

# INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA

IN THE MATTER OF:

**THE RULES OF THE INVESTMENT INDUSTRY REGULATORY  
ORGANIZATION OF CANADA (IIROC)**

AND

**THE BY-LAWS OF THE  
INVESTMENT DEALERS ASSOCIATION OF CANADA (IDA)**

AND

*DAVID WILSON MURDOCH*

## SETTLEMENT AGREEMENT

### I. INTRODUCTION

1. IIROC Enforcement Staff and the Respondent, David Wilson Murdoch, consent and agree to the settlement of this matter by way of this settlement agreement (“the Settlement Agreement”).
2. The Enforcement Department of IIROC has conducted an investigation (“the Investigation”) into the conduct of Mr. Murdoch.
3. On June 1, 2008, IIROC consolidated the regulatory and enforcement functions of the Investment Dealers Association of Canada and Market Regulation Services Inc. Pursuant to the Administrative and Regulatory Services Agreement between IDA and IIROC, effective June 1, 2008, the IDA has retained IIROC to provide services for IDA to carry out its regulatory functions.
4. The Respondent consents to be subject to the jurisdiction of IIROC.
5. The Investigation discloses matters for which the Respondent may be disciplined by a hearing panel appointed pursuant to IIROC Transitional Rule No.1, Schedule C.1, Part C (“the Hearing Panel”).

## **II. JOINT SETTLEMENT RECOMMENDATION**

6. Staff and the Respondent jointly recommend that the Hearing Panel accept this Settlement Agreement.
7. The Respondent admits to the following contravention of IIROC Rules, Guidelines, IDA By-Laws, Regulations or Policies:

From August 2005 to February 2008, the Respondent, as Branch Manager, failed to adequately supervise an RR, David Kenneth Smith, and the accounts of LS, contrary to IDA Regulation 1300.2 and Policy No. 2.
8. Staff and the Respondent agrees to the following terms of settlement:
  - a) A suspension of registration approval for 12 months as Branch Manager or from acting in any supervisory capacity; and
  - b) A fine in the sum of \$50,000.
9. The Respondent agrees to pay costs to IIROC in the sum of \$3,500.

## **III. STATEMENT OF FACTS**

### **(i) Acknowledgment**

10. Staff and the Respondent agree with the facts set out in this Section III and acknowledge that the terms of the settlement contained in this Settlement Agreement are based upon those specific facts.

### **(ii) Overview**

11. The Respondent, as Branch Manager, failed to take reasonable and adequate steps to supervise a Registered Respondent (RR) and his handling of certain client accounts. The Branch Manager failed to adequately question the RR with respect to:
  - a) Changes to the investment objectives for the accounts and the reasons for those changes;
  - b) High amounts of commissions earned on the accounts;
  - c) Excessive trading in the accounts; and
  - d) Discretionary trading in the accounts.
12. Furthermore, the Branch Manager ought to have confirmed with the client that she was in agreement with and understood the activities undertaken in her account.

### **(iii) Factual Background**

13. During the material time, the Respondent was ~~(and still is)~~ the Branch Manager for the Vancouver office of Northern Securities Inc. (NSI). As Branch Manager, he is also responsible for supervising the firm's sub-branches in British Columbia, including Kelowna.
14. As such, the Respondent was responsible for the supervision of David Kenneth Smith, a Registered Representative in the Kelowna branch.
15. In August 2005, Smith joined NSI. Shortly thereafter, LS, who had been a client of Smith at his previous firm, opened two accounts at NSI.
16. At the time of the account opening, LS was 75 years old and retired. LS is also Smith's mother-in-law.
17. LS opened a Canadian margin account and a RRIF account. Her New Client Account Form indicated the following Investment Objectives and Risk Tolerance for both accounts:
  - 60% - moderate to higher-risk income producing securities;
  - 15% - moderate risk, growth-oriented securities;
  - 25% - higher-risk, speculative securities and trading strategies
18. LS' approximate annual income was listed at \$90,000 and her Net Liquid Assets at \$1.9 million. The total equity balance in LS' accounts at NSI at the time of the account opening represented over 90% of her Net Liquid Assets.

*Changes to Investment Objectives*

19. Beginning in January 2006, the investment objectives of LS' accounts were changed a number of times. The first change took place only 5 months after the account was opened, and increased the risk tolerance to the following:
  - 50% - moderate to higher-risk income producing securities;
  - 10% - moderate risk, growth-oriented securities;
  - 40% - higher-risk, speculative securities and trading strategies
20. The Respondent spoke to Smith about the changes in or around January 2006, and Smith advised him that the client wanted to do more speculative trading. The Respondent was satisfied with this response, despite the age and financial circumstances of the client and the fact that the objectives were changing only 5 months after the account was opened.

21. The investment objectives were again changed in November 2006, this time following an inquiry from NSI Head Office Compliance, advising Smith that the client holdings did not match the stated investment objectives. In response, Smith submitted an updated NCAF and increased the risk tolerance to the following:

50% - moderate to higher-risk income producing securities;  
50% - higher-risk, speculative securities and trading strategies

22. Again, in March 2007, NSI Head Office Compliance queried the holdings in the account, and Smith responded with the following changes to Investment Objectives:

51% - moderate to higher-risk income producing securities;  
49% - higher-risk, speculative securities and trading strategies

23. Although he was aware of this “update” to the NCAF, the Respondent did not raise any concerns with Smith.

24. In October 2007, Head Office Compliance again queried the account, raising concerns about the investments in high-risk securities. Despite this query, the Respondent did not raise any concerns himself with Smith, and did not contact the client.

25. In response to the queries from Compliance, Smith advised that the client had changed her investment objectives for the account and that updated account documents would be provided in the next few weeks. The investment objectives were not changed until February 2008, to the following:

25% - moderate to higher-risk income producing securities;  
75% - higher-risk, speculative securities and trading strategies

26. By this time, the equity value of LS’ accounts had declined significantly.

27. Despite the fact that this was the third time that the account objectives changed only after queries from Compliance, and the major decline in the value of the accounts, the Respondent did not have any issues with the increase in the risk tolerance levels in the accounts and did not speak to Smith or the client about this increase.

#### *High Commissions and Excessive Trading*

28. During the relevant period, the LS accounts on average generated approximately \$15,000 in commission per month. In September 2005 the commissions reached \$49,000 and in 5 different months the commission was over 90% of Smith’s total commission for each of those months.

29. The Respondent did not express any concern or make any inquiries of the Respondent or LS relating to the high level of commission.

*Discretionary Trading*

30. The LS accounts were averaging more than 66 trades a month. This would have necessitated a considerable amount of contact between Smith and LS in order to obtain authorization for those trades. The Respondent believed Smith was directing the activity in the account, despite the fact that the account was not set up as a discretionary account.
31. The Respondent relied on a letter written by Smith's previous firm to LS. The letter confirmed that the firm had spoken with LS and was satisfied that she was fully aware of all of the trades in her account. However, the Respondent failed to consider that the letter was three years old, and that in the same letter the previous firm advised that it would continue to closely monitor the trading in the account, despite LS' assurances.

*Head Office Compliance Queries*

32. As described above, Smith was contacted on several occasions by Head Office Compliance regarding the activity in the LS accounts. The Respondent was aware of many of these queries, although on one occasion he was not copied on correspondence between Head Office Compliance and Smith.
33. The Respondent was of the view that since Compliance was dealing with an issue, he was no longer responsible for that particular issue. This view is contrary to the obligations imposed upon him by Regulation 1300.2 and Policy No. 2.

*Queries Raised by the Respondent*

34. On three or four occasions the Respondent did query Smith with respect to the level of trading activity in the account shortly after the account was opened. He was satisfied with Smith's assertion that LS wanted to do such trading.
35. Although the Respondent spoke to Smith on these occasions, he maintained no record of these discussions or queries.
36. The Respondent failed to:
  - a) make direct inquiries of the RR regarding:
    - i. why the trading was increasing in volume and risk;
    - ii. why the investment objectives in the accounts were changing only after queries from Compliance and so soon after the accounts were opened;
    - iii. why the client was willing to continue to incur major losses in the account;
    - iv. why the accounts were generating such large commissions; and
    - v. whether the client was authorizing each and every trade in the account and whether such authorizations were being documented.
  - b) make direct inquiries of the client regarding her awareness of and comfort with the activities of the RR and the activity in her account;

- c) closely monitor the trading in the account on a daily and monthly basis; and
- d) maintain evidence of those inquiries and his monitoring.

#### *LS Client Complaint*

- 37. By letter dated February 28, 2008, a lawyer for LS advised NSI that Smith had made numerous unauthorized and unsuitable trades in LS' accounts, and that LS had suffered a considerable loss as a result. The letter was dated two weeks after LS signed the last NCAF updating her objectives.
- 38. NSI has settled with LS with respect to her complaint and reimbursed her for her losses.

#### **IV. TERMS OF SETTLEMENT**

- 39. This settlement is agreed upon in accordance with IIROC Dealer Member Rules 20.35 to 20.40, inclusive and Rule 15 of the Dealer Member Rules of Practice and Procedure.
- 40. The Settlement Agreement is subject to acceptance by the Hearing Panel.
- 41. The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.
- 42. The Settlement Agreement will be presented to the Hearing Panel at a hearing ("the Settlement Hearing") for approval. Following the conclusion of the Settlement Hearing, the Hearing Panel may either accept or reject the Settlement Agreement.
- 43. If the Hearing Panel accepts the Settlement Agreement, the Respondent waives his/her/its right under IIROC rules and any applicable legislation to a disciplinary hearing, review or appeal.
- 44. 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 matters disclosed in the Investigation.
- 45. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel.
- 46. Staff and the Respondent agree that if the Hearing Panel accepts the Settlement Agreement, they, or anyone on their behalf, will not make any public statements inconsistent with the Settlement Agreement.
- 47. Unless otherwise stated, any monetary penalties and costs imposed upon the Respondent are payable immediately upon the effective date of the Settlement Agreement.

48. Unless otherwise stated, any suspensions, bars, expulsions, restrictions or other terms of the Settlement Agreement shall commence on the effective date of the Settlement Agreement.

**AGREED TO** by the Respondent at the City of "Vancouver" \_\_\_\_\_ in the Province of  
\_\_BC\_\_\_\_\_, this \_\_28th\_\_\_\_ day of \_\_February\_\_\_\_, 2012\_\_\_\_\_.

\_\_\_\_\_  
"Witness  
**WITNESS**

\_\_\_\_\_  
"David Murdoch\_\_\_\_\_  
**RESPONDENT**

**AGREED TO** by Staff at the City of \_\_Toronto\_\_\_\_\_ in the Province of Ontario\_\_,  
this \_\_1st\_\_\_\_ day of \_\_March\_\_\_\_, 2012\_\_\_\_\_.

\_\_\_\_\_  
Witness  
**WITNESS**

\_\_\_\_\_  
Diana Iannetta\_\_\_\_\_  
**DIANA IANNETTA**  
Senior Enforcement Counsel on  
behalf of Staff of the Investment  
Industry Regulatory Organization of  
Canada

**ACCEPTED** at the City of \_\_Vancouver\_\_\_\_\_ in the Province of \_\_\_\_\_BC\_\_\_\_\_,  
this \_\_20th\_\_\_\_ day of \_\_March\_\_\_\_, 2012\_\_\_\_, by the following Hearing Panel:

Per: Ms. Linda Murray\_\_\_\_\_  
Panel Chair

Per: Mr. Chris Lay\_\_\_\_\_  
Panel Member

Per: Mr. Brian Field\_\_\_\_\_  
Panel Member