respondent on July 17, 2009, the Respondent had not yet received the complaint letter. Following the call on July 17, 2009, the clients faxed the letter to the Respondent.

91. According to the Respondent's substantive response, the Respondent's grounds for dismissing the complaint were as follows:

(a) The Respondent asserted that the mutual funds in the joint accounts were suitable having regard to the documented KYC information on file for individual accounts[10] that DH and EH maintained with the Respondent, which indicated that:

(i) their risk tolerance was medium-high,
(ii) their investment time horizon was 11-20 years; and
(iii) their investment objectives were income and growth;

(b) The Respondent concluded, using the weighted average methodology for evaluating suitability that the investments purchased in the joint accounts were suitable when assessed against the medium-high risk tolerance on file for the individual accounts of the clients,

(c) although Fried had acknowledged in a statement to the Respondent that he was aware that clients DH and EH intended to use some of the sale proceeds invested in the joint accounts to pay the balance due on closing for their new home, the Respondent informed clients DH and EH that:

(i) Fried denied to the Respondent that the clients had told him that they would require the entire amount of the sale proceeds on closing within one year;
(ii) Fried denied to the Respondent that he had promised to preserve their capital;
(iii) Fried asserted to the Respondent that clients DH and EH had told him that they had other financial resources available to them to pay the balance due on closing; and
(iv) in light of the fact that the clients and Fried had put forward conflicting versions of events, the Respondent stated that it had no choice but to rely on the available

[10]In its response to the complaint, the Respondent was relying on updates to the documented KYC information for client EH's and client DH's individual accounts that the Respondent obtained on May 5, 2008, approximately two months before the joint accounts were opened.

documentary evidence, namely the NAAFs and KYC forms on file for the clients' individual accounts to assess the merits of the clients' complaint.

92. The Respondent failed to handle the complaint from clients DH and EH promptly and fairly in accordance with MFDA Rule 2.11, in that:

(a) contrary to MFDA requirements, the Respondent never documented the clients' KYC information for the joint accounts and it was not appropriate to presume that the KYC information on file for the individual accounts of clients DH and EH was appropriate for or applicable to the joint accounts that were opened for the clients;

(b) the Respondent ignored the fact that Fried had used a photocopy of a trade form signed by clients DH and EH in blank to purchase the mutual funds in the joint accounts which had subsequently declined in value, such that there was no evidence that clients DH and EH had authorized the purchase of the specific mutual funds at issue;

(c) the Respondent improperly justified the suitability of the mutual funds in the joint accounts *ex-post* using the weighted average methodology for assessing suitability;

(d) had the Respondent used the method for assessing suitability that it had in place at the time that it provided its substantive response to the clients' complaint, it should have concluded that the investments in the joint accounts were unsuitable;

(e) the Respondent ignored the fact that, notwithstanding Fried's admission that he knew the clients were relying on some portion of the sale proceeds to pay the balance due on closing for the new home, Fried had implemented virtually the identical strategy in both the Small Joint Account and the Large Joint Account with no apparent regard for capital preservation, a very short time horizon or a very low risk tolerance; and

(f) in spite of the absence of any notes made by Fried of his meeting with the clients on June 26, 2008, the Respondent failed to give sufficient weight to the clients' recollection of events, which recollection was supported by documentary evidence, including the agreement of purchase of sale in respect of their new home, the reference on the memo line of two of the cheques to "House Sale", and correspondence they had sent to Fried prior to the closing date.

93. In March 2010, after receiving the Respondent's substantive response, clients DH and EH wrote to the Respondent and objected to the Respondent's conclusions which were based in part on KYC information that was never meant to be applicable to the joint accounts.

94. In May 2010, the Respondent reimbursed clients DH and EH for the $2,680 in fees that they had paid to Fried personally.

95. In August 2010, Staff commenced its 2010 Compliance Examination of the Respondent. During the Compliance Examination at head office, Staff observed that two of the trade tickets that had been submitted by Fried in July 2008 to process the initial trades in one of the joint accounts of clients DH and EH contained photocopied client signatures. The Respondent agreed that the photocopied signatures appeared to indicate that Fried had obtained pre-signed trade order forms from clients DH and EH and used them to select and purchase the mutual funds in the joint accounts.

96. Further investigation by the Respondent revealed that Fried frequently obtained, maintained and used pre-signed forms to process trades for clients. Furthermore, on multiple occasions, Fried had charged clients fees (in addition to the commissions that he received or would receive from the Respondent) that were: (i) not disclosed to or authorized by the Respondent; (ii) not explained to the clients; nor (iii) justified on the basis of any services or work product that was actually provided to the clients. On the basis of these findings and others, the Respondent terminated Fried effective September 27, 2010.

97. In addition to not responding to the clients' complaint fairly, the Respondent failed to respond to the complaint promptly. The Respondent did not provide timely updates to the clients about the status of their complaint while its investigation and review was in progress, and did not account for the length of time (approximately 8 months) that it took to provide its substantive response to the complaint, which length of time was unreasonable in all the circumstances.

98. The Respondent admits that by engaging in the conduct described above, the Respondent failed to handle the clients' complaint promptly and fairly, contrary to MFDA Rules 2.11 and 2.1.1, and MFDA Policy No. 3.

SUBSEQUENT DEVELOPMENT

Current Practices

99. The Respondent has revised its policies and procedures since the 2008 Compliance Examination Report and now requires a new NAAF that includes documentation of KYC information to be completed in respect of each new client account that is opened by the Respondent (including new investment accounts of existing clients) and the Respondent has also discontinued use of the weighted average method for evaluating suitability.

Litigation By DH And EH

100. DH and EH were dissatisfied with the Respondent's substantive response to their complaint. Consequently, on July 30, 2014, they commenced a civil action against the Respondent before the Superior Court of Justice in Toronto to recover compensation for the losses in the joint investment accounts that were opened by the Respondent in July 2008. In furtherance of a resolution of this regulatory proceeding and the civil suit commenced against the Respondent by clients DH and EH, the Respondent entered into a settlement with clients DH and EH and agreed to pay (and has now paid) $50,000 to clients DH and EH in full and final settlement of their civil claim. Staff took the value of this compensation payment into account in arriving at the appropriate amount of the fine to be imposed on the Respondent in this proceeding. The compensation payment constitutes one of the Terms of Settlement, as set out in sub-paragraph 105(b) below.