Unofficial English Translation

Re Beaulne

IN THE MATTER OF:

The Rules of the Investment Industry Regulatory Organization of Canada (IIROC)

and

Benoit Beaulne

2012 IIROC 61

Investment Industry Regulatory Organization of Canada (IIROC)
Hearing Panel (Québec District)

Hearing: September 12, 2012
Decision: October 31, 2012

Hearing Panel
Me Claire Richer (Chair), Ms. Élaine C. Phénix, Mr. André D. Godbout
Appearances
Me Myriam G. Del Zotto, Counsel for IIROC
Respondent was not represented by counsel, nor was he present.

DECISIONS I) ON A MOTION BY VIRTUE OF SECTION 7.2 OF THE RULES OF PRACTICE AND PROCEDURE AND II) ON PENALTIES

I. PREAMBLE

¶ 1 In the Notice of Hearing dated May 18, 2012 (Notice of Hearing), IIROC set September 12 and 13, 2012, as the dates of the disciplinary hearing to determine whether the Respondent committed the contraventions alleged by IIROC Staff, the whole as detailed more fully in the aforesaid notice (Notice of Hearing) which is appended hereto and is deemed to be an integral part thereof.

¶ 2 On August 30, 2012, IIROC filed a motion with the Hearing Panel in application of Rule 7.2 of the IIROC Dealer Members Rules of Practice and Procedure (the Rules of Practice and Procedure) due to the fact that the Respondent had failed to serve a written response by virtue of Rule 7.1 of the Rules of Practice and Procedure.

¶ 3 The hearing was held on September 12, 2012. Respondent did not attend the hearing and was not represented by counsel. In fact, Respondent informed Counsel for IIROC by phone on September 5, 2012 that he would not be present, which he confirmed by email the same day.

II. HEARING ON THE MOTION BY VIRTUE OF RULE 7.2 OF THE RULES OF PRACTICE AND PROCEDURE

Hearing

¶ 4 Counsel reminded the Hearing Panel that IIROC sent the Notice of Hearing to the Respondent on May 18, 2012, with an explanatory letter describing the consequences of failing to serve a response to said notice

within the prescribed time limit as required pursuant to Rule 7.1 of the Rules of Practice and Procedure.

¶ 5 Having received no response from the Respondent in accordance with Rule 7.1 of the Rules of Practice and Procedure, IIROC sent the Notice of Hearing and explanatory letter to the Respondent again, on June 20, 2012. Respondent was also granted an extension of the deadline in order to serve a response.

¶ 6 On August 2, 2012, having still received no response from the Respondent, IIROC sent a third mailing, which contained, in addition to the Notice of Hearing and a second explanatory letter, a detailed list of the documents that led to the disciplinary proceeding instituted against the Respondent.

¶ 7 On August 30, 2012, still having had no news from the Respondent, Counsel for IIROC filed with the Hearing Panel and served on the Respondent the motion that is the subject of the present hearing.

¶ 8 As mentioned, Respondent informed Counsel for IIROC late in the day on September 5 that he would not attend and would not be represented by counsel at the hearing.

¶ 9 Counsel deposited before the members of the Hearing Panel a copy of Respondent's email of September 5, 2012 in which he also mentions that he had received IIROC's communications, twice in fact. The document is placed in evidence as a complement to, among others, the copies of the letters of June 20 and August 2 sent to the Respondent, along with all of the reports of transmission and service by bailiff of said mailings to the Respondent which had been delivered to the Hearing Panel with its motion.

¶ 10 By virtue of the motion, Counsel first requested to the Hearing Panel that the deadline for serving the motion on the Respondent be shortened by one day.

¶ 11 Counsel reminded the Hearing Panel that it may accept as proven the facts and contraventions alleged in the Notice of Hearing pursuant to Rule 7.2 of the Rules of Practice and Procedure, to wit:

> "7.2 ***Failure to Serve Response***
>
> *If a Respondent served with a Notice of Hearing fails to serve a Response in accordance with Rule 7.1:*
>
> *(a) the Organization may proceed with the hearing of the matter as set out in the Notice of Hearing without further notice to and in the absence of the Respondent; and*
>
> *(b) the Hearing Panel may, accept as proven the facts and violations alleged by the Organization in the Notice of Hearing, and may impose penalties and costs pursuant to Dealer Member Rules 20.33, 20.34 and 20.49.*

¶ 12 Consequently, if the motion is granted, Counsel requested that the Hearing Panel hear IIROC's observations and recommendations on penalties immediately.

¶ 13 Counsel argued that Respondent's behaviour creates a presumption of tremendous indifference on the latter's part, even an absence of remorse or of any acknowledgment of misconduct on his part.

Decision and reasons

¶ 14 After deliberation and given that Respondent did not respond to the Notice of Hearing even though he confirmed to Counsel, by phone and by email, that he received a copy thereof more than once and that he would neither attend nor be represented at the hearing, the Hearing Panel grants IIROC's motion and, more specifically:

i) confirms that it accepts to shorten by one day the deadline for notification or service of the motion on the Respondent;

ii) accepts as proven the facts and contraventions alleged by IIROC in the Notice of Hearing and, consequently, finds Respondent guilty of the following contraventions that are alleged in the Notice of Hearing:

1. Between October 2008 and April 25, 2010, the Respondent failed to use due diligence to ensure that his investment recommendations in leveraged exchange-traded funds constituted a

suitable investment for two (2) of his clients, given their financial and personal circumstances and their investment objectives, contrary to IIROC Dealer Member Rules 1300.1 (a), (p) and (q);

2. Between June 2008 and April 25, 2010, the Respondent failed to use due diligence to ensure that he had the necessary knowledge of the features and risks inherent in leveraged exchange-traded funds before recommending such an investment to two (2) of his clients, contrary to IIROC Dealer Member Rule 1300.1 (a).

and

iii) accepts to hear immediately IIROC's observations regarding the penalties to assess on the Respondent.

III. THE PENALTY HEARING

Hearing

¶ 15 The penalty hearing was held subsequently, on September 12, 2012.

¶ 16 The pleadings of IIROC's legal counsel were accompanied by abundant case law (distributed to the Hearing Panel beforehand), which was summarized in a comparison table that was distributed to the Hearing Panel and commented by Counsel.

¶ 17 In addition, Counsel reviewed IIROC Rules 20.33 and 20.49 regarding penalties, as well as the applicable disciplinary sanction guidelines, specifically Guideline 3.1 concerning improper sales practices.

¶ 18 The following aggravating and mitigating factors were then presented and elaborated upon:

a) Aggravating factors: the Respondent's lack of remorse, the financial vulnerability of the two clients in question, the gravity of Respondent's misconduct in failing to respect the level of risk tolerance stated in the New Account Application forms of said clients; the duration of the contraventions over a period of two years was also emphasized;

b) Mitigating factors: the fact that during the two-year period, Respondent was under strict supervision, that he derived no financial gain, and has no prior disciplinary record.

¶ 19 Counsel for IIROC recommends a fine of $40,000, costs in the amount of $10,000 (on a total of $70,548.47), disgorgement of $1,490.72 in fees collected by Respondent, a two-year suspension of approval in any capacity with an IIROC-regulated firm, the requirement to repeat IIROC's Conduct and Practices Handbook (CPH) Course before seeking reapproval, and 12 months of strict supervision in the event of reapproval.

Decision and reasons

Decision

¶ 20 After deliberation, analysis of the pleadings, examination of the documentation relative to the Notice of Hearing and the origins of the disciplinary proceedings, including the interviews with the Respondent and the two clients, and the trading reports for said clients, and after studying the case law submitted by Counsel, the Hearing Panel imposes the following penalties on the Respondent, namely:

a) a fine in the amount of $30,000;

b) costs in the amount of $10,000;

c) disgorgement of $1,490.72 in fees collected;

d) a two-year suspension of approval in any capacity with an IIROC-regulated firm; and

e) upon expiration of the two-year suspension, having repeated or repeating the CPH course before seeking reapproval and, in the event of reapproval, strict supervision for a period of twelve (12) months.

Reasons

¶ 21 The Hearing Panel has had no indication of any remorse on the Respondent's part, nor that Respondent has taken the counts against him seriously, given his failure to serve a response to the Notice of Hearing and to attend the hearing to explain himself or even answer the questions of the Hearing Panel, quite the contrary.

¶ 22 Respondent's misconduct and his offensive activity are of a grave nature; moreover, they are reprehensible and unacceptable for any representative.

¶ 23 Not only did Respondent appear not to have a good knowledge of the complex and risky financial instruments that he recommended to his two clients but, contrary to his primary "know your client" obligation, Respondent ignored the instructions stated on their new account application form. Moreover, Respondent had for years acted as the representative of these two clients, a retired couple who depended on the income from their respective portfolios, and the latter were justified in relying on Respondent's expertise.

¶ 24 Indeed, the documents consulted clearly show that the percentage of the two clients' respective assets limited to a single risky instrument (Leveraged Exchange-Traded Funds or LETF) came to represent nearly 100% as the financial crisis grew, whereas their new account application form stipulated a maximum of 20%.

¶ 25 It seems to us reasonable to think that the Respondent knew or should have known that the LETF, in the circumstances, were unsuitable instruments for these two clients given their financial means, which was known to the Respondent. The prospectus for said LETF contained numerous statements that should have alerted the Respondent, including the following statement found on page 7 of the Notice of Hearing:

> *"An ETF by itself does not constitute a balanced investment plan. ETFs are not for investors whose main objective is a regular income or the preservation of capital. Investors must be prepared to lose a large portion or even all of the money that they invest in an ETF (...)";*

¶ 26 The fact that he was under strict supervision during this period and that, at the same time, the financial markets were in grave turmoil, should have induced the Respondent to act with greater caution with his clients. Despite the deterioration of his clients' portfolios, Respondent continued his risky strategy by risking it all.

¶ 27 Respondent's presence at the hearing might have shed some light on this and other points, if the latter had deigned to attend.

¶ 28 The case law on the principle of investment suitability is abundant. We cite, for example, a pertinent extract from the Alberta decision, *Lamoureux* [2001] A.S.C.D., no 613:

> "*The obligation to ensure that recommendations are suitable or appropriate for the client rests solely with the registrant. This responsibility cannot be substituted, avoided or transferred to the client, even by obtaining from the client an acknowledgment that they are aware of the negative material factors or risks associated with the particular investment … Acknowledgment on the part of an investor of awareness of the material negative factors or risk does not convert an unsuitable investment into a suitable one."*

¶ 29 The Hearing Panel considers Respondent's behaviour equivalent to blatant mismanagement of his clients' accounts and intends to remind Respondent, and the industry generally, that such behaviour demands real deterrence.

¶ 30 In this respect, the following extract from *Re Mills* [2001] I.D.A.C.D. No. 7, April 17, 2001, like many other decisions, remains entirely relevant:

> *"Industry expectations and understandings are particularly relevant to general deterrence. If a penalty is less than industry understandings would lead its Members to expect for the conduct under consideration, it may undermine the goals of the Association's disciplinary process; similarly, excessive penalties may reduce respect for the process and concomitantly diminish its deterrent effect. Thus the responsibility of the District Council in a penalty hearing is to determine a penalty appropriate to the conduct and respondent before it, reflecting that its primary purpose is prevention rather than punishment."*

Signed at Montréal, Province of Québec, this October 31, 2012.

Claire Richer, Panel Chair

Élaine C. Phénix, Panel Member

André D. Godbout, Panel Member