INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

ON BEHALF OF

THE INVESTMENT DEALERS ASSOCIATION OF CANADA

IN THE MATTER OF:

THE BY-LAWS OF THE INVESTMENT DEALERS ASSOCIATION OF CANADA

AND

THE DEALER MEMBER RULES OF THE INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

AND

RÉAL CASTONGUAY

NOTICE OF HEARING

TAKE NOTICE that, pursuant to Part 10 of Rule 20 of the Investment Industry Regulatory Organization of Canada (IIROC) and s. 1.9 of Schedule C.1 to Transition Rule No. 1, a hearing will be held before a hearing panel of IIROC (Hearing Panel) on March 21, 2012, in the IIROC Boardroom at 5 Place Ville Marie, suite 1550, Montréal (Québec) at 9 a.m., or as soon thereafter as the hearing can be heard.

TAKE FURTHER NOTICE that, pursuant to Rule 6.2 of the Dealer Member Rules of Practice and Procedure, the hearing shall be designated on the:

☒ The Standard Track

☐ The Complex Track

TAKE FURTHER NOTICE that on June 1, 2008, IIROC consolidated the regulatory and enforcement functions of the Investment Dealers Association of Canada (IDA) and Market Regulation Services Inc. (RS). Pursuant to the *Administrative and Regulatory Services Agreement* between the IDA and IIROC, the IDA has retained IIROC to provide services for the IDA to carry out its regulatory functions with respect to the conduct of IDA registrants occurring before June 1, 2008.

THE PURPOSE OF THE HEARING is to determine whether Réal Castonguay (Respondent) has committed the following contraventions that are alleged by the staff of IIROC (Staff):

(i) Between October 2003 and June 2007, the Respondent showed a lack of diligence toward one of his clients by neglecting to inform the latter of the existence of an essential fact in connection with the Cierra and Prospector offerings, even though he was aware of this essential fact at the time his client invested in these two offerings, thereby engaging in conduct unbecoming or detrimental to the public interest, contrary to By-law 29.1 of the IDA;

(ii) Between January 2003 and June 2007, the Respondent facilitated investments for two (2) individuals, one a client and the other a non-client, in the Cierra and Prospector offerings, without the knowledge and consent of his employer, an IDA Member firm, thereby engaging in conduct unbecoming or detrimental to the public interest, contrary to By-law 29.1 of the IDA.

PARTICULARS

TAKE FURTHER NOTICE that the following is a summary of the facts alleged by Staff and which are to be relied upon at the hearing of this matter:

SUMMARY

1. The Respondent facilitated investments for two (2) individuals, one a client and the other a non-client, in the Cierra and Prospector offerings, without the knowledge of his

employer, and neglected to inform them of a decision by the Commission des valeurs mobilières du Québec (CVMQ) notably regarding allegations of dishonesty against two individuals who were closely involved in the Canadian companies, and who acted as middlemen with investors in respect of these two same investment products. The Respondent failed to inform his client and the latter's wife of the existence of the decision rendered by the CVMQ, even though he knew that they were continuing to invest in the Cierra and Prospector offerings at the time the decision was rendered;

THE RESPONDENT

2. The Respondent has worked in the securities industry as a registered representative (retail) since 1991;

3. Between July 1992 and December 2002, the Respondent worked at MCA Valeurs mobilières inc. (MCA), an IDA Member firm;

4. At the material times, the Respondent was employed with Raymond James Ltd. (RJ), an IDA Member firm;

5. On June 1, 2008, the Respondent became a registrant of IIROC;

6. Since the month of October 2009, the Respondent has been in the employ of Canaccord Capital Inc., which is also on IIROC-regulated firm;

LACK OF DILIGENCE

7. Between 1992 and 2002, namely while the Respondent worked for MCA, he met Mr. B, a representative registered with the CVMQ, and they became friends;

8. On October 17, 2003, the CVMQ rendered a decision concerning company D, Mr. B and Mr. C. The decision states, notably:

    (i) That the investment setup offered by Gestionnaire DPI and company D for the purchase of DPI, DPI (IV) and DPI (V) shares constitutes an artifice for eluding the obligation to prepare a prospectus;

    (ii) That the offering memorandums of October 9, 1998 and 1999 which formed the basis for a public distribution to investors, contained false and misleading information concerning the use of the investment product. Company D was the underwriter of this public distribution;

    (iii) That commissions were paid by company D to a representative who did not possess the required approval, and to an unregistered person;

(iv) That company D and Mr. B failed in their obligation to act in good faith, and with honesty and loyalty in their dealings with investors;

(v) That the CVMQ's director of compliance expelled company D, Mr. B and Mr. C for a period of ten (10) years each;

9. At the time client A invested in the Cierra and Prospector offerings, the Respondent was aware of the October 17, 2003 decision handed down by the CVMQ against company D, Mr. B and Mr. C;

10. However, despite the fact that the CVMQ decision was rendered contemporaneously to client A's investments in the Cierra and Prospector offerings, the Respondent did not inform him of its existence;

11. Yet the CVMQ decision clearly casts doubt on the integrity of both Mr. B and Mr. C, two individuals who were very closely involved in the Cierra and Prospector investments, being shareholders and directors of company D:

(i) At the time client A began investing in the Cierra offering, and up until October 17, 2003, Mr. B was associated with Mr. C with whom he owned and operated company D;

(ii) At the time client A began investing in the Cierra offering, and up until October 17, 2003, company D was registered as a full service dealer with the CVMQ, with Mr. B designated as the President and Officer in charge of administration, and Mr. C, as the Chairman of the Board of Directors. Mr. B and Mr. C were also registered with the CVMQ as representatives with unrestricted practice;

(iii) Services financiers Internat Inc. (SFI) was designated as the agency authorized to act on behalf of Cierra on Canadian territory. Mr. C was designated as the first shareholder and sole member of SFI's board of directors;

(iv) The Respondent facilitated client A's investments in the Cierra offering based on the information transmitted by Mr. B;

(v) In 2006, the Respondent attended an information meeting organized by Mr. B. This presentation was specifically directed at Cierra company investors and was intended to introduce them to the Prospector offering. It was following this information meeting that the Respondent facilitated client A's investment in the Prospector offering;

(vi) Réseau, the Canadian corporation acting on an agency basis for Prospector with investors on Canadian territory, is a company whose majority

shareholder is a Barbados-based company for which Mr. B is designated as the President and Secretary;

(vii) There is therefore a close professional relationship between the following persons:

a. Mr. B, Mr. C. and Company D;
b. SFI (Cierra) and Mr. C;
c. Réseau (Prospector) and Mr. B.

12. By deciding not to inform his client A of the existence of this decision, the Respondent failed in his duty of diligence;

13. He deprived client A of essential information that would have allowed the latter to make an informed decision regarding the choice to invest or not in the Cierra and Prospector offerings;

14. Client A lost all of the investments made in the Cierra and Prospector offerings. This loss totals approximately $244,866;

15. In addition to losing the full amount of his investments in the Cierra and Prospector offerings, client A received notices of assessment from Revenu Québec and the Canada Revenue Agency. Indeed, the tax deductions claimed in connection with these investments were declared ineligible for tax deduction purposes by these two government authorities;

16. On September 29, 2009, the Canada Revenue Agency laid an information with the Court of Québec in order to obtain a search warrant. This search warrant was part of an investigation process intended to determine whether Mr. B voluntarily avoided the payment of taxes by helping taxpayers invest in financial products such as Prospector. In support of this warrant, the investigator argued notably that the decision rendered by the CVMQ was reasonable grounds for issuing the search warrant;

17. From reading this information, we learn not only that the decision rendered by the CVMQ constitutes material information, but that it also confirms the existence of a potential conflict of interest between Mr. B and Réseau. Finally, it exposes the fact that the Prospector offering was first and foremost an illegal tax evasion scheme;

OFF-BOOK INVESTMENTS

Cierra Offering

18. The Respondent and client A met in an informal setting, since they live in the same residential neighborhood. Also, their professional offices are located in neighboring buildings which multiplied the opportunities to meet;

19. The Respondent learned from client A that the latter had a high taxable income and wanted to invest in financial products that would save him money on taxes;

20. It was in this context that the Respondent informed his client of the existence of tax-deductible investments such as the products of DPI limited partnership;

21. The Respondent was himself informed of the existence of this investment at a presentation given by Mr. B in the MCA offices;

22. On or about February 16, 2000, client A formally retained the professional services of the Respondent to manage his brokerage accounts. At the time, the Respondent was employed with MCA;

23. In the course of 2002, the Respondent discussed with client A the possibility of investing in the Cierra offering, another product that would allow him tax savings;

24. On or about August 22, 2002, client A signed an agreement with the Cierra company;

25. On or about January 6, 2003, the Respondent left MCA to go work for RJ. Consequently, on or about January 9, 2003, client A signed new account application forms, so that all of the brokerage accounts held at MCA were transferred to RJ. The following accounts were thus opened in client A's name:

    (i) 6F3-520A-0 (Canadian cash account);
    (ii) 6F3-520B-0 (U.S. cash account);
    (iii) 6F3-520R-0 (RRSP account);
    (iv) 6F3-520Z-0 (RESP account).

26. The Respondent also facilitated the investment in the Cierra offering for client A's spouse, who was not an RJ client. All of this was done without the knowledge of RJ;

27. Between October 2002 and December 2004, client A personally remitted to the Respondent several cheques made out to SFI for investments in the Cierra company. The approximate total amount of client A's investments in the Cierra company is $115,000. For her part, client A's spouse allegedly invested approximately $14,000.

28. At no time did the investments in the Cierra offering appear on client A's account statements or on RJ's books;

Prospector Offering

29. Because the investments in the Cierra offering did not generate the anticipated profits, the Respondent informed client A of the possibility of investing in another offering by the name of Prospector;

30. Between December 2004 and June 2007, client A invested an approximate total amount of $129,866 in the Prospector offering;

31. At no time did the investments in the Prospector offering made by client A appear on his account statements or on the books at RJ;

32. On October 22, 2008, client A sent a written complaint to the Respondent and to RJ in which he emphasized, notably, the Respondent's misconduct in the management of his accounts and the fact that this failing caused him substantial financial losses.

GENERAL PROCEDURAL MATTERS

TAKE FURTHER NOTICE that the hearing and related proceedings shall be subject to IIROC's Rules of Practice and Procedure.

TAKE FURTHER NOTICE that, pursuant to Rule 13.1 of the Rules of Practice and Procedure, the Respondent is entitled to attend and be heard, be represented by counsel or an agent, call, examine and cross-examine witnesses, and make submissions to the Hearing Panel at the hearing.

RESPONSE TO NOTICE OF HEARING

TAKE FURTHER NOTICE that the Respondent must serve upon the Staff of IIROC a Response to the Notice of Hearing in accordance with Rule 7 of the Rules of Practice and Procedure, within twenty (20) days (for a Standard Track disciplinary proceeding) or within thirty (30) days (for a Complex Track disciplinary proceeding) from the effective date of service of the Notice of Hearing.

FAILURE TO RESPOND OR ATTEND HEARING

TAKE FURTHER NOTICE that, if the Respondent fails to serve a Response or attend the hearing, the Hearing Panel may, pursuant to Rules 7.2 and 13.5 of the Rules of Practice and Procedure:

(a) proceed with the hearing as set out in the Notice of Hearing, without further notice to the Respondent;

(b) accept as proven the facts and contraventions alleged by the Staff in the Notice of Hearing; and

(c) order penalties and costs against the Respondent pursuant to Dealer Member Rule 20.33, 20.34 and 20.49.

PENALTIES & COSTS

TAKE FURTHER NOTICE that, if the Hearing Panel concludes that the Respondent did commit any or all of the contraventions alleged by IIROC Staff in the Notice of Hearing, the Hearing Panel may, pursuant to Dealer Member Rule 20.33 and 20.34, impose any one or more of the following penalties:

Where the Respondent is/was an Approved Person:

(a) a reprimand;

(b) a fine not exceeding the greater of:

(i) 1,000,000 $ per contravention; and

(ii) an amount equal to three times the profit made or loss avoided by such Approved Person by reason of the contravention.

(c) suspension of approval for any period of time and upon any conditions or terms;

(d) terms and conditions of continued approval;

(e) prohibition of approval in any capacity for any period of time;

(f) termination of the rights and privileges of approval;

(g) revocation of approval;

(h) a permanent bar from approval with IIROC;

(i) any other fit remedy or penalty.

Where the Respondent is/was a Member firm:

(a) a reprimand;

(b) a fine not exceeding the greater of:

(i) 5,000,000 $ per contravention; and

(ii) an amount equal to three times the profit made or loss avoided by the Member by reason of the contravention;

(c) suspension of the rights and privileges of the Member (and such suspension may include a direction to the Member to cease dealing with the public) for any period of time and under any conditions or terms;

(d) terms and conditions of continued Membership;

(e) termination of the rights and privileges of Membership;

(f) expulsion of the Member from membership in the IIROC;

(g) any other fit remedy or penalty.

TAKE FURTHER NOTICE that if the Hearing Panel concludes that the Respondent did commit any or all of the contraventions alleged by the Association in the Notice of Hearing, the Hearing Panel may, pursuant to Dealer Member Rule 20.49, assess and order any investigation and prosecution costs determined to be appropriate and reasonable in the circumstances.

DATED at Montréal, this 3rd day of February 2012

(s) Carmen Crépin

Carmen Crépin
Vice-President – Québec

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