Unofficial English Translation

Re National Bank Financial Inc.

IN THE MATTER OF:

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

and

National Bank Financial Inc.

2018 IIROC 09

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

Hearing held: December 7, 2017 and February 9, 2018
Decision rendered: April 3, 2018

Hearing Panel:
Me Alain Arsenault, Chair, Mr. Yves Ruest and Mr. Marcel Paquette
Appearances:
Me Francis Larin, Enforcement Counsel
Me Julie-Martine Loranger (McCarthy Tétrault, LLP), Counsel for the Respondent

DECISION ON SETTLEMENT AGREEMENT

I. PREAMBLE

¶ 1 After investigation, the Enforcement Department of the Investment Industry Regulatory Organization of Canada ("IIROC") concluded that National Bank Financial Inc. (the "Respondent") had committed a violation for which it may be disciplined by a Hearing Panel appointed pursuant to Section 8408 of the Consolidated Rules of IIROC (the "Hearing Panel"):

> *"Between June 15, 2009 and November 30, 2011, the Respondent failed to establish and maintain a system that allowed adequate supervision of the business activities of one of its registered representatives, contrary to Rule 38.1 and to Part III of Rule 2500 of the IIROC Dealer Member Rules."*

¶ 2 On November 14 and 15, 2017, the parties consented and agreed to the settlement of this matter by way of a settlement agreement, a copy of which is appended hereto and is deemed to be an integral part hereof.

¶ 3 This Settlement Agreement, by which the Respondent acknowledges its guilt in respect of the offence, provides for the following terms of settlement:

a) A fine in the amount of $110,000;

b) Costs in the amount of $10,000.

¶ 4 The factual background in this matter is presented in paragraphs 5 to 32 of this Settlement

Agreement, as follows:

> *"5. On June 11, 2009, IIROC published Guidance Note 09-0172 entitled 'Sales Practice Obligations Relating to Leveraged and Inverse Exchange-Traded Funds';*
>
> *6. This notice reminds Dealer Members of their supervision obligations, especially when they are promoting leveraged ETFs, or allowing their registered representatives to recommend such products;*
>
> *7. In June 2009, the Respondent organized a training session on the features and risks inherent in these products. Following this training, measures were taken to keep it available to the Respondent's employees via its intranet, and the training is still available on the intranet;*
>
> *8. On June 15, 2009, the Respondent published a communiqué on the subject of leveraged ETFs, which was titled 'Flash conformité 93'. This communiqué notably emphasizes the following information:*
>
> *(i) It references Guidance Note 09-0172 published by IIROC;*
>
> *(ii) It states that leveraged ETFs are typically unsuitable for retail investors who plan to hold them for longer than one trading session, particularly in volatile markets;*
>
> *(iii) It mentions that ETFs raise particular problems with respect to the knowledge and complexity of these products;*
>
> *(iv) It suggests that investment advisors carefully evaluate the suitability of every product that they recommend to their clients;*
>
> *(v) It reminds advisors that all sales literature must accurately and impartially present the products' features;*
>
> *(vi) It informs advisors that the Respondent has set up training regarding these products;*
>
> *(vii) It informs advisors of the Respondent's position regarding the recommended client profile for trading in its products and the suggested concentration, namely:*
>
> *a) Investment objectives: maximum growth;*
>
> *b) Investment knowledge: good or excellent;*
>
> *c) Concentration: marginal percentage of ETF assets.*
>
> *9. On July 3 and December 3, 2009, the Respondent made changes to the communiqué, notably permitting clients with a 'growth' profile to trade leveraged ETFs.*
>
> *10. On or around July 3, 2009, to ensure that the information in its 'Flash conformité 93' communiqué was being applied properly, the Respondent made a preliminary analysis of the activities of its investment advisors and identified one of its registered representatives, Mr. Christian Cloutier (Cloutier) as having a high number of clients with positions in leveraged ETFs, more specifically in Horizons BetaPro (HB) and ProShares Trust (PS);*
>
> *11. Following its preliminary analysis, although the Respondent had, at the time, established the number of such clients of Cloutier at 173, on or around August 19, 2009, it confirmed that, rather, the number 173 referred to the HB positions held by Cloutier's clients;*
>
> *12. For the period between June 2009 and December 2011, the number of Cloutier's clients who do not meet the profile stipulated in the Respondent's 'Flash conformité 93' communiqué, as well as the number of positions in question, break down as follows:*

LIST OF NON-COMPLIANT CLIENTS AND POSITIONS						
	June 2009	*December 2009*	*June 2010*	*December 2010*	*June 2011*	*December 2011*
Clients	*75*	*73*	*57*	*45*	*29*	*27*
HB positions	*132*	*124*	*77*	*22*	*9*	*7*
PS positions	*154*	*146*	*100*	*71*	*54*	*52*
Total Positions	*286*	*270*	*177*	*93*	*63*	*59*

13. *In July 2009, Cloutier verbally promised the Respondent to comply with the profile stipulated in the 'Flash conformité 93' communiqué, and to begin the process of liquidating the positions that did not meet that profile;*

14. *In August 2009, finding that Cloutier had still not begun the process of liquidating these positions, the Respondent ordered a report prepared by its staff, which established, among other things, the number of HB positions held by Cloutier's clients that were inconsistent with the profile stipulated in the 'Flash conformité 93' communiqué, with respect to investment objectives, as well as an average holding period of 263 days for these same positions;*

15. *On or around October 27, 2009, the Respondent sent Cloutier a first letter of warning;*

16. *The letter emphasized that many of Cloutier's clients did not meet the profile stipulated in the 'Flash conformité 93' communiqué and, to that end, the Respondent was requiring Cloutier to draw up a restructuring plan for the portfolios concerned, with fixed deadlines and specific objectives, within 30 days;*

17. *On or around November 26, 2009, Cloutier responded in writing that he would gradually proceed with a reduction of the positions concerned, but without providing any fixed deadlines or specific objectives;*

18. *In January 2010, the Respondent's compliance department met with Cloutier and asked him to liquidate his clients' ETF positions that still did not meet the profile stipulated in the "Flash conformité 93" communiqué, by no later than the end of April 2010;*

19. *On or around April 28 and April 29, 2010, the Respondent's compliance department sent Cloutier two lists, of clients and HB positions that still did not meet the profile stipulated in the 'Flash conformité 93', this time giving him until July 31, 2010 to comply;*

20. *On or around July 15, 2010, the Respondent sent Cloutier a new list of HB positions held by his clients and that still did not meet the profile stipulated in the 'Flash conformité 93', which totaled 78 positions at the time;*

21. *Despite the supervision measures put in place by its compliance department, the Respondent acknowledges that the various reports and lists that had been prepared up until then, concerning the ETF positions held by Cloutier's clients, did not identify either the investment knowledge of these clients, or the positions that they held in PS that did not meet the profile stipulated in the 'Flash conformité 93' communiqué, which were by then more numerous than the HB positions held by Cloutier's clients;*

22. *Cloutier had still not corrected the situation by the deadline set by the Respondent, namely July 31, 2010;*

23. *On or around October 4, 2010, the Respondent sent Cloutier a new list containing just the HB positions held by his clients that still did not meet the profile stipulated in the 'Flash conformité 93' communiqué, which totaled 43 positions by then;*

24. *On or around January 4, 2011, the Respondent's compliance department required and obtained, for the first time, the positions that Cloutier's clients held in PS;*

25. *On or around February 1, 2011, the Respondent sent Cloutier a second letter of warning;*

26. *The letter states, among other things, that despite the liquidation of some of the HB positions held by Cloutier's clients, many of these were in fact replaced with investments in PS, and that consequently, numerous positions remained in leveraged ETFs that still do not meet the profile stipulated in the 'Flash conformité 93' communiqué;*

27. *The second letter of warning to Cloutier set a new deadline to comply by April 30, 2011;*

28. *On or around February 15, 2011, the Respondent sent Cloutier a new list of all the leveraged ETF positions held by his clients which, for the first time, included the positions in PS;*

29. *Despite the deadline set by the Respondent in the second letter of warning to Cloutier, on April 30, 2011, there were still numerous clients and leveraged ETF positions that did not meet the profile stipulated in the 'Flash conformité 93' communiqué;*

30. *On or around October 7, 2011, the Respondent sent a letter to the Cloutier clients holding positions in leveraged ETFs, to inform them of the risks associated with these products;*

31. *On or around December 21, 2011, Cloutier's employment with the Respondent was terminated;*

32. *At the time, some of Cloutier's clients still held leveraged ETF positions that did not meet the profile stipulated in the 'Flash conformité 93' communiqué."*

¶ 5 On December 7, 2017 and February 9, 2018, a settlement hearing was held, during which the Hearing Panel heard the arguments of the legal counsel for both IIROC and the Respondent, who jointly requested acceptance of the Settlement Agreement that was concluded between them on November 14 and 15, 2017, the whole pursuant to Section 8428 (*Rules of Practice and Procedure*) and Section 8215 (*Enforcement Proceedings*) of IIROC's Consolidated Rules.

¶ 6 At the hearing, the legal counsel for both parties outlined the circumstances of the case that justify the terms of settlement agreed between the parties and presented decisions to demonstrate that the agreement falls within a reasonable range of appropriateness for disciplinary sanctions in similar matters.

¶ 7 The mitigating circumstances raised are as follows:

a) The Respondent's alleged misconduct concerns inadequate supervision, not the absence of supervision;

b) The Respondent took measures to ensure that its representatives have a sufficient and adequate level of knowledge of the features and risks inherent in leveraged exchange-traded funds, (leveraged ETFs);

c) Thus, following publication of IIROC Guidance Note 09-0172 in June 2009, the Respondent strengthened its policies by publishing the *Flash conformité 93* communiqué, and by the same token shoring up the requirements needed to recommend leveraged ETFs to clients;

d) In July 2009, before any investigation or examination by IIROC, the Respondent identified one of its registered representatives, Mr. Christian Cloutier (Cloutier) as having a high number of clients with positions in leveraged ETFs that did not meet the profile stipulated in Guidance Note 09-0172 and the *Flash conformité 93* communiqué;

e) Following this preliminary identification, the Respondent instructed Mr. Cloutier to respect this profile, and had several discussions and follow-ups with him in this regard;

f) On April 30, 2011, since many of the clients and leveraged ETF positions still did not meet the profile stipulated in the *Flash conformité 93* communiqué, the Respondent took the initiative of sending a letter to the clients concerned, to inform them of the risks associated with these products.

¶ 8 The legal counsel for the parties did not mention any aggravating factors during the first day of the hearing, although it became apparent subsequently that the Respondent had a disciplinary history in the matter of supervision.

¶ 9 In *Re Kloda*, 2016 IIROC 50, the hearing panel summed up as follows the powers and duties with which it is invested in a settlement hearing:

> *"10. The question for the Hearing Panel is whether, given the misconduct, the penalties fall within 'a reasonable range of appropriateness'. The Hearing Panel can either accept or reject the Settlement Agreement. It may not in any way alter the agreement or have knowledge of facts not in evidence in the Agreement. The Hearing Panel powers end there.*
>
> *11. As expressed in* Siska*:*
>
> > *Our mission is not that of an appeal body. We are not required to consider whether, having heard the case in an adversarial proceeding in the first instance, we would have ruled or not as the Parties agreed in their SETTLEMENT AGREEMENT. Neither is it up to us to consider whether the content of the SETTLEMENT AGREEMENT is too lenient or too harsh. That is not our role in the matter either. Even were we of the opinion that, having heard the case in first instance, our decision on Penalties would have been more lenient or more severe than the SETTLEMENT AGREEMENT, that would not be our mission either.*
>
> *12. As also pointed out in* Faber*:*
>
> > *It is not a question of whether the agreed-upon penalties are ones which this Panel would have imposed had the matter come before us for determination at a hearing. It is also not open to us to amend, re-write or alter the terms of the agreement reached between the parties.*
>
> *13. The primary purpose of IIROC disciplinary proceedings is to maintain high standards of conduct in the securities industry and to protect market integrity and improve overall business standards and practices.*
>
> *14. Disciplinary sanctions are twofold: not only a specific sanction against a contravention to the Rules but also a means that should serve as deterrence. 'In order to achieve this, sanctions should be significant enough to prevent and discourage future misconduct by the respondent (specific deterrence), and to deter others from engaging in similar misconduct (general deterrence)'. This is specifically what the Hearing Panel has to assess.*
>
> *15. Are the conclusions lenient or harsh to the point of being unreasonable, contrary to the public interest and/or of a nature to bring IIROC's disciplinary process into disrepute? The analyzed answer the Hearing Panel gives to that question should either be yes or no to the Agreement as submitted.*
>
> [References omitted]

¶ 10 After hearing the arguments of counsel for both parties and analyzing the Settlement Agreement, the Hearing Panel informed counsel on December 7, 2017, that the factual background, as presented, was

insufficient to allow it to determine whether the terms of settlement agreed between the parties were reasonable. The Hearing Panel therefore asked counsel to provide certain additional facts, which gave rise to a discussion on the powers of a hearing panel in a settlement hearing.

¶ 11 Counsel for the parties placed a lot of emphasis on IIROC Rule 8215(5) which stipulates that "[…] *After a settlement hearing, a hearing panel may accept or reject a settlement agreement*," as well as on Rule 8428(6) which mentions that "*At a settlement hearing, facts that are not contained in the settlement agreement must not be disclosed to the hearing panel without the consent of all parties, unless the respondent does not appear, in which case Enforcement Staff may disclose additional relevant facts, if requested by the hearing panel.* […]".

¶ 12 What clearly emerges from the case law and the regulations is that the powers of a hearing panel presiding over a settlement hearing are limited to either accepting or rejecting the agreement as presented, especially since, in the matter that concerns us, the parties took care to mention, in paragraph 40 of the agreement, that "*the Settlement Agreement shall constitute the entirety of the agreed facts presented at the Settlement Hearing, unless the parties agree that additional facts should be presented*."

¶ 13 The criteria for determining whether a hearing panel must accept or reject a settlement agreement are the public interest test and the sound administration of justice, as the Supreme Court of Canada specified in R. v. *Anthony-Cook*, [2016] 2 SCR 204 :

> *"32. Under the public interest test, a trial judge should not depart from a joint submission on sentence unless the proposed sentence would bring the administration of justice into disrepute or is otherwise contrary to the public interest. But, what does this threshold mean? Two decisions from the Newfoundland and Labrador Court of Appeal are helpful in this regard.*
>
> *33. In* Druken*, at para. 29, the court held that a joint submission will bring the administration of justice into disrepute or be contrary to the public interest if, despite the public interest considerations that support imposing it, it is so 'markedly out of line with the expectations of reasonable persons aware of the circumstances of the case that they would view it as a break down in the proper functioning of the criminal justice system'. And, as stated by the same court in R. v.* B.O.2*, 2010 NLCA 19, at para. 56 (CanLII), when assessing a joint submission, trial judges should 'avoid rendering a decision that causes an informed and reasonable public to lose confidence in the institution of the courts'.*

¶ 14 In *Re Cavalaris*, 2017 IIROC 04, the hearing panel confirmed, in paragraphs 15 to 19, that the public interest test is the one applied to joint submissions in the administrative law context, and is why the hearing panel must either accept or reject the proposed settlement agreement. The hearing panel notes, in paragraph 19:

> *"19. […] a joint submission in the regulatory context would be rejected only where the proposal, if accepted, would lead to the conclusion that the regulatory scheme had broken down or was otherwise not in the public interest."*

¶ 15 It adds, in paragraph 21:

> *"21. The sanction imposed must be appropriate to the circumstances of the particular conduct and the particular respondent, recognizing the need for specific and general deterrence. The IIROC Sanction Guidelines, while not binding, are useful in providing guidance. The Guidelines provide both general principles as well as a non-exhaustive list of key factors to consider for sanctions. […]"*

¶ 16 In the same vein, the hearing panel in *Re Industrial Alliance Securities Inc.*, 2015 IIROC 42, observed that "*To determine the reasonable nature of a penalty proposed in a settlement agreement, the hearing panel must ensure that the key factors cited in the* Dealer Member Disciplinary Sanction Guidelines *(Guidelines) have been taken into consideration*."

¶ 17 In this instance, the hearing Panel therefore has a duty to determine whether the terms of settlement agreed between the parties are reasonable and pass the public interest test, based solely on the facts reported in

said agreement. As already mentioned, the Guidelines can prove enlightening in such an exercise.

¶ 18 Indeed, page 2 of the Guidelines indicates that, among other things, the aim is to help the hearing panel determine whether to accept a settlement agreement. As the Guidelines state: *"[t]he appropriate sanction depends on the facts of a particular case and the circumstances of the conduct"*. They then outline certain sanction principles for IIROC disciplinary proceedings "*that should be considered in connection with the imposition of sanctions in all cases."*

¶ 19 The sanction principles that apply in this instance are:

> ***"1. Disciplinary sanctions are preventative in nature and should be designed to protect the investing public, strengthen market integrity, and improve overall business standards and practices.***
>
> *The purpose of sanctions in a regulatory proceeding is to protect the public interest by restraining future conduct that may harm the capital markets. In order to achieve this, sanctions should be significant enough to prevent and discourage future misconduct by the respondent (specific deterrence), and to deter others from engaging in similar misconduct (general deterrence).*
>
> *[…]*
>
> *General deterrence can be achieved if a sanction strikes an appropriate balance by addressing a Regulated Person's specific misconduct but is also in line with industry expectations. Any sanction imposed must be proportionate to the conduct at issue and should be similar to sanctions imposed on respondents for similar contraventions in similar circumstances. The sanction should be reduced or increased depending on the relevant mitigating and aggravating factors.*
>
> ***2. Disciplinary sanctions should be more severe for respondents with prior disciplinary records.***
>
> *A respondent's prior disciplinary record is an aggravating factor and may warrant a harsher sanction than would be required had this been the respondent's first disciplinary contravention.*
>
> *A prior disciplinary record for a similar or identical contravention strongly suggests that the prior sanction was not a sufficient deterrent, thereby necessitating an increased sanction in order to address specific deterrence. […]*
>
> *[…]*
>
> ***9. Remedial sanctions tailored to the specific misconduct can be a useful tool in effectively addressing regulatory misconduct.***
>
> *Sanctions in disciplinary proceedings are intended to prevent the recurrence of misconduct and deter others from similar misconduct. Therefore, sanctions may be tailored to the misconduct at issue in each case. This necessitates a review of the nature of the misconduct and both the aggravating and mitigating factors and the degree of responsibility by the respondent.*
>
> [References omitted]

¶ 20 Since sanctions should be tailored to address the misconduct involved in a particular case, a penalty must be proportionate to the gravity of the misconduct and the relative degree of responsibility of a respondent. To properly assess the gravity of specific misconduct, the decision-maker should look to a number of factors, including :

> *1. The number, size and character of the transactions at issue.*

2. *Whether the respondent engaged in numerous acts and/or a pattern of misconduct.*

3. *Whether the respondent engaged in the misconduct over an extended period of time.*

4. *Whether the misconduct was intentional, willfully blind, or reckless with respect to regulatory requirements.*

5. *Extent of harm to clients or other market participants.*

6. *Extent of harm to market integrity or the reputation of the marketplace, or both.*

7. *The level of vulnerability of the injured or affected client(s).*

8. *Consider the respondent's relevant disciplinary history […]*

9. *Extent to which the respondent obtained or attempted to obtain a financial benefit from the misconduct […]*

10. *[…]*

11. *In the case of a Dealer Member, whether the respondent accepted responsibility for and acknowledged the misconduct to the regulator prior to detection and intervention by the regulator.*

12. *[…]*

13. *Whether an individual respondent or Dealer Member respondent voluntarily employed subsequent corrective measures to revise general and/or specific procedures to avoid recurrence of misconduct.*

14. *Whether the respondent made voluntary acts of compensation, including voluntary disgorgement of commissions, profits, other benefits and/or payment of restitution to clients.*

15. *Whether the respondent provided proactive and exceptional assistance to IIROC in the investigation of the misconduct […]*

16. *Whether the respondent attempted to delay IIROC's investigation, to conceal information from IIROC, or intentionally provided inaccurate or misleading testimony or documentary information to IIROC.*

17. *Whether the respondent demonstrated reasonable reliance on competent supervisory, legal or accounting advice.*

18. *[…]*

19. *Whether the respondent attempted to conceal his or her misconduct or to lull into inactivity, mislead, deceive or intimidate a client, regulatory authorities or, in the case of an individual respondent, the member firm with which he or she is/was associated.*

20. *Whether the respondent failed to heed regulatory guidance with respect to the misconduct at issue.*

21. *Whether the respondent engaged in the misconduct at issue notwithstanding prior warnings from IIROC, another regulator or a supervisor (in the case of an individual respondent) that the conduct contravened firm policies, IIROC rules or applicable securities laws or regulations or was not in the best interests of the client or public."*

¶ 21 In the current case, the facts as presented in the Settlement Agreement are not, according to the Hearing Panel, sufficient to allow it to appreciate the nature and context of the misconduct, in order to confirm that the terms of agreement between the parties are reasonable and satisfy the public interest test.

¶ 22 Indeed, accepting a settlement agreement on the basis of incomplete facts that do not even tell you

whether the affected clients suffered any loss, certainly does not protect the public interest through general deterrence, since securities industry members will not know the gravity of the misconduct and the scope of the harm that gave rise to the sanction, as applicable.

¶ 23 More generally, how can the test of the reasonable well-informed person be applied if the facts are so incomplete that they do not permit this standard of objectivity to be reached? How does one determine, based on the case law, whether the agreed sanctions are reasonable in the context where it is impossible to compare the pertinent facts, namely the degree of gravity of the misconduct and the harm that resulted?

¶ 24 In the Hearing Panel's opinion, accepting the settlement agreement as presented is likely to bring the administration of IIROC rules into disrepute and to harm the reputation of the securities market. More importantly, we must not, because our justice system assigns so much importance to dispute resolution, run the risk of undermining the public's trust in the authority that is responsible for ensuring public protection and the integrity of the securities market. IIROC, while it must encourage settlement negotiation, must not become a kind of "*old boys' club*" where outsiders would find it impossible to know the nature and scope of the misconduct that led to the settlement agreement.

¶ 25 It is with these considerations in mind that this Hearing Panel insisted that counsel for the parties complete the factual background in the matter, so that it might decide whether to accept the proposed agreement. In so doing, the Hearing Panel was following the approach advocated by the Québec Court of Appeal in *Poulin c. La Reine*, 2010 QCCA 1854, in which the Court mentions that if the judge has any reluctance regarding a joint submission, he must inform the parties and give them the opportunity to respond.

¶ 26 In *Re Donnelly*, 2016 IIROC 23, the hearing panel stated moreover that a hearing panel is entitled to reject a settlement agreement if the information provided does not allow it to determine whether the agreed sanctions are reasonable:

> *"5. The panel determined that it had to be satisfied regarding three considerations before it could accept the settlement agreement. First, the agreed penalties had to be within an acceptable range taking into account similar cases. Secondly, the agreed penalties had to be fair and reasonable (i.e. proportional to the seriousness of the contravention and taking into consideration other relevant circumstances) and should appear to be so to members of the public and industry. Thirdly, the agreed penalties should serve as a deterrent to the respondent and to industry. To be satisfied on these three considerations required an understanding of the particular facts of the case, the circumstances of the respondent, and the impact on him of the agreed penalties.*
>
> *[…]*
>
> *9. A panel considering whether to accept a settlement agreement and its agreed penalties is in a different position than a panel determining an appropriate penalty in a contested hearing.*
>
> *10. Each needs to consider precedents and the law and, most importantly, the particular facts and circumstances of the case, including the particular circumstances of the specific respondent.*
>
> *11. However, unlike a panel in a contested hearing that must set the actual penalties that appear appropriate to it, a panel in a hearing to consider a settlement agreement has only two options under IIROC rules: to accept the agreed settlement with its penalties because the panel agrees that the penalties are acceptable, or to reject the agreed settlement <u>because the agreed penalties are not acceptable or because the panel has not been given enough information for it to come to a determination that the agreed penalties are acceptable</u>."* [Our emphasis]

¶ 27 Evidently, as was specified in *Re Donnelly*, the hearing panel may invite the parties to provide the additional information that it thinks it needs to reach a reasonable decision, but it cannot compel them to (par. 12).

¶ 28 It is with these considerations as backdrop that the hearing panel summed up, in *Re Scotia Capital*,

2017 IIROC 48, the tests by which a hearing panel must accept or reject a settlement agreement:

> *"8. In the recent case* Bugden (Re)*, 2017 IIROC 30, after considering the test established in* Milewski*, the Panel stated as follows with respect to the settlement process:*
>
> > *[…] The efficacy of the settlement process is a cornerstone of effective and efficient regulatory process. Parties who have engaged in good faith negotiations to reach an agreement that is appropriate in the circumstances and is reasonable in its application of the principles of general and specific deterrence, remedial intent and public interest are entitled to expect the agreement to receive appropriate consideration by a panel. If in its due consideration the panel determines the agreement falls within the governing parameters, it should be accepted; if not the agreement should be rejected. The parties would then be free to enter into a subsequent agreement or proceed to a hearing on the merits."*

¶ 29 The Supreme Court of Canada also recognized, in the *Anthony-Cook* ruling cited above, that certainty concerning the outcome of the settlement agreement must yield when its acceptance would tend to bring the administration of justice into disrepute:

> *"42. Hence, the importance of trial judges exhibiting restraint, rejecting joint submissions only where the proposed sentence would be viewed by reasonable and informed persons as a breakdown in the proper functioning of the justice system. A lower threshold than this would cast the efficacy of resolution agreements into too great a degree of uncertainty. The public interest test ensures that these resolution agreements are afforded a high degree of certainty.*
>
> *43. At the same time, this test also recognizes that certainty of outcome is not 'the ultimate goal of the sentencing process. Certainty must yield where the harm caused by accepting the joint submission is beyond the value gained by promoting certainty of result'."* [Reference omitted]

¶ 30 The Court notes in this regard that acceptance of a recommendation should not be done blindly and that if the agreement is controversial, the judge will be justified in wanting to know the circumstances:

> *"53. Third, when faced with a contentious joint submission, trial judges will undoubtedly want to know about the circumstances leading to the joint submission — and in particular, any benefits obtained by the Crown or concessions made by the accused. The greater the benefits obtained by the Crown, and the more concessions made by the accused, the more likely it is that the trial judge should accept the joint submission, even though it may appear to be unduly lenient. For example, if the joint submission is the product of an agreement by the accused to assist the Crown or police, or an evidentiary weakness in the Crown's case, a very lenient sentence might not be contrary to the public interest. On the other hand, if the joint submission resulted only from the accused's realization that conviction was inevitable, the same sentence might cause the public to lose confidence in the criminal justice system.*
>
> *54. Counsel should, of course, provide the court with a full account of the circumstances of the offender, the offence, and the joint submission without waiting for a specific request from the trial judge. As trial judges are obliged to depart only rarely from joint submissions, there is a 'corollary obligation upon counsel' to ensure that they 'amply justify their position on the facts of the case as presented in open court '. […] Sentencing — including sentencing based on a joint submission — cannot be done in the dark. The Crown and the defence must 'provide the trial judge not only with the proposed sentence, but with a full description of the facts relevant to the offender and the offence ', in order to give the judge 'a proper basis upon which to determine whether [the joint submission] should be accepted ' […].*
>
> *55. This is not to say that counsel must inform the trial judge of 'their negotiating positions or the substance of their discussions leading to the agreement ' […]. But counsel must be able to inform the trial judge why the proposed sentence would not bring the administration of justice into disrepute or otherwise be contrary to the public interest. If they do not, they run the risk*

that the trial judge will reject the joint submission.

56. There may, of course, be cases where it is not possible to put the main considerations underlying a joint submission on the public record because of safety or privacy concerns, or the risk of jeopardizing ongoing criminal investigations […]. In such cases, counsel must find alternative means of communicating these considerations to the trial judge in order to ensure that the judge is apprised of the relevant considerations and that a proper record is created for appeal purposes.

57. A thorough justification of the joint submission also has an important public perception component. Unless counsel put the considerations underlying the joint submission on the record, 'though justice may be done, it may not have the appearance of being done; the public may suspect, rightly or wrongly, that an impropriety has occurred ' […]. [References omitted]

¶ 31 In *Re Scotia Capital*, cited above, the hearing panel imported these principles to a settlement hearing over which it was presiding:

"15. The obligation on Staff in an IIROC case is the same as owed by any lawyer in a prosecutorial role: that is that he or she must make full disclosure to the tribunal of all material facts which bear on the case before it. In terms specific to the present circumstances, Staff must ensure that the hearing panel charged with whether or not to accept a joint settlement has all the facts in Staff's possession which might reasonably be expected to be material to that decision. If the hearing panel were deprived of such information, it would not only be contrary to the public interest, it also would hold the administration of justice in disrepute […]

16. Clearly, Staff has the express power to withhold facts and, if it does so, it is open to the hearing panel to refuse to accept the joint settlement. But to do so, it has to know what information has been withheld. If the facts withheld are material but their nature is unknown, there is a serious breakdown in the administration of justice. Thus the role of Staff is crucial in ensuring that the hearing panel has the facts necessary to decide whether to accept a settlement agreement. The right of Staff to withhold facts is unchallenged except to the extent it prevents a hearing panel from having facts material to the exercise of its discretion."

¶ 32 Let us note that it will not always necessarily be about obtaining accurate quantitative data, but about making sure that all of the relevant facts are brought to the hearing panel's attention. The key factors mentioned in the *IIROC Sanction Guidelines* are a good indicator of facts that can be considered relevant.

¶ 33 On this score, the Hearing Panel would like to revisit the IIROC prosecution's insistence on claiming that, if a particular fact could have had an impact on determining the reasonableness of the settlement terms agreed between the parties, he would have included it in the agreement's factual background. With respect, given the rules applicable to settlement hearings, the limited powers of the Hearing Panel in this matter and the case law cited above, it is not up to the Hearing Panel to rule a fact irrelevant for the sole reason that the parties did not include it in their settlement agreement. Indeed, such omission could be an oversight, or stem from the negotiations leading up to the settlement agreement.

¶ 34 Of course, the reasons that might lead a party to publicly present one fact and not disclose another are numerous, and there can be no question of informing the hearing panel as to what these reasons are. Indeed, to encourage parties to settle their differences and protect the integrity of the settlement process, the latter must have the assurance that any negotiations that result in a settlement agreement being signed will remain confidential and cannot be used against them subsequently. Nonetheless, the point remains that all relevant facts – including the presence or absence of a loss for the clients – must be brought to the attention of the hearing panel one way or another, in the wording of the settlement agreement, since the facts mentioned in the agreement are the only ones that the hearing panel may rely on to make its decision on whether to accept or reject the settlement agreement.

¶ 35 In the matter at hand, counsel agreed, on February 9, 2018, to provide the Hearing Panel with some of

the supplementary information that was requested. These facts, which will be appended to the settlement agreement, are as follows:

Losses	$ (13,660.89)	13 clients
Gains	$ 549,084.62	61 clients
Total	$ 535,423.73	74 clients

¶ 36 Though succinct, the new information now allows the Hearing Panel to appreciate the reasonableness of the terms of settlement agreed between the parties.

¶ 37 In this regard, the prosecution cited numerous decisions pertaining to contraventions similar to the one alleged against the Respondent in this instance. Since every case must be evaluated according to its own facts and circumstances, it is pointless to review the particular facts of each of the cited decisions. Suffice it to say that in *Re RBC Dominion Securities*, cited above, and in *Re Leede and Bergen*, 2015 IIROC 37, a settlement agreement had been signed, in both cases providing for a fine of $90,000 to be paid by the dealer for failing to adequately supervise a registered representative and the accounts of certain clients, during a period of approximately a year and a half and three and a half years respectively, which is consistent with the contravention that is in question here.

¶ 38 We note that *Re RBC Dominion Securities* concerned 37 clients, some of whom suffered losses. In its reasons for accepting the settlement agreement, the hearing panel notably retained the fact that, prior to any investigation or examination by IIROC, the respondent had instructed the representative concerned to recommend to his clients that they discontinue the strategy that had been put in place and which was unsuitable for them.

¶ 39 In *Leede and Bergen*, the four clients concerned sustained losses ranging from 8% to 28% of their portfolio.

¶ 40 In the matter before us, the Respondent failed to adequately supervise its registered representative, Mr. Cloutier, as well as the latter's client accounts, over approximately a two-and-a-half-year period. Of the 75 clients concerned, 13 sustained an average loss of $1,050.84. As in *RBC Dominion Securities*, the Respondent had, prior to any investigation or examination by IIROC, detected a high number of clients with positions in leveraged ETFs that did not meet the profile stipulated in *Guidance Note 09-0172* and the *Flash conformité 93* communiqué.

¶ 41 Following this early detection, the Respondent instructed its registered representative to respect said profile, and had several discussions and follow-ups with him on the subject. However, given the persistent non-compliance of some of the positions held by Mr. Cloutier's clients, the Respondent took corrective measures, sending a letter to the clients whose positions in leveraged ETFs did not meet the profile stipulated in the *Flash conformité 93* communiqué, to inform them of the risks associated with these products.

¶ 42 Moreover, just prior to the material period, the Respondent had taken measures to ensure that its representatives had sufficient and adequate knowledge of the features and risks inherent in leveraged ETFs, notably by setting up a training on these products and publishing the *Flash conformité 93* communiqué, thus strengthening its policies and solidifying the necessary requirements for recommending leveraged ETFs to clients.

¶ 43 Thus, there is no question of this being, to echo the words of the hearing panel in *RBC Dominion Securities* above, "[…] *a case of complete abdication of responsibility by the branch manager or the head office compliance department. It is a case where they could have done more and investigated the situation more thoroughly*" (par. 34).

¶ 44 Still, as mentioned in the *IIROC Sanction Guidelines*: "*a prior disciplinary record for a similar or identical contravention strongly suggests that the prior sanction was not a sufficient deterrent*."

¶ 45 Thus, the Respondent's own disciplinary record on a similar matter, in 2011, shows that it agreed to pay

a fine of $250,000.

¶ 46 Considering the contravention of the same nature alleged herein, it would be easy to conclude that that amount was not high enough to achieve the desired objective of deterrence, especially since the circumstances of the 2011 agreement are similar to those at issue here, notably the facts that the failure to supervise occurred over a period of more than a year, that the Respondent was aware of the irregularities in question but did not take corrective measures within a reasonable timeframe, and that no client reported any loss arising from the conduct of the representatives concerned.

¶ 47 Nevertheless, in 2011, the Respondent's failure to supervise continued until IIROC discovered the problems in the course of an investigation, and the shortcomings persisted even after the material investigation period. This element must be considered a factor inasmuch as, in the case that concerns us, the Respondent detected the problem and attempted to remedy it – even though it could have done more – before any intervention by IIROC.

¶ 48 Therefore, the Hearing Panel must base itself on all those circumstances, on the relevant case law, and on the stated objectives of the *IIROC Sanction Guidelines*, to determine whether the $110,000 fine agreed to in this settlement agreement is reasonable.

¶ 49 This amount, which sits between the $90,000 fine endorsed by the case law for a similar contravention and the $250,000 fine previously paid by the Respondent in a matter of the same nature, but which presented a strong aggravating factor that is missing in the present case, does not appear contrary to public order, nor would it tend to bring the administration of justice into disrepute.

¶ 50 Consequently, the Hearing Panel accepts the Settlement Agreement which is appended below to give effect to it.

NOW THEREFORE THE HEARING PANEL:

ACCEPTS the Settlement Agreement signed by the parties on November 14 and 15, 2017, appended hereto, and gives effect to it from this date.

Signed at Montréal, this 3rd day of April, 2018

Me Alain Arsenault

Mr. Marcel Paquette

Mr. Yves Ruest, member

SETTLEMENT AGREEMENT

PART I - INTRODUCTION

1. The Investment Industry Regulatory Organization of Canada ("IIROC") will issue a notice of application to announce that a settlement hearing will be held before a Hearing Panel (the Hearing Panel) to consider whether, pursuant to Section 8215 of the Consolidated Rules of IIROC, the Hearing Panel should accept a settlement agreement (the Settlement Agreement) between Staff of IIROC (Staff) and National Bank Financial Inc. (the Respondent).

PART II - JOINT SETTLEMENT RECOMMENDATION

2. Staff and the Respondent jointly recommend that the Hearing Panel accept the Settlement Agreement in accordance with the terms set forth below.

PART III – AGREED FACTS

3. For purposes of the Settlement Agreement, the Respondent agrees with the facts set out in Part III of this Settlement Agreement.

Overview

4. After establishing that several clients of one of its registered representatives held positions in leveraged exchange-traded funds (leveraged ETFs), whereas these positions did not coincide with their investment objectives or investment knowledge, the Respondent failed to take reasonable measures to ensure that this situation was corrected in a timely fashion.

PARTICULARS

5. On June 11, 2009, IIROC published Guidance Note 09-0172 entitled "*Sales Practice Obligations Relating to Leveraged and Inverse Exchange-Traded Funds"* ;

6. This notice reminds Dealer Members of their supervision obligations, especially when they are promoting leveraged ETFs, or allowing their registered representatives to recommend such products;

7. In June 2009, the Respondent organized a training session on the features and risks inherent in these products. Following this training, measures were taken to keep it available to the Respondent's employees via its intranet, and the training is still available on the intranet;

8. On June 15, 2009, the Respondent published a communiqué on the subject of leveraged ETFs, which was titled "*Flash conformité 93*". This communiqué notably emphasizes the following information:

   (i) It references Guidance Note 09-0172 published by IIROC;

   (ii) It states that leveraged ETFs are typically unsuitable for retail investors who plan to hold them for longer than one trading session, particularly in volatile markets;

   (iii) It mentions that ETFs raise particular problems with respect to the knowledge and complexity of these products;

   (iv) It suggests that investment advisors carefully evaluate the suitability of every product that they recommend to their clients;

   (v) It reminds advisors that all sales literature must accurately and impartially present the products' features;

   (vi) It informs advisors that the Respondent has set up training regarding these products;

   (vii) It informs advisors of the Respondent's position regarding the recommended client profile for trading in ETFs, namely:

      a) Investment objectives: maximum growth;

      b) Investment knowledge: good or excellent;

      c) Concentration: marginal percentage of ETF assets.

9. On July 3 and December 3, 2009, the Respondent made changes to this communiqué, notably permitting clients with a "growth" profile to trade leveraged ETFs.

10. On or around July 3, 2009, to ensure that the information in its "*Flash conformité 93*" communiqué was being applied properly, the Respondent performed a preliminary analysis of the activities of its investment advisors and identified one of its registered representatives, Mr. Christian Cloutier (Cloutier), as having a high number of clients with positions in leveraged ETFs, more specifically in Horizons BetaPro (HB) and ProShares Trust (PS);

11. Following its preliminary analysis, although the Respondent had, at the time, established the number of such clients of Cloutier at 173, on or around August 19, 2009, it confirmed that, rather, the number 173 referred to the positions held in HB by Cloutier's clients;

12. For the period between June 2009 and December 2011, the number of Cloutier's clients who do not meet the profile stipulated in the Respondent's "*Flash conformité 93*" communiqué, as well as the number of positions in question, break down as follows:

LIST OF NONCOMPLIANT CLIENTS AND POSITIONS						
	June 2009	December 2009	June 2010	December 2010	June 2011	December 2011
Clients	75	73	57	45	29	27
HB positions	132	124	77	22	9	7
PS positions	154	146	100	71	54	52
Total positions	286	270	177	93	63	59

13. In July 2009, Cloutier verbally promised the Respondent to comply with the profile stipulated in the "*Flash conformité 93*" communiqué, and to begin the process of liquidating the positions that did not;

14. In August 2009, finding that Cloutier had still not begun the process of liquidating these positions, the Respondent ordered a report prepared by its staff, which established, among other things, the number of HB positions held by Cloutier's clients that were inconsistent with the profile stipulated in the "*Flash conformité 93*" communiqué, with respect to investment objectives, as well as an average holding period of 263 days for these same positions;

15. On or around October 27, 2009, the Respondent sent Cloutier a first letter of warning;

16. The letter emphasized that many of Cloutier's clients did not meet the profile stipulated in the "*Flash conformité 93*" communiqué and, to that end, the Respondent was requiring Cloutier to draw up a restructuring plan for the portfolios concerned, with fixed deadlines and specific objectives, within 30 days;

17. On or around November 26, 2009, Cloutier responded in writing that he would gradually proceed with a reduction of the positions concerned, but without providing any fixed deadlines or specific objectives;

18. In January 2010, the Respondent's compliance department met with Cloutier and asked him to liquidate his clients' ETF positions that still did not meet the profile stipulated in the "*Flash conformité 93*" communiqué, by no later than the end of April 2010;

19. On or around April 28 and April 29, 2010, the Respondent's compliance department sent Cloutier two lists, of clients and HB positions that still did not meet the profile stipulated in the "*Flash conformité 93*", this time giving him until July 31, 2010 to comply;

20. On or around July 15, 2010, the Respondent sent Cloutier a new list of HB positions held by his clients and that still did not meet the profile stipulated in the "*Flash conformité 93*", which totaled 78 positions at the time;

21. Despite the supervision measures put in place by its compliance department, the Respondent acknowledges that the various reports and lists that had been prepared up until then, concerning the ETF positions held by Cloutier's clients, did not identify either the knowledge of investing of these clients, or the positions that they held in PS that did not meet the profile stipulated in the "*Flash conformité 93*" communiqué, which were by then more numerous than the HB positions held by Cloutier's clients;

22. Cloutier had still not corrected the situation by the deadline set by the Respondent, namely July 31, 2010;

23. On or around October 4, 2010, the Respondent sent Cloutier a new list containing just the HB positions

held by his clients that still did not meet the profile stipulated in the "*Flash conformité 93*" communiqué, which totaled 43 positions by then;

24. On or around January 4, 2011, the Respondent's compliance department required and obtained, for the first time, the positions that Cloutier's clients held in PS;

25. On or around February 1, 2011, the Respondent sent Cloutier a second letter of warning;

26. The letter states, among other things, that despite the liquidation of some of the HB positions held by Cloutier's clients, many of these were in fact replaced with investments in PS, and that consequently, numerous positions remained in leveraged ETFs that still do not meet the profile stipulated in the "*Flash conformité 93*" communiqué;

27. The second letter of warning to Cloutier set a new deadline to comply by April 30, 2011;

28. On or around February 15, 2011, the Respondent sent Cloutier a new list of all the leveraged ETF positions held by his clients which, for the first time, included the positions in PS;

29. Despite the deadline set by the Respondent in the second letter of warning to Cloutier, on April 30, 2011, there were still numerous clients and leveraged ETF positions that did not meet the profile stipulated in the "*Flash conformité 93*" communiqué;

30. On or around October 7, 2011, the Respondent sent a letter to the Cloutier clients holding positions in leveraged ETFs, to inform them of the risks associated with these products;

31. On or around December 21, 2011, Cloutier's employment with the Respondent was terminated;

32. At the time, some of Cloutier's clients still held leveraged ETF positions that did not meet the profile stipulated in the "*Flash conformité 93*" communiqué.

PART IV – CONTRAVENTION

33. By reason of the above-described conduct, the Respondent contravened IIROC Dealer Member Rules as follows:

> Between June 15, 2009 and November 30, 2011, the Respondent failed to establish and maintain a system that allowed adequate supervision of the business activities of one of its registered representatives, contrary to Rule 38.1 and to Part III of Rule 2500 of the IIROC Dealer Member Rules.

PART V - TERMS OF SETTLEMENT

34. The Respondent accepts the following penalties and costs:

    a) A fine in the amount of $110,000; and

    b) The Respondent agrees to pay IIROC costs in the amount of $10,000.

35. If the Hearing Panel accepts this Settlement Agreement, the Respondent agrees to pay the above-mentioned amounts within 30 days of such acceptance, unless otherwise agreed between Staff and the Respondent.

PART VI – STAFF COMMITMENT

36. If the Hearing Panel accepts the Settlement Agreement, Staff will not initiate any further action against the Respondent in relation to the facts set out in Part III and the contraventions in Part IV of this Settlement Agreement, subject to the provisions of paragraph 37 below.

37. If the Hearing Panel accepts this Settlement Agreement and the Respondent fails to comply with any of its terms, Staff may bring proceedings under Rule 8200 against the Respondent. These proceedings may be based on, but are not limited to, the facts set out in Part III of this Settlement Agreement.

PART VII – SETTLEMENT ACCEPTANCE PROCEDURE

38. The Settlement Agreement is subject to acceptance by the Hearing Panel;

39. The Settlement Agreement shall be presented to a Hearing Panel at a settlement hearing held in accordance with the procedures described in Sections 8215 and 8428, in addition to any other procedures that may be agreed upon between the parties.

40. Staff and the Respondent agree that this Settlement Agreement shall constitute all of the agreed facts that will be submitted at the settlement hearing, unless the parties agree that additional facts should be submitted at the settlement hearing. If the Respondent does not appear at the settlement hearing, Staff may disclose additional relevant facts, if requested by the Hearing Panel.

41. If the Hearing Panel accepts the Settlement Agreement, the Respondent waives its right, under IIROC rules and any applicable legislation, to a disciplinary hearing, review or appeal.

42. If the Hearing Panel rejects the Settlement Agreement, Staff and the Respondent may enter into another settlement agreement; or Staff may proceed to a disciplinary hearing in relation to the same allegations or to related allegations.

43. The terms of this Settlement Agreement are confidential unless and until this Settlement Agreement has been accepted by the Hearing Panel.

44. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel and IIROC will post a full copy of this Settlement Agreement on the IIROC website. IIROC will also publish a summary of the facts, contraventions, and the sanctions agreed upon in this Settlement Agreement.

45. If this Settlement Agreement is accepted, the Respondent agrees that neither it, nor anyone on its behalf, will make a public statement inconsistent with this Settlement Agreement.

46. The Settlement Agreement shall become effective and binding upon the Respondent and Staff from the date of its acceptance by the Hearing Panel.

PART VIII – SIGNATURE OF THE SETTLEMENT AGREEMENT

47. This Settlement Agreement may be signed in one or more counterparts which, together, will constitute a binding agreement.

48. The fax or electronic copy of any signature will be treated as an original signature.

SIGNED this 14th day of November, 2017**.**

(S) WITNESS	**(S) DAVID GRAY**
Witness	**Name: « David Gray »** **Title: « VP, Legal Affairs »** **For National Bank Financial Inc.**

SIGNED this 15th day of November, 2017**.**

(S) LINDA VACHET	**(S) FRANCIS LARIN**
Witness	**Francis Larin** Senior Enforcement Counsel, on behalf of Enforcement Staff of the Investment Industry Regulatory Organization of Canada

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