

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

DUNDEE SECURITIES CORPORATION

SETTLEMENT AGREEMENT

I. INTRODUCTION

1. IIROC Enforcement Staff and the Respondent, Dundee Securities Corporation, 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 Dundee Securities Corporation.
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 contraventions of IIROC Dealer Member Rules, Guidelines, IDA By-Laws, Regulations or Policies:
 - a) Between approximately May, 2006 and April, 2008, the Respondent failed to effectively exercise its supervisory responsibilities concerning the management of the accounts of clients, RH and JH, contrary to IDA By-Law 1300.2(a) (now known as IIROC Dealer Member Rule 1300.2(a)) and Policy No. 2 (now known as IIROC Dealer Member Rule 2500);
 - b) Between approximately August, 2007 and April, 2008, the Respondent failed to effectively exercise its supervisory responsibilities concerning the management of the accounts of clients, JR and ER, contrary to IDA By-Law 1300.2(a) (now known as IIROC Dealer Member Rule 1300.2(a)) and Policy No. 2 (now known as IIROC Dealer Member Rule 2500).
8. Staff and the Respondent agrees to the following terms of settlement:
 - a) The Respondent shall pay a fine to IIROC in the sum of \$110,000.00.
9. The Respondent agrees to pay costs to IIROC in the sum of \$10,000.00.

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) Factual Background

11. Clients RH/JH, and JR/ER, were both senior, retired couples and not sophisticated investors. RH/JH and JR/ER were clients of Kenneth Gareau, a Registered Representative in a sub-branch office of the Respondent, Dundee Securities Corporation ("Dundee") (as it was then named) located in Regina, Saskatchewan.
12. JR/ER's accounts contained investment objectives and risk tolerance parameters which were not accurate in light of their age, investment knowledge, employment status and financial situation. With respect to both RH/JH, and JR/ER, their holdings were not suitable for their circumstances.

13. Between approximately May, 2006 and April, 2008, Dundee was performing Tier 1 supervisory functions of Gareau through its compliance officers at its head office in Toronto.
14. Dundee failed in its supervisory duties as its compliance officers approved the account forms for JR/ER with objectives that were too risky, and failed to make inquiries into the suitability of trades in the accounts of JR/ER and RH/JH.

Respondent

15. At all material times, the Respondent was a duly registered member firm of the IDA and its successor, IIROC.

Registered Representative

16. Kenneth Gareau was a Registered Representative with Dundee in a sub-branch office in Regina, Saskatchewan.
17. On September 26, 2011, following a disciplinary hearing, an IIROC Hearing Panel found that Gareau had acted contrary to Dealer Member Rule 29.1 because he had failed to accurately record risk tolerance and investment objectives on new client account forms (“NCAFs”) for clients RH/JH and JR/ER, and that he had acted contrary to Dealer Member Rule 1300.1(q) because he had made unsuitable recommendations for clients RH/JH and JR/ER. In addition, the Hearing Panel found that he had acted contrary to IDA By-Law 29.1 because he conducted a transaction against the expressed wishes of JR/ER.
18. The Panel, finding that Gareau had failed to accurately record risk tolerance and investment objectives on NCAFs for clients RH/JH relates to a time period which is outside the relevant supervision period of May, 2006 to April, 2008 (“Relevant Period”).

Supervision

19. During the Relevant Period, Gareau was the Branch Manager of his sub-branch. He was supervised by compliance officers located at the Respondent’s head office in Toronto, who were acting in a Tier 1 capacity during the Relevant Period. In or about May, 2008, a new local Branch Manager in Saskatchewan was appointed as a Tier 1 supervisor over Gareau.
20. In order to conduct Tier 1 supervision, the Respondent’s compliance officers were required to review and approve NCAFs and client account updates, as well as review daily and monthly trading summary reports.

Clients RH/JH

21. Clients RH/JH, born in 1942 and 1946, are a retired couple and were not sophisticated investors.
22. In or about May, 2006, after a lifetime of farming, RH/JH sold their farm and equipment and retired with slightly more than \$1 million from that sale. They planned to use approximately \$225,000 of that money to build a new house in Fort Qu'appelle, Saskatchewan to live in and invest the remaining funds in low risk investments to augment retirement payments they would receive from the Canada Pension Plan ("CPP") and the Old Age Security Program ("OAS").

New Accounts

23. In May, 2006 they met Gareau and opened a new account. The NCAF for this account states that the couple had an income of \$40,000, "good" investment knowledge and investment objectives of 100% capital appreciation, and risk tolerance of 100% medium.
24. At that time, RH/JH did not have a significant source of income apart from approximately \$7,000 per year from CPP. They had minimal investment knowledge, and their primary investment objective was preservation of capital with low risk tolerance. They intended to rely on their investments for income.
25. In July, 2006 additional new investment accounts were opened — a joint margin account; a corporate margin account; and individual RRSP accounts (together the "Investment Accounts"). The Investment Accounts all contained similar investment objective and risk tolerance parameters, as well as income information.
26. The Respondent, acting through head office compliance officers in a Tier 1 supervisory capacity, approved the NCAFs for the Investment Accounts, including the use of margin, without any documented questions or queries.
27. After the Investment Accounts were opened, RH/JH deposited funds or transferred securities into the accounts in the total amount of approximately \$1,215,000.

Recommendations

28. Between approximately July, 2006 and May, 2008 through a number of large transactions, Gareau recommended RH/JH purchase the following (approximate amounts) in the Investment Accounts:
 - (a) Equity based mutual funds \$1,266,000;
 - (b) Limited Partnership Units \$ 170,000;
 - (c) Hedge Fund \$ 100,000;

(d)	Dundee REIT; Dundee Wealth Inc.	<u>\$ 58,000</u>
	Total	\$1,594,000

Use of Margin

29. There was extensive use of margin in certain of the Investment Accounts.
30. In September, 2006, Gareau recommended RH/JH borrow \$120,000 on margin from the corporate margin account to make the first annual payment on a universal life insurance policy which he arranged to be sold to them.
31. In September, 2006 RH/JH borrowed \$140,000 on margin in order to purchase the Limited Partnership Units (see paragraph 28 above).
32. By the end of September, 2006 RH/JH had accumulated margin debt of \$220,000.
33. In October, 2007 Gareau recommended that RH/JH establish a Home Equity Line of Credit and borrow \$200,000 against the value of their newly acquired home which had been paid for with proceeds from the sale of their farm. There were no other mortgages against the home, which was valued at approximately \$225,000.
34. The \$200,000 was used to purchase equity mutual fund investments as described in paragraph 28.
35. By May, 2008, RH/JH had accumulated total margin debt of approximately \$552,000 and were being charged \$2,349 per month on that margin debt. Additionally, they owed \$200,000 on the Home Equity Line of Credit.

Withdrawals

36. Because they had no other significant source of income, RH/JH withdrew amounts ranging from \$4,900 - \$6,100 on a monthly basis from their investment accounts for regular living expenses. But, the investments in their accounts were not income producing investments that were intended to produce the type of regular monthly income RH/JH required from their accounts. To obtain available funds to withdraw, Gareau sold portions of the existing equity mutual funds each month.

Losses

37. In October, 2008, after almost all equity markets around the world had dropped significantly, Gareau switched RH/JH's equity mutual funds into money market funds.
38. From the beginning of August, 2006 to the end of November, 2008, RH/JH's net investment in the Investment Accounts was approximately \$1,046,350. Over that 28 month period they incurred realized and unrealized losses of approximately \$629,750 or

approximately 60.2% of their net investment, when during the same period, the TSX Composite Index decreased approximately 21.6%.

39. The losses in RH/JH's accounts were significantly increased because of the extensive use of margin debt in their accounts.

Suitability

40. The recommended purchases in the Investment Accounts, which were essentially entirely equity based, were not suitable for these clients who relied on their investments for income.
41. In addition, the extensive use of margin in the Investment Accounts was not suitable for these clients who were retired and relying on their investments for income.

Clients – JR/ER

42. JR, born in 1936, and ER, born in 1939 are a married couple with minimal investment knowledge. They retired in 2003, after a lifetime of farming.
43. In August, 2007 they opened a joint investment account and individual RRIF accounts. Their NCAFs state that their investment knowledge was "good", and their investment objectives were 100% growth and risk tolerance 100% medium. Their stated annual income was \$15,000.
44. Their assets consisted of their home, as well as securities totaling approximately \$198,500. These securities were mostly comprised of low risk interest and dividend paying securities. They also held some shares in Canadian banks, and balanced mutual funds.
45. At that time, their only income consisted of monthly CPP/OAS payments of approximately \$1,550. They had minimal investment knowledge, and their primary investment objective was preservation of capital with low risk tolerance. They intended to rely on their investments for income.

Recommendations

46. After JR/ER's existing securities were transferred in to their respective accounts in or about September, 2007, Gareau sold them. With the proceeds, between October and November, 2007, he recommended that they purchase approximately \$197,000 in equity based mutual funds

Suitability

47. In effect, nearly all of the couple's liquid assets were held in equities. These holdings were not suitable for JR/ER given their age, employment status, investment knowledge and financial situation.

48. In all of their communications with Gareau, including a hand written letter dated March 7, 2008, JR/ER clearly communicated that they could not tolerate any losses in their investment accounts.
49. JR/ER were relying on regular income from their investments to supplement their CPP and OAS payments. In their joint account at the previous registered firm they held \$51,000 par value of a Bell Canada bond which was paying 5% or \$2,550 per year. Against JR/ER's express wishes, Gareau sold this existing security to buy unsuitable securities which paid Gareau more than \$2,000 in commission.
50. All of the mutual funds purchased in JR/ER's accounts were purchased subject to deferred service charges ("DSC").
51. Such extensive use of DSC mutual funds in JR/ER's accounts was not suitable for them given their age and the fact that they needed to withdraw money from their accounts to fund their retirement.
52. In October, 2008, after almost all equity markets around the world had dropped significantly, Gareau switched JR/ER's equity mutual funds into money market funds.
53. From September, 2007 to February, 2009 JR/ER's accounts incurred losses of approximately \$64,000 or 36% of their combined portfolio. During this time, the S&P/TSX Composite Index declined approximately 41%.

Supervisory Failures

54. During the Relevant Period, Tier 1 supervision of Gareau was being conducted by compliance officers at Dundee Head office in Toronto.
55. These supervisors had certain duties and responsibilities, including the supervision of Gareau, the approval of new account applications/updates, and the supervision of account activity.
56. There were numerous red flags with respect to the accounts of RH/JH and JR/ER (together the "Clients") for which the supervisors failed to take any meaningful action to investigate. These red flags included the following:
 - (a) the Clients were retired;
 - (b) the Clients' investment objectives and risk tolerance parameters were very high;
 - (c) the Clients were holding virtually all equities, and despite their age and circumstances there were virtually no fixed income holdings; and
 - (d) with respect to RH/JH, there was a very high use of margin.

57. Despite the presence of these red flags, the supervisors:
- (a) Failed to use due diligence to ensure that the Clients' stated investment objectives and risk tolerances were consistent with their true financial situation, investment knowledge, investment objectives and risk tolerances;
 - (b) Failed to question the trading activity in the accounts and whether the trades and holdings were suitable for the Clients;
 - (c) Failed to make inquiries into the suitability of the extensive use of margin by RH/JH; and
 - (d) Failed to give due regard to the risks to the Clients, and allowed Gareau to pursue a highly aggressive strategy which was not suitable for the Clients and ultimately resulted in substantial realized and unrealized losses when the market declined.
58. In failing to adequately question the account activity in light of these red flags, the Respondent's supervisors failed to effectively perform its supervisory responsibilities.

Mitigating Factor

59. RH/JH received compensation for their losses of approximately \$500,000, which included a \$75,000 contribution from the Respondent. JR/ER received compensation for their losses of \$6,477.62.
60. The Respondent at all times co-operated with IIROC Staff during the investigation.

IV. TERMS OF SETTLEMENT

61. 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.
62. The Settlement Agreement is subject to acceptance by the Hearing Panel.
63. The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.
64. 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.
65. 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.

66. 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.
67. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel.
68. 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.
69. Unless otherwise stated, any monetary penalties and costs imposed upon the Respondent are payable immediately upon the effective date of the Settlement Agreement.
70. 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 “Toronto” in the Province of “Ontario”,
this 4th day of December, 2013.

“Witness”
WITNESS

“Moira Simo”
RESPONDENT

Per: “Moira Simo”

AGREED TO by Staff at the City of “Toronto” in the Province of “Ontario”,
this 4th day of December, 2013.

“Witness”
WITNESS

“David McLellan”
DAVID MCLELLAN
Enforcement Counsel on behalf of
Staff of the Investment Industry
Regulatory Organization of Canada

ACCEPTED at the City of “Toronto” in the Province of “Ontario”,
this “4th” day of “December”, 2013, by the following Hearing Panel:

Per: “Edward McDermott”
Panel Chair

Per: “Robert Guilday”
Panel Member

Per: “Michael Walsh”
Panel Member