Regulating Canada’s Securities Market: An Examination of the Investment Dealers Association’s Enforcement Practices from 1984 to June 2008

by

Mark E. Lokanan

M.A. (Criminal Justice), San Diego State University, 2004
B.A., York University, 1998

Dissertation Submitted in Partial Fulfillment of the Requirements for the Degree of Doctor of Philosophy

in the
School of Criminology
Faculty of Arts and Social Sciences

© Mark Eshwar Lokanan 2012

SIMON FRASER UNIVERSITY

Summer 2012

All rights reserved.
However, in accordance with the Copyright Act of Canada, this work may be reproduced, without authorization, under the conditions for “Fair Dealing.” Therefore, limited reproduction of this work for the purposes of private study, research, criticism, review and news reporting is likely to be in accordance with the law, particularly if cited appropriately.
Approval

Name: Mark Eshwar Lokanan
Degree: Doctor of Philosophy
Title of Thesis: Regulating Canada’s Securities Market: An Examination of the Investment Dealers Association’s Enforcement Practices from 1984 to June 2008

Examinig Committee:
Chair: Margaret Jackson, Professor

Joan Brockman
Senior Supervisor
Professor, School of Criminology

Bill Glackman
Supervisor
Associate Professor, School of Criminology

Neil Boyd
Supervisor
Professor, School of Criminology

Wendy Chan
Internal Examiner
Professor
Simon Fraser University/Department of Sociology and Anthropology

Cristie Ford
External Examiner
Assistant Professor, University of British Columbia, Faculty of Law

Date Defended/Approved: June 15, 2012
Partial Copyright Licence

The author, whose copyright is declared on the title page of this work, has granted to Simon Fraser University the right to lend this thesis, project or extended essay to users of the Simon Fraser University Library, and to make partial or single copies only for such users or in response to a request from the library of any other university, or other educational institution, on its own behalf or for one of its users.

The author has further granted permission to Simon Fraser University to keep or make a digital copy for use in its circulating collection (currently available to the public at the “Institutional Repository” link of the SFU Library website (www.lib.sfu.ca) at http://summit/sfu.ca and, without changing the content, to translate the thesis/project or extended essays, if technically possible, to any medium or format for the purpose of preservation of the digital work.

The author has further agreed that permission for multiple copying of this work for scholarly purposes may be granted by either the author or the Dean of Graduate Studies.

It is understood that copying or publication of this work for financial gain shall not be allowed without the author’s written permission.

Permission for public performance, or limited permission for private scholarly use, of any multimedia materials forming part of this work, may have been granted by the author. This information may be found on the separately catalogued multimedia material and in the signed Partial Copyright Licence.

While licensing SFU to permit the above uses, the author retains copyright in the thesis, project or extended essays, including the right to change the work for subsequent purposes, including editing and publishing the work in whole or in part, and licensing other parties, as the author may desire.

The original Partial Copyright Licence attesting to these terms, and signed by this author, may be found in the original bound copy of this work, retained in the Simon Fraser University Archive.

Simon Fraser University Library
Burnaby, British Columbia, Canada

revised Fall 2011
Abstract

Every year, thousands of Canadians fall prey to investment fraud. Estimates for 2007 indicate that roughly one-in-twenty Canadians are victims of investment fraud at some point in their lives. Given the frequency of investment fraud in Canada, it is not surprising that losses to Canadians amount to billions of dollars as well as other harmful personal consequences. Financial and personal losses, along with diminishing public confidence in capital markets, led to calls for stricter enforcement. This dissertation examines the enforcement practices of the Investment Dealers Association of Canada (IDA), the national self-regulatory organization responsible for policing investment dealers and Member firms that trade in the debt and equity markets. Data from 1984-2008 were collected from three sources – the IDA Enforcement and Annual Reports, the IDA’s tribunal cases, and appeal cases of the IDA’s decisions to the Alberta, British Columbia, and Ontario securities commissions. The findings from the study show that while the IDA processed a significant number of complaints in the case assessment stage, the number shrank considerably as the complaints made their way through to the investigation and internal prosecution stages of the disciplinary system. The top two offences dealt with by formal disciplinary proceedings were unsuitable investment and inappropriate discretionary trading. The majority of investors had limited investment knowledge, and many were encouraged to borrow money to invest. Results also show that the IDA’s by-law enforcement was often inadequate and did not send a sufficiently strong deterrent message to market participants. The majority of cases were disposed of via settlement agreements rather than hearings, and the fines imposed were often not proportionate to the offence(s). Between 2002 and 2007, the IDA collected less than 50% of the fines it levied. Harsher fines were imposed by hearing panels that were chaired by a public member. When determining penalties, more weight was given to mitigating rather than aggravating factors. Regulatory reforms should focus on greater transparency, stricter enforcement, and more attention to aggravating factors when assigning penalties. Fraud awareness programs should not be a one size fits all approach and must be tailored to different subsets of investors.

Keywords: Investment fraud; self-regulation; misconduct funnel; enforcement; quasi-criminal offences; aggravating and mitigating factors
Dedication

To all of the individuals who have been victims of investment fraud
Acknowledgements

I would like to thank my dissertation committee for guiding me through to the successful completion of this dissertation. No words can express my gratitude for the support that I received from my senior supervisor, Professor Joan Brockman. I will just say thank you for your advice, support and for giving me the opportunity to grow both as a person and as a scholar. Your mentorship and encouragement throughout the years was an invaluable experience. In addition, I want to thank Professor Bill Glackman for his assistance and advice in simplifying the methodological section. Thanks also to Professor Neil Boyd for his continued support and feedback throughout the dissertation process. I am very grateful to Professor Cristie Ford for taking the time out of her schedule to serve as the external examiner and offering insightful comments on the final draft of my dissertation. Thanks also to Professor Wendy Chan for agreeing to serve as the internal examiner. I would also like to thank Dr. Sheri Fabian for her advice throughout and assistance in formatting my dissertation. Let me also say thank you to Dr. Barry Cartwright for his advice and encouragement over the years. To the entire Crim. 1000 crew, thank you very much for all your support and feedback.
# Table of Contents

 Approval ............................................................................................................................ ii  
 Partial Copyright Licence ................................................................................................. iii  
 Abstract ............................................................................................................................ iv  
 Dedication ........................................................................................................................... v  
 Acknowledgements ............................................................................................................... vi  
 Table of Contents .............................................................................................................. vii  
 List of Tables ...................................................................................................................... xi  
 List of Figures ..................................................................................................................... xiii  

## Chapter 1: Introduction ................................................................................................... 1  
 Financial Losses .................................................................................................................. 2  
 Personal Consequences ....................................................................................................... 3  
 Market Integrity ................................................................................................................... 4  
 Financial/securities regulation and the IDA ....................................................................... 5  
 Structure of the Dissertation ............................................................................................... 9  

## Chapter 2: Significance - The case for a Study on the IDA ........................................... 12  
 The Wider Context of Securities Regulation in Canada ...................................................... 12  
 Self-Regulation and the Market .......................................................................................... 19  

## Chapter 3: The Literature on Self-Regulation ................................................................. 21  
 Self-Regulation as a Concept ............................................................................................. 21  
 A Continuum of Self-Regulation ....................................................................................... 23  
 Global Trends in Securities Regulation ........................................................................... 26  
    Australia ......................................................................................................................... 27  
    Japan .............................................................................................................................. 29  
    Hong Kong .................................................................................................................... 31  
    Brazil ............................................................................................................................. 33  
    United Kingdom .......................................................................................................... 36  
    United States ............................................................................................................... 39  
    Canada .......................................................................................................................... 40  
 Arguments for Self-Regulation ......................................................................................... 43  
    Public Interest .............................................................................................................. 43  
    Industry Expertise ....................................................................................................... 43  
    Efficient Regulation ..................................................................................................... 44  
    Effective Compliance ................................................................................................. 45  
 Arguments against Self-Regulation .................................................................................. 45  
    Lenient Enforcement ................................................................................................. 45  
    Deflects Criminal Complaints away from the Justice System ................................... 46  
    Inability to Adapt to Changing Market Structure ...................................................... 47  
 SROs and Industry Regulation ........................................................................................... 47  
 SROs, Securities Commissions and Securities Regulation ............................................... 48  
 SROs, Criminal Justice System and Securities Regulation ............................................... 58
List of Tables

Table 6-1  Events Reported to ComSet................................................................. 95
Table 6-2  Subject Nature of ComSet Events Reported ........................................ 99
Table 6-3  Types and Percentage of Complaints (by Issue) Opened by the 
Case Assessment Group from January 01 – December 31 .......................... 100
Table 6-4  Top Four Complaints Received by the Case Assessment Group 
from 2002-2007 ............................................................................................... 103
Table 6-5  Total Files Opened and Closed by Case Assessment Group from 
2002-2007 ..................................................................................................... 104
Table 6-6  Total Files Opened and Closed by Investigation Unit from 2002-
2007 .................................................................................................................. 106
Table 6-7  Top Four Issues Referred to Investigation from 2003-2007 .............. 108
Table 6-8  Results of Cases that were Referred to Enforcement Counsel for 
Prosecution from 2002-2007 ...................................................................... 109
Table 6-9  Top Four Issues Referred to Prosecution from 2003-2007 by 
Hearing Panels ................................................................................................. 111
Table 6-10 Penalties Assessed on Individual Offenders by Hearing Panels ......... 112
Table 6-11 Penalties Assessed on Member Firms .................................................. 114
Table 6-12 IDA’s Fine Collection .......................................................................... 117
Table 7-1   Investors per Case in the IDA Study ....................................................... 122
Table 7-2   Age of Investors in the Three Studies ...................................................... 124
Table 7-3   Purpose of Investment in the IDA and Eron Studies ............................. 128
Table 7-4   Sources of Investment in the IDA and Eron Studies ............................ 129
Table 7-5   Annual Household Income of Investors in the Three Studies ............. 134
Table 7-6   Household Net Worth (Excluding principal residence) of Investors of 
the Three Studies ............................................................................................. 135
Table 7-7   Crosstabulation of Offenders’ Gender and Disciplinary History .......... 139
Table 7-8   Offenders’ Current Industry Status ...................................................... 140
Table 7-9   Occupation of Offenders ....................................................................... 143
Table 7-10 Types of Member Firms Involved in Enforcement Hearing ............... 148
Table 7-11 Number and Percentage of IIROC’s Regulated Integrated, Retail, 
and Institutional Member Firms ...................................................................... 149
Table 7-12 Disciplinary History of Member Firms ............................................... 150
Table 7-13 Type of Disciplinary Hearing for Individual Offenders and Member 
Firms .................................................................................................................. 151
Table 7-14 Table Showing the IDA’s Offence Categories ...................................... 155
Table 7-15 Number of Offences per Case................................................................. 156
Table 7-16 Offence Committed by Individual Offenders and Member Firms........... 158
Table 7-17 Individual offenders Disciplined for Quasi-criminal offences............... 161
Table 7-18 Total Fines, Costs, and Disgorgement and other Non-Monetary Penalties Imposed on Individual Offenders ....................................................... 163
Table 7-19 Penalties Imposed on Member Firms..................................................... 168
Table 8-1 Individual Registrants and Member Firms Appeals to the Securities Commissions ........................................................................................................ 173
Table 8-2 IDA and Victims Appeals to the Securities Commissions ...................... 174
List of Figures

Figure 7-1 Victims per Case........................................................................................................121
Figure 7-2 Investors’ Occupational Classification..............................................................125
Figure 7-3 Investors’ Investment Knowledge........................................................................127
Figure 7-4 Type of Accounts ..................................................................................................132
Figure 7-5 Investors’ Investment Objectives.........................................................................133
Figure 7-6 Investors’ financial losses ....................................................................................137
Figure 7-7 Investors’ Relationship to the Offender..............................................................139
Figure 7-8 Years of Offenders’ Work Experience in the Securities Industry.....................146
Figure 7-9 Number of Disciplinary Proceedings by District Councils ................................153
Figure 7-10 Average and Median Fines and Costs Imposed on Individual Offenders...........164
Figure 9-1 Aggravating Factors Considered and Aggravating Factors Identified, But Not Considered in the Imposition of Penalties ...................................................................184
Figure 9-2 Mitigating Factors Considered in the Imposition of Penalties ............................196
Chapter 1: Introduction

Meet Chris Morgis. In 2001, a Toronto real estate developer named Chris Morgis, "lost $2 million due to unauthorized trading by the now-defunct brokerage [firm named] Thomson Kernaghan & Co" (Hamilton, 2007a). Morgis “filed complaints with the Investment Dealer Association ("the IDA") in March 2001[,]…but the agency did not respond for more than a year” (Hamilton, 2007a). In 2002, Thomson Kernaghan & Co. went bankrupt and “its former Chair, Mark Valentine, was later found guilty of securities fraud in the United States (U.S.)” (Hamilton, 2007a). Morgis noted that dealing with Canadian regulators was a “disappointing process” (Hamilton, 2007a). Morgis contended that there “was smoke” and then “there was a fire, but the IDA did [not] go in” (Hamilton, 2007a). He charged that since Thomson Kernaghan & Co. was a member of the IDA, he was complaining to the very people that he had an issue with, and they were “reluctant” to put their members in a situation in which they could face criminal charges (MacNeil & Solomon, 2008).

Morgis’ case is just one example of the thousands of Canadians who are affected by investment fraud in Canada. In 2007, a study conducted by the Canadian Securities Administrators (CSA) noted that roughly “one-in-twenty Canadians (4.51%) have been victims of investment fraud” (CSA, 2007a:4). “When extrapolated to the Canadian adult population (approximately 22.5 million adult Canadians); an estimated 1,014,750 Canadians have fallen victim to investment fraud at some point in their lives” (p.4). In a more recent study commissioned by the British Columbia Securities Commission

1 This quote, and the subsequent direct quotes in this paragraph that are referenced to Hamilton’s (2007a) article, are side notes from the main piece. For the full article, see The Toronto Star at http://www.thestar.com/printArticle/281645
(BCSCn) of Canadians aged 50 and older, it was noted that “[n]early 1-in-5 (17%) of respondents believe they have been a victim of investment fraud at some point in their lives” (BCSCn, 2012a: 7). When the data is looked at regionally,

[O]ne-in-seven (14%) British Columbians say that they have been victims of fraud one time, while almost one-in-ten (8%) say they have been victims of fraud multiple times. On average, BC residents are more likely to have been victims of fraud once (14% vs. 10%) and are about as likely as Canadians in other provinces to have been victims of fraud multiple times (8% vs. 6%) (p. 7).

Given the frequency of investment fraud in Canada, it is not surprising that the losses to Canadians amount to billions of dollars.

Financial Losses

Anecdotal evidence in Canada suggests that investors’ losses run into billions of dollars. National Pensioners & Senior Citizens Federation (NPSCF), the United Senior Citizens of Ontario (USCO), and Small Investors Protection Association (SIPA) notes that “[i]nvestor losses caused by white-collar securities crime and excessive mutual fund fees are estimated to be $18 billion annually” (NPSCF-USCO-SIPA, 2007: 1).

Regulatory “failures touch virtually everyone in the country, including retail stock traders, families heavily invested in mutual funds, and the employees of companies that have been financially devastated by corporate fraud” (Hamilton, 2007b: para. 3). As the following numbers suggest, when you add other types of financial losses that occurred from pension funds, mutual funds and investments, the figures are quite staggering. It is estimated that

*over $110 billion* of aggregate damages since the mid 1980’s are due to white-collar securities crime; another *$55 billion* of damages in the last 10 years are due to excessive mutual fund fees relative to the rest of the world; of the $18 billion estimated annual investor losses, *$13 billion* are
due to white-collar securities crime and $5 billion are due to excessive mutual fund fees; about 15% of expected investment returns are being skimmed by white-collar securities crime and excessive mutual fund fees every year (NPSCF-USCO-SIPA, 2007: 1-5 emphasis added).

**Personal Consequences**

Investors must also deal with the harmful personal consequences that result from their losses. While some corporate crimes more obviously directly hurt workers (e.g., violations of safety and health codes\(^3\)) or consumers (e.g., product-safety violations\(^4\)) (Calavita & Pontell, 1995: 200), securities and investment frauds can also lead to personal harm (Boyd, 2005: 28-29). Boyd’s (2005) study on the Eron mortgage fraud (“Eron”) in British Columbia, notes that the majority of investors who suffered losses of $50,000 or more, “report extreme or major harm to their emotional well-being, their current financial situation and their retirement security” (Boyd, 2005: 28). Boyd went on to argue that “almost 30 per cent of this group report extreme or major harm to physical health, and 20 percent report extreme or major harm to friendships and marital relations” (Pp. 28-29).

Like Boyd (2005), the CSA also highlighted the personal consequences of investment fraud in Canada. The CSA’s study found that

[v]ictims, especially victims who lose $10,000 or more, frequently experience higher stress levels and feelings of anger. They often experience depression or feelings of loss and isolation. Less frequent, but still common among those who experience major losses, are panic or anxiety attacks, increased vulnerability to physical illness or extreme weight loss or gain (CSA, 2007a: 1).

The CSA also noted that

\(^3\) See Braithwaite & Fisse (1983).
[a] small but significant group of fraud victims pull back from their friends, family and the broader community. Between one-in-ten and one-in-five victims report less involvement in social activities (19%), loss of friends (16%), reduced involvement in family activities (12%) and less volunteer activities (p. 2).

**Market Integrity**

Financial crimes also raise questions about the “integrity” and operation of a well-regulated financial system (Le Pan, 2007: 4). The general view is that “capital market integrity can be thought of as a level of … confidence in the functioning of the market.” and “integrity is closely related to investors’ perception of the fairness of the markets” (IDA, 2006a: 29). Not only can scandalous practices rob people of their life savings and pension funds, but they can also work to “undermine the financial system itself” (Calavita & Pontell, 1995: 200).

If investors believe that the capital market is open to manipulation, there is false or incomplete information, corporate governance is not effective and they are not being treated fairly, investors will either leave the market or if they stay reduce the price (increase the cost of equity) of the securities to protect against this behaviour. Both outcomes will have a negative impact on the economy (IDA, 2006a: 29).

The failure of the regulatory agencies to monitor and control their members can therefore lead to “considerable loss of investor’s confidence” in the investment industry (CSA, 2007: 5; Gray, Frieder, & Clark, 2005: 2; also see Howlett, 2004: para.7).⁵ “Confidence in the integrity of capital markets translates into real benefits for our economy and for individual Canadians” (Le Pan, 2007: 4). When public confidence drops, so does the market. The significant drop in the stock markets around the world in

---

⁵ Although the Howlett’s (2004) article was specifically referring to Ontario, the comments made are applicable to the entire Canadian investment industry.
2008 and 2011, and the protestors/marchers (and their supporters) occupation on Wall Street, Bay Street and other financial city centers alike, amply substantiate this claim.

**Financial/securities Regulation and the IDA**

Financial and personal losses along with diminishing public confidence in the market illustrate a larger problem with securities regulations in Canada. It is alleged that a “patchwork system of thirteen provincial [and territorial securities] regulators and self-regulatory organizations (SROs)” are ineffective at policing Canada’s securities market (MacNeil & Solomon, 2008). In order to eliminate “potential regulatory gaps or overlaps arising from member regulation and market regulation being split into two SROs,” the IDA (the SRO responsible for regulating investment and brokerage firms in Canada) and Market Regulation Services Inc. (“RS”- the SRO responsible for regulating the marketplace) merged in June of 2008, to create the Investment Industry Regulatory Organization of Canada (“IIROC”) (Jenah 2008: 2; IIROC, 2008a: para.1).9

As a “national self-regulatory organization”, IIROC is one of the two major SROs entrusted with the task of overseeing Canada’s investment and securities

---

6 For ease of exposition, provincial and territorial securities regulators hereinafter will be referred to as provincial regulators.
7 “Market Regulation Services Inc. (RS) was formed on March 1, 2002, as a joint initiative of TSX Inc. and the Investment Dealers Association (IDA). RS became the independent market integrity services provider for the Toronto Stock Exchange (TSX), the TSX Venture Exchange (TSX-V), Canadian Trading & Quotation System Inc. (CNQ), Bloomberg Tradebook Canada Company and Liquidnet Canada Inc” (Alberta Securities Commission & British Columbia Securities Commission, 2005: 3).
8 The term “marketplaces,” as it is used in this dissertation, “includes exchanges, an entity that maintains a market for bringing together buyers and sellers of securities and a dealer that executes a trade of an exchange-traded security outside of a marketplace” (Jordan & Hughes, 2007: 50)
9 Given that the merger between the IDA and RS did not occur until June 2008, and the cases that will be used in my dissertation are before the merger, I will use the acronym IDA when making reference up to June of 2008. IIROC will be used to refer to any activities after June 2008.
10 The other is the Mutual Funds Dealers Association (MFDA) (see MFDA, 2009: 1). The MFDA is the self-regulatory organization (SRO) responsible for regulating mutual fund dealers in
IIROC regulates broker-dealer firms (“Member firms”) and their employees (“registered members”) who sell brokerage and investment services to prospective investors (Jenah 2008: 1-4).

As it now stands, “IIROC is recognized as an SRO by all [of the] provincial Securities Commissions across Canada” (Jenah 2008: 2) and “operates under Recognition Orders from the Canadian Securities Administrators [(CSA)] (Canada’s provincial … securities regulators)” (IIROC, 2009a: para. 1). IIROC in turn, sets educational requirements, ethical standards, and compliance rules that govern the conduct of its registered members and member firms (Jenah, 2007a: 2, 8, & 15). Registered members and member firms must comply with these rules, or face penalties for violations that range from a written reprimand, to permanent bans from participating in the market (see IIROC, 2008c: 4). IIROC’s nine District Councils are responsible for enforcing these rules (IIROC, 2010b: para. 1):

- Alberta District (comprised of the Province of Alberta and the Northwest Territories),
- Manitoba District (comprised of the Province of Manitoba and the Territory of Nunavut),
- New Brunswick District,
- Canada” (p. 1).

Some of the investment and securities markets that IIROC oversees are the Toronto Stock Exchange (TSX), TSX Venture Exchange (TSX V), Canadian National Stock Exchange (CNSX), Pure Trading (facilitated by CNSX), Bloomberg Tradebook Canada Company (Bloomberg), Liquidnet Canada Inc, BlockBook, MATCH Now, Alpha ATS, OMEGA ATS is an Alternative Trading System (ATS), and Chi-X Canada. For a description of the types of trades in each one of these marketplaces, see IIROC (2008e).


The legislation of the Yukon, the Northwest Territories and Nunavut does not currently provide for recognition of SROs” (Jenah 2008:2).

Note that “the securities regulatory authorities of British Columbia, Alberta, Ontario, Quebec, Saskatchewan and Newfoundland and Labrador have delegated to IIROC the authority to grant registration under provincial securities legislation” (IIROC, 2009a: para. 2) “The British Columbia Securities Commission, Alberta Securities Commission, Saskatchewan Financial Services Commission and the Superintendent of Securities of Newfoundland and Labrador have delegated the authority to grant registration to both IIROC Dealer Members and their individual employees or agents” (para. 2). “The Ontario Securities Commission and Autorité des Marchés Financiers du Québec have delegated authority to registered individual employees and agents only” (para. 2).
Newfoundland and Labrador District, Nova Scotia District, Ontario District, Pacific District (comprised of the Province of British Columbia and the Yukon Territory), Prince Edward Island District, Quebec District, and Saskatchewan District (para. 10).\(^{15}\)

Given that IIROC is in its elementary stages, this dissertation will focus on the enforcement of complaints by IIROC’s predecessor - the IDA. According to Langton (2005), the results of a 1999-2000 Ontario Securities Commission’s (OSC) audit of the IDA revealed that the enforcement side of the IDA was riddled with weaknesses.

Among its conclusions, the OSC found a growing backlog of enforcement cases; no screening process for complaints and a bloated case review process; and a ‘significant number of changes to penalty recommendations’ by the former senior vice president of member regulation (Langton, 2005: para. 8).

MacNeil & Solomon (2008) also highlighted the inherent flaws within the IDA enforcement section. These sorts of criticisms raise concerns as to whether the IDA was doing its part in protecting investors from over-zealous brokers and investment dealers. Given the accusations of weak enforcement (see Langton, 2005: para 8; MacNeil & Solomon, 2008), it makes sense to examine the IDA’s track record over time in regards to its enforcement actions following complaints.

To do this, I will utilize a model developed by Brockman and McEwen (1990; also see Brockman 2004) that examines how complaints are processed from the initial reporting through to the final disposition by one SRO – the Law Society of British Columbia. Brockman and McEwen (1990: 37) modify the crime funnel that was developed to show how the number of cases involving street crime shrinks as they are

\(^{15}\) See IIROC (2010b) for the mandate, make-up, and specific responsibilities of the District Councils.
processed from arrest to sentencing through the criminal justice system, and apply it to examine the disposition of complaints by The Law Society of British Columbia.

Brockman and McEwen’s model of case disposition by SROs is built on three fundamental concepts: “funnel in”, “funnel out” and “funnel away” (see Brockman & McEwen 1990; Brockman, 2004).

“Funnel in” tests the claim made by SROs, “that they enforce standards which would not otherwise be enforced” by other government agencies (Brockman & McEwen, 1990: 3). At the center of this premise is the notion that SROs “scrutinize a wider variety of behaviours and thereby ensure a higher standard of conduct than if the public had to rely on government regulation” (p. 3). “Funnel in” would subject more “deviant behaviour for observation, investigation and sanctions which would not otherwise be the subject of such careful review” under centralized government regulation (p. 3). “‘Funnel out’ looks at how offenders might escape disciplinary action once they enter the system, and the potential leniency of penalties imposed on those who are formally sanctioned” (Brockman, 2004: 73). Brockman and McEwen (1990: 3-4) note that, “rather than widening the net of social control, the disciplinary system” of SROs “‘funnels out’ so many deviants that it is, in fact, ineffective as a means of social control.” “Members of SROs and not the public are viewed as being the beneficiaries of self-regulation” (p. 4). The preoccupation of SROs to protect their own, “may function to keep their members from coming into contact with the criminal justice system when criminal offences have been committed” (p. 4). This charge alleges that “SROs ‘funnel away’ individuals from the criminal justice system who might otherwise come into contact with it” (p. 4).

The purpose of this dissertation is to use the SRO funnel, as it was developed by Brockman and McEwen (1990) and further refined by Brockman (2004), to explore the
processing of complaints received by the IDA and the manner in which they are dealt with by the Disciplinary Committee. The main question then becomes one that seeks to understand the enforcement process of the IDA in disciplining its members. More specifically, the question to pose is: What are the salient patterns and trends in the enforcement of complaints received by the IDA on its registered members and member firms? To accomplish this task, the study will first look at the enforcement process by using the IDA's Enforcement and Annual Reports. Next, the study will examine the enforcement pattern of the IDA by using data from the IDA’s cases. To do this, the study will first display the data by looking at the demographics and the investment background of the investors. Second, the study will then examine the general characteristics of the offenders (registered members and Member firms) accused of violating the IDA’s By-laws. Third, the study will analyze the patterns and trends in the enforcement of complaints for both registered members and Member firms.

**Structure of the Dissertation**

The remainder of this dissertation is structured along the following format:

Chapter 2 looks at the debates surrounding the efficacy of self-regulation as part of the investor safety net. The views from regulators, victims’ rights advocates, commissioned reports, and advisory panels are examined to provide a rationale as to why it is important to study the performance of the SRO in charge of policing investment dealers trading in the debt and equity markets in Canada.

Chapter 3 canvasses the literature on self-regulation. In doing so, I first sketch its theoretical underpinnings and highlight the relevance of SROs in the regulatory landscape of countries where self-regulation continues to play a part in regulating the capital markets. I then examine the arguments that have been used to justify the use of
self-regulation and criticisms levelled by critics against its usage. Next, I briefly highlight the role of self-regulation in securing compliance in other industries. I then examine self-regulation in relations to other regulatory agencies, namely the U.S. Securities and Exchange Commission (SEC), the OSC, and the criminal justice system, in governing the securities industry.

Chapter 4 outlines the evolution of the IDA. This chapter traces the IDA as an Association that existed in name only and scarcely disciplined its members, to a fully functional SRO that is subjected to government oversight. The chapter chronicles the IDA’s progress and shows how the Association’s authority in industry governance decreased, as the government took on a more active role in regulating the securities market.

Chapter 5 describes the research design and methodology that was used to gather and analyze the data. More specifically this chapter provides information on general data collection and the sources of data used in the dissertation. The general framework surrounding the coding scheme and the type of information that was obtained from the data, are discussed as well. This chapter also addresses the concerns related to reliability and validity in the data collection process.

Chapter 6 is the first of three chapters that analyses data from different sources. Chapter 6 employs descriptive statistics to analyse data from the IDA Enforcement and Annual Reports. More specifically, in examining the IDA’s enforcement process, this chapter uses the misconduct funnel to analyse the processing of complaints from initial reporting to final disposition by the IDA’s disciplinary system.
Chapter 7 analyses data from the IDA’s cases. This chapter first looks at the demographic portrait of victims, then examines the characteristics of the individual offenders and Member firms found guilty of violating the IDA By-laws. Next, the chapter looks at the enforcement profile of the IDA in holding these individual offenders and Member firms accountable to its By-laws.

Chapter 8 analyses data from the securities commissions. The chapter examines all of the cases that were reviewed by the securities commissions from registered representatives, Member firms, the IDA, and victims themselves. Instead of going into detail about the substance of the appeals, the purpose of this chapter is to highlight the types of appeals that were reviewed by the commissions and their verdicts.

Chapter 9 presents a qualitative analysis of the aggravating and mitigating factors considered by the IDA’s hearing panels in the imposition of sanctions. In examining these factors, particular attention is given to aggravating factors identified and considered in assessing penalties and aggravating factors identified, but that were not considered in penalty imposition. In addition, I look at the aggravating factors that were also used as mitigating factors by the hearing panels in considering the appropriate penalties.

Chapter 10 discusses the findings and looks at the policy implications of the study. In doing so, I address the steps that IIROC should take as part of Canada’s regulatory landscape, in order to protect investors from being swindled by unscrupulous investment advisors.
Chapter 2: Significance - The Case for a Study on the IDA

It is a widely held belief that white-collar securities crimes are rampant in Canada (see FAIR Canada, 2011b: 2). FAIR Canada reported that “financial fraud and other financial market misconduct affecting Canadians, appear[s] in the media virtually on a daily basis” (p. 9). An example of these frauds is a case in Quebec where

Montreal investment adviser Earl Jones was charged with four counts each of fraud and theft in connection with four former clients. Quebec's securities regulator alleges Jones swindled at least 50 investors out of at least $30 million in a possible Ponzi scheme (Canadian Broadcasting Corporation, 2009: para. 7-8).

In 2010, Jones pleaded guilty to fraud charges and was sentenced to 11 years in prison (Canadian Broadcasting Corporation, 2010: para. 1). Other examples of Ponzi-style fraud cases are the “Brost, Sorenson et al. scheme in Alberta, [which] operated between 1999 and 2005, [and] where investors lost up to $400 million (FAIR Canada, 2011b: 19). There is also the Manna fraud in British Columbia, which was “committed by four principals…between 2005 and 2007, [and] totaled up to $16 million in investor losses” (p. 19). Monetary losses of this magnitude pose threats to Canada’s financial system and deter investors by driving them away from investing in the markets. All of these factors combined, raise questions on issues related to coordination among regulators and the role of the IDA in policing white-collar securities crime in Canada (see FAIR Canada, 2011b: 24).

The Wider Context of Securities Regulation in Canada

According to some commentators, the IDA (now IIROC) is embedded in a maze of regulation (Urquhart, 2008: 6; Pan, 2009: 25-27). In Canada, "securities regulation is
entirely in the hands of the provinces” with “each province maintain[ing] its own securities commission16 (Pan, 2009: 25). “Accountability for securities regulation extends from the securities regulator to the Minister responsible for securities regulation and, ultimately, the legislature, in each province” (Hockin Panel, 2009a: 39). In their quest “to promote coordination of regulation across borders, the provincial commissions have formed the Canadian Securities Administrators…, consisting of the chairs of the thirteen provincial securities regulators” (Pan, 2009: 25). The CSA’s mission is “[t]o give Canada a securities regulatory system that protects investors from unfair, improper or fraudulent practices and fosters fair, efficient and vibrant capital markets, by developing a national system of harmonized securities regulation, policy and practice” (CSA, 2009a: para 1).

“In addition to the provincial commissions, several SROs play an important role in the regulation of Canada’s securities markets” (Pan, 2009: 26). “The most important of these SROs are IIROC and the MFDA” (p. 26-27)17. The provincial securities commissions and SROs are complimented by the Royal Canadian Mounted Police (RCMP) and Provincial and territorial Attorneys-General (CSA, 2007: 4).

This enforcement mosaic has been criticized for being “fragmented,” and not allowing “Canada to be as responsive and effective as it should be” (Hockin Panel, 2009a: 41; also see Hamilton, 2007a: para. 24). This concern was also echoed by Utpal Bhattacharya (2006), who was asked to prepare a report by the Task Force to

16 With the exception of Newfoundland, Prince Edward Island and the Territories, (where securities trading are “regulate[d] directly through government ministries”) each province “has created a Securities Commission under the powers of the relevant securities legislation” (Carnaghan & Gunz, 2006: 21).
17 There is also the Chambre de la sécurité financière (CSF) in Quebec. The CSF “oversees financial planners and some securities intermediaries Quebec” (CSA, 2007: 4).
Modernize Securities Legislation in Canada ("the Task Force")\textsuperscript{18}, "documenting the effect of enforcement of securities laws on cost of equity and liquidity [\(\ldots\)] and …to study Canada in as much detail as available data will allow" (Bhattacharya, 2006: 6). Bhattacharya's report noted that securities regulation in Canada is "decentralized" and "fragmented" with "provincial securities commissions and self-regulatory organizations" all involved in a complex process of regulation that involves "multiple rules, decision makers and costs" (p.6). While Bhattacharya's report alludes to the benefits of having so many regulatory bodies, it also highlights the drawbacks – one of which is the poor enforcement of securities laws (p.6).

As with most white-collar crime, securities violations can stimulate a range of official responses from SRO investigations and hearings to criminal prosecution. In between these extremes are the possibility of regulatory actions by provincial securities commissions and quasi-criminal prosecutions under provincial legislation. The same activity can call for all four types of responses; however, it would be rare for all four to occur. Decisions regarding which enforcement agency should pursue white-collar securities crime create a complex coordination issue. For example, at one point the IDA and the MFDA "identified at least 84 cases of suspected fraud, forgery or misappropriation of funds to police", but there’s no guarantee that these will be taken on (Hamilton, 2007a: para. 34, 35).\textsuperscript{19}

Douglas Hyndman, when chair of the BCSCn, highlighted the distinction between regulatory action and criminal prosecutions (Hyndman, 2007a: 4-5):

\textsuperscript{18} Bhattacharya’s (2006) report is one of about thirty research papers and reports prepared for the Task Force to look at securities regulation in Canada (See IDA, 2006a, 17-21).
\textsuperscript{19} According to Hamilton (2007a: para: 36), "it's unclear how many of these cases have been investigated" … as the RCMP’s Integrated Market Enforcement Team (IMET) “resists disclosing names of those being probed until charges have been formally laid.”
Criminal and regulatory enforcement serve different but complementary purposes. Criminal enforcement punishes wrongdoers for past misconduct. Regulatory enforcement protects investors and markets from future misconduct. Both provide deterrence but in different ways (p. 5).

Hyndman went on to argue that

Criminal enforcement offers more serious penalties, including jail, and the stigma of a conviction. It requires proof beyond a reasonable doubt. Strict rules govern how authorities can obtain and use evidence. The accused has a right against self-incrimination. Regulatory enforcement, by contrast, offers less severe sanctions — monetary penalties and disqualification from the market — but is more flexible. The standard of proof is lower, as are the thresholds for gathering and using evidence (p. 5).

As a result of these fundamental “differences, the courts have drawn lines between the two processes, so authorities can[not] use regulatory investigation powers to conduct a criminal investigation” (p. 5). However, “regulators and police can and do cooperate, but there are limits and [they] cannot intertwine the processes” (p.5).

Given the limits to which regulators and the police can cooperate in enforcing securities laws, Hyndman suggests that it is “time for criminal enforcement [in Canada] to step up to the plate” (Hyndman, 2009a: 11). Hyndman drew inferences from the U.S. to reinforce his point (see Hyndman, 2007a: 4). According to Hyndman,

Those who attack our enforcement record point to tough U.S. enforcement actions and say we need to change Canadian regulation so we will measure up. But the major disparity between Canada and the U.S. is in the criminal justice sphere — not regulatory enforcement. Most of the U.S. cases cited as examples of tough enforcement are not regulatory matters at all, but criminal cases prosecuted in court by the U.S. Department of Justice or state attorneys general (Hyndman, 2007a: 4).
Some of the cases Hyndman referred to are the “the high-profile U.S. cases — WorldCom, Enron, and Adelphia— [which] were the result of criminal, not regulatory enforcement” (as cited in Hamilton, 2007a: para. 34).

Urquhart (2008: 6-9) highlights the roles of the IDA and the securities commissions in relation to the criminal justice system. According to Urquhart, the RCMP and the regional and municipal police forces have been inundated with calls from investors, and have expressed concerns that they “cannot continue to send all persons with complaints of wrongdoing in the investment industry and in public corporations to the provincial securities commissions” (2008: 7). Urquhart notes that neither the provincial securities commissions nor the IDA have the legislative mandate to prosecute criminal charges under the Criminal Code (Urquhart, 2008: 7-8). The IDA has “no legislative authority, nor public accountability mechanisms, to ensure that wrongdoers are properly investigated and prosecuted” (p. 7). Being an SRO, the IDA has “no authority to lay criminal or quasi-criminal charges involving jail sentence penalties, either directly or by presenting such charges to a court” (p. 7). The IDA is however, required to refer cases with evidence of criminal offences to the criminal justice system for further investigation (IIROC, 2008c: 1). Likewise, the “provincial securities commissions do not have the authority to prosecute criminal charges under the federal Criminal Code” (Urquhart, 2008: 8 emphasis added). In theory, the provincial securities commissions could bring a private prosecution under the Criminal Code, but this would be subject to provincial prosecutors’ powers to take over such prosecutions (see Brockman & Rose, 2011: 74-76).²⁰

²⁰ Brockman and Rose (2011: 74-76) did not specifically refer to the provincial securities commissions; rather, they provide an explanation on the instances where “a private individual can
Urquhart (2008:1) calls for a “complete overhaul of Canada’s process for receiving complaints from the public and whistleblowers about white-collar securities crime.” More specifically, Urquhart laments the need for “a securities crime complaints intake and assessment system managed by police, rather than the investment industry’s Self-Regulatory Organizations…and provincial securities commissions” (p. 6). Urquhart goes so far as to suggest that Canada should eliminate its reliance on SROs when it comes to protecting investors (2008:1).

However, despite these criticisms of Canada’s securities enforcement system, the CSA (in its 2008, 2009, and 2010 Enforcement Reports) seems to think that coordination is working (see CSA, 2008: 4; CSA, 2009b: 4; CSA, 2010: 5). One indicator used to gauge “the level of securities enforcement activity in Canada,” is to look at “the number of proceedings commenced” (CSA, 2008: 4). The CSA provides the following statistics in their report on securities commissions’ enforcement across Canada. In 2008, “the 215 total proceedings commenced …include 279 individuals and 137 companies…CSA members concluded 123 cases in 2008, involving 193 individuals and 129 companies” (CSA, 2008: 4). In 2009, “the 124 total proceedings commenced …include 154 individuals and 112 companies… CSA members concluded 141 cases in 2009, involving 160 individuals and 103 companies” (CSA, 2009b: 4). In 2010, “the 178

prosecute a case” under the Criminal Code. Even though the possibility of private prosecution exists, “in 2002, the federal government introduced a new procedure for justices to deal with private information…, which gives prosecutors more supervisory powers over private prosecutions” (p. 74). Brockman and Rose also note that the Attorney General of the province may still intervene in such a case and take control of the prosecution under section 579 [of the Criminal Code]” (p. 75).

21 Proceedings commenced are cases in which a Commission staff’s allegations have been filed or, in the case of a quasi-criminal proceeding, an information sworn before the courts, both of which allege wrongdoing. Many of the proceedings commenced in 2008 were still underway at the end of the year. In such cases, there has been no finding of wrongdoing. CSA notes that “[m]any of the proceedings commenced in 2009 were still underway at the end of the year, and in such cases, decisions have yet to be rendered” (CSA, 2009b: 4).
total proceedings commenced … include … 301 individuals and 183 companies… CSA members concluded an aggregate total of 174 cases in 2010, involving 207 individuals and 100 companies” (CSA, 2010: 5).

If one was to set previous years as benchmarks for gauging the performance of CSA member staff, it is evident from the numbers provided that the level of enforcement activities commenced by CSA member staff decreased from 171 in 2008 to 124 in 2009 and increased again to 178 in 2010 (CSA, 2010: 5). The number of cases concluded increased steadily from 123 in 2008 to 141 in 2009 and 174 in 2010 (p. 5).

Prior to this time, there had been calls for structural changes to the enforcement process. In 2006,

[t]he Task Force recommend[ed] that a co-operative national program be established and funded by securities regulators, self-regulatory organizations (SROs) and law enforcement agencies: (1) to establish priorities for enforcement, (2) to develop reporting systems that would provide a basis for assessing the effectiveness of enforcement processes in achieving their objectives, (3) to identify and collect any additional relevant data, and (4) to report the data and their qualitative analysis of it to an independent research body which will evaluate and issue public reports on the effectiveness of enforcement processes (IDA, 2006a: 11).

Similarly, Nick Le Pan’s (2007) report to the RCMP, “Enhancing Integrated Market Enforcement Teams (IMET), Achieving Results in Fighting Capital Markets Crime”, calls for more "collaborat[ion] with other law enforcement agencies and securities regulators to ensure that all complaints and enquiries received by IMET pertaining to … market offences (e.g. money laundering in capital markets, securities law violations and other commercial crimes and violations)...be referred to the RCMP Commercial Crime Branch” (Le Pan, 2007: 12).
Self-Regulation and the Market

An important principle in making SROs effective is to make sure that they carry out their enforcement mandate by holding members accountable to law and ethical standards (Ayres & Braithwaite, 1992: 103-105; also see Simpson, 2002: 99). At the same time, SROs in the financial sector must also attempt to protect investors from over-zealous investment dealers and brokers (Gray et al., 2005: 3-5). The extent to which IIROC is holding members accountable is not yet known. This study will examine the historical work of what is now IIROC, in order to provide policy suggestions for future enforcement in the securities arena.

In 2007, it was estimated that Canadians held “almost $2 trillion in financial assets,” and Federal Finance Minister Flaherty stated that, “effective enforcement is critical if [the government is] going to truly protect investors and make [Canada] globally competitive” (Flaherty, 2007: para. 10). Since “effective rules of the game and how well you enforce them are essential” (para. 10), a study of how an SRO that is responsible for guarding a substantial portion of the financial assets of Canadians enforces the rules, is timely. Moreover, the Expert Panel on Securities Regulation (Hockin Panel) believes that while

...self-regulation is an important feature of our regulatory system that should be preserved, the Panel heard numerous complaints about the lack of independence of the SROs from the industry, the contractual relationships with the regulator (rather than a legislative one), and the concerns from investors about the process of complaint-handling and redress. A full review of SROs was beyond the scope of the Hockin Panel mandate. The Commission, once formed, should take stock of the performance and responsibilities of the SROs (Hockin Panel, 2009a: 46 emphasis added).
More recently, the Transition Plan for the Canadian Securities Regulatory Authority (“Transition Plan”) (2010), notes that the Canadian Securities Regulatory Authority (CSRA), once formed, “will ultimately want to review and consider the future role of self-regulatory organizations” in the securities industry (Canadian Securities Transition Office, 2010: 15 emphasis added). My dissertation can be seen as taking stock of both the “performance and responsibilities,” and “reviewing” the roles of a single SROs’ operations - the IDA and its enforcement record.

Investors, government officials, and the public in general, deserve to know the IDA’s enforcement record, particularly its ability to hold investment dealers accountable to its rules. This type of study has the ability to reveal such information and its results can be used by policy makers to improve on areas that are seen as ineffective. It could lead to the implementation of more informed regulatory policies in order to better regulate the investment and securities markets and restore investors’ faith and confidence to invest in “open and fair capital markets” (IDA, 2002: para.1).
Chapter 3: The Literature on Self-Regulation

Self-Regulation as a Concept

Generally the term “self”, as it is used in “self-regulation”, has come to signify a “collective grouping” of people that seek to regulate their members without state intervention (Chartered Financial Analyst (CFA), 2007: 1; also see McCaffrey & Hart, 1998: 7). The term “regulate” means that the collective, as a group, attempts to exercise control “to meet some established standards” (Turnbull, 1997: 3). The group acts under the rubric of an organization, an industry, or a professional association (usually called an SRO), to establish standards that will govern the conduct of its members (CFA, 2007: 1-2).

Others have charged that “self-regulation refers to situations in which firms, individuals, or other parties are allowed to monitor and adjust their behaviour using certain standards and perhaps to set the standards themselves” (McCaffrey & Hart, 1998: 6). A more attenuated definition notes that “ ‘self-regulatory organization’ means [an entity] that is organized for the purpose of regulating the operations and the standards of practice and business conduct, in capital markets, of its members and their representatives with a view to promoting the protection of investors and the public interest” (Hockin Panel, 2009b: 25). Some even go as far as defining self-regulation as “a system that encourages (‘regulates’) certain social behaviours by a collective (the ‘Self’) in order to avoid direct State intervention (‘regulation’)” (CFA, 2007: 1). While these definitions like any other definition of self-regulation are not all encompassing, those associated with market regulation share as their underlying theme, the importance of integrity in the marketplace (Pritchard, 2003: 33); the “common guidelines to govern

21
[the] collective behaviour” of the actors involved (CFA, 2007: 1); and the importance of “transparency” in regulatory activities (Jassem, 2005: 2).

That said, for the purpose of this dissertation, the term “self-regulation” under the rubric of an SRO, has evolved to refer to

the delegation of government regulatory functions to a quasi-public body that is officially expected to prevent or reduce both incompetence (lack of knowledge or ability) and misconduct (criminal, quasi-criminal, or unethical behaviour) by controlling the quality of service to the public, through regulating or governing a number of areas (Brockman, 1998: 588).

Central to this definition is the notion that the government has delegated regulatory functions to the SRO. It is expected that the SRO will fulfill its regulatory functions by holding its members accountable to law and ethical standards. In order to hold its members accountable to law and ethical standards, and prevent further government intervention, the SRO must align its interest with that of the public. When viewed through this lens, the government can be said to be acting as a regulatory oversight body that intends to hold the SRO accountable for its actions.

The complexities of the activities that SROs regulate, make it very difficult to have a single definition that guides their regulatory practices. Given this variation, most SROs have implemented “tailor-made regulatory regimes to suit the complex business and regulatory environments in which they operate” (Jordan & Hughes, 2007: 210). Even though the regimes may be different in their scope and mandate, their single most “overarching purpose...is to keep industry interests aligned with the public interest so as to avoid government intervention and the possibility of more-restrictive regulation” (CFA,

23 See Brockman (1998) for the framework used to qualify for self-regulation status.
The different forms of regulatory regimes give rise to a number of “regulatory attributes” that are composed within various forms of SROs (CFA, 2007: 9; also see Brockman & McEwen, 1990: 2).

A Continuum of Self-Regulation

SROs range from voluntary or pure self-regulation to regulation by government oversight (Brockman & McEwen, 1990: 2-3). The different types of SROs, “can be viewed on a continuum in terms of the degree to which a government backs the organization and the power which it has delegated to the SRO” (p. 2). In turn, the “SROS enlist state support for legislation, which ensures that only their members (that is, those who are sufficiently skilled, knowledgeable and, in some cases, reputable) are allowed to offer their services to the public (licensure) or are allowed to use a specific title (certification)” (Brockman, 1998: 588).

The underlying variable then is the SRO’s relationship with the state, which starts from voluntary self-regulation and involves no formal supervision to the degree of government oversight exhibited over the SRO at the highly regulated end of the continuum.

According to the CFA, voluntary SROs are “a group of individuals” involved in a “particular trade” or share a common “skill”, and get together to “represent the interests of their members” (CFA, 2007: 9). They are not “state-backed in the formal sense; the government neither legislates them into existence nor delegates powers to them” (Brockman & McEwen 1990: 2). They may also have ethical and minimal educational standards to which their members must adhere. Even though “the government might facilitate their formation through legislation governing associations and corporations, it is not usually involved in enforcing rules created by the SROs” (p.2). SROs that fall into this category usually do not “discipline [their] members for noncompliance with [their]
guidelines” or “possesses [the] mechanisms for investigating alleged misconduct by members, or sanction their members for infractions brought by outside authorities” (CFA, 2007: 9-10). Examples of these are “the early stock exchanges that fixed commissions …[and] an investment club, where members participate in the group and adhere to written standards that govern the treatment of the group’s pooled resources” (p. 9).

Next on the continuum are accredited associations with compulsory standards and membership requirements (CFA, 2007: 10). Membership in these associations confers status and gives the registered members a competitive advantage over non-members24 (p. 10). Lack of membership however, “does not affect their ability to work in that market sector” (p.10). In Canada, “provincial and territorial law gives a professional [association] for each [accounting] designation the power to govern the profession in that jurisdiction” (Competition Bureau, 2007: 43). An example of such an association is the Institute of Chartered Accountants of British Columbia (ICABC) (p.43). The ICABC has its own education requirements and standardized examinations that members are expected to complete in order to be licensed as Charted Accountants (CA) in the province (Pp. 43-44). Once licensed, a CA has “Title Protection” and can expect to earn more than an accountant who is not licensed and accredited.25

24 The word “non-members” should be emphasized here. While a licensed accountant (CA for example) has “Title Protection” and can be disciplined by the ICABC for misconduct, no such penalties are in place for the college commerce graduate (a non-member) who performs accounting duties in his job without a license to practice as an accountant. That said, being a licensed CA provides more than “Title Protection.” A CA who is licensed by the ICABC can “perform services related to financial statements; issuance of any opinion or report whereby the issuer is acting as an independent accountant or auditor, or has expert knowledge in accounting or auditing matters; accounting, where it involves analysis, advice, or interpretation in an expert capacity (excluding bookkeeping unless financial statements are also prepared); and tax advice and counselling in an expert capacity (excluding mechanical processing of tax returns)” (ICABC, 2009c: para. 1).

25 Brockman (1998: 588) distinguish between “licensure” and “specific title”. Brockman notes that “SROs enlist state support for legislation, which ensures that only their members (that is, those
There are also “Professional Conduct Enquiry and Discipline Processes” in place by the ICABC, “to protect the public and maintain the integrity of the profession” (ICABC, 2009a: para. 1). Through the CA Act and The Bylaws and Rules of the Institute, the Professional Conduct Enquiry Committee has the power to investigate and refer complaints to the Discipline Tribunal for hearing (ICABC, 2009b: para. 2-3). No such mechanisms are in place however, to protect the public from individuals who are performing accounting related duties, but are not licensed.

Moving along the continuum are those associations, which by law require membership to practice (CFA, 2007: 10). They are backed by the state, in that they are “created by legislation” and “delegated the power to make rules, investigate and adjudicate alleged breaches, and impose penalties on wayward members” (Brockman & McEwen 1990: 3). These SROs are usually established by professional groups, such as doctors and lawyers. An example of such an SRO is the Law Society of British Columbia. The Society has its own membership and licensing requirements for lawyers and articling students who wish to practice law in the province. Through the Legal Profession Act, there are provisions that govern the complaints and disciplinary processes of members’ accused of misconduct (see Law Society of B.C., 2008). The one distinguishing feature that sets these SROs apart from those that are classified as accredited associations with compulsory standards, is that individuals cannot offer specified services without being licensed by the regulatory body that oversees their profession.

who are sufficiently skilled, knowledgeable and, in some cases, reputable) are allowed to offer their services to the public (licensure) or are allowed to use a specific title (certification)” (p. 588).
At the more highly regulated end of the continuum are SROs where the government or government agency oversees the SRO’s regulatory activities (Brockman 1998: 591; CFA, 2007: 10-11). Even though an SRO in this category has the power to regulate themselves, the “government retains ultimate oversight authority in which it can override the group’s regulatory proposals or impose rules and regulations as it deem[s] warranted” (CFA, 2007: 10-11; also see Brockman 1998: 591 and Priest 1997-1998 for variations on this oversight). The presence of the government in overseeing the operations of SROs in this category “serves as a motivator” for them “to conduct [their] activities in such a way,” so as to ward off direct government intervention (CFA, 2007: 11). The Financial Industry Regulatory Authority (FINRA) in the U.S. falls into this category. The SEC oversees the regulatory activities of FINRA, but allows it to “generate rules and policies for broker-dealers and trading markets” (Pan, 2009: 17-18, 39). In Canada, the provincial securities commissions are the oversight committees for SROs such as IIROC, which in turn oversees the market regulation of exchanges, member firms and investment and brokerage dealers.

**Global Trends in Securities Regulation**

In this section, the purpose is not to evaluate in detail the regulatory systems of the major world markets.\(^{26}\) Rather, the intention is to look at countries where regulatory reforms have had a major impact in regulating the marketplace and the role of self-regulation as part of the investors’ protection safety net in the securities industry. Whatever its form, self-regulation continues to play an integral role in the regulation of the securities industry in both developed and emerging economies (see Carson, 2011:

\(^{26}\) See Pan (2009) and Carson (2011) for a discussion on the regulatory systems of some of the major world markets.
In North America, self-regulation "continues to play a strong role ... where independent SROs are assuming responsibilities from exchange SROs" (p. 2). In North America, self-regulation "continues to play a strong role ... where independent SROs are assuming responsibilities from exchange SROs" (p. 2). Australia traditionally had a strong exchange regulatory model, but has since transferred market regulation to a government regulator (see Carson, 2011: pp. 3 and 43-44). In other economies, self-regulation as a regulatory tool is under pressure to survive the changing nature of financial institutions, as they try to adapt to more complex capital market structures (see CFA, 2007: vi-vii; Jordan & Hughes, 2007: 219-221). In Europe, self-regulation "now plays a minor role," while in Asia, the "reliance on self-regulation has been reduced, but it remains important in most countries" (Carson, 2011: 2).

**Australia**

Australia has a "‘twin peaks’ model of financial regulation" made up of the Australian Securities and Investment Commission (ASIC) and the Australian Prudential Regulatory Authority (APRA) (Cooper, 2006: 4). In the past, "the Australian Securities Exchange (ASX) had maintained broad SRO responsibilities by law," but in 2010, "the government announced that most of the ASX’s responsibilities [would] be transferred to

---

27 Some of the changes in the marketplaces over the last several years are, "consolidations [and] demutualization [of exchanges], diversification of financial instruments traded, [electronic trading], and... a blizzard of other technological changes" (Jordan & Hughes, 2007: 4; also see CFA, 2007: 3-4 for a discussion on how the advancement of technology affects the regulation of the marketplaces). The term "demutualization," "generally involves conversion of an exchange from a not-for-profit member-owned organization to a for-profit shareholder-owned corporation" (Hughes, 2002: 33). It is the “process of changing an organization from its mutual ownership structure to a shared ownership structure” (p. 35). As it applies to stock exchanges, demutualization “changes the orientation and mandate of an exchange from a cooperative to a business” (Carson, 2003: 5). The first stock exchange to demutualize was the Stockholm Stock Exchange in 1993 (Hughes, 2002: 35). Some of the other exchanges to follow “Stockholm’s lead are the Australian Stock Exchange (ASX), Toronto Stock Exchange (TSE), Singapore Stock Exchange, Hong Kong Stock exchange, and … Pacific Exchange (PCX)” (p. 35).

28 The ASX was formed by the merger of the Australian Stock Exchange and the Sydney Futures Exchange in 2006 (ASX Group, 2012: para. 2). In 2010, the "ASX launched a new group structure to better position it in the contemporary financial market environment" (para. 3). As of “August 2010[,] the Australian Securities Exchange has been known as the ASX Group” (para. 3).
the ASIC, the government authority... [which assumed] the majority of ASX’s regulatory functions” (Carson, 2011: 3 and 29).

The ASIC is an “independent...Government body” that acts as “Australia’s corporate, markets and financial services regulator” (ASIC, 2012: para.1 and 3). The ASIC “regulate Australian companies, financial markets, financial services organizations and professionals who deal and advise in investments, superannuation, insurance, deposit taking and credit” ( para. 7).

As the consumer credit regulator, [the ASIC] license and regulate people and businesses engaging in consumer credit activities (including banks, credit unions, finance companies, and mortgage and finance brokers). [The ASIC] ensure that licensees meet the standards - including their responsibilities to consumers - that are set out in the National Consumer Credit Protection Act 2009. As the markets regulator, [the ASIC] assess how effectively authorized financial markets are complying with their legal obligations to operate fair, orderly and transparent markets...As the financial services regulator, [the ASIC] license and monitor financial services businesses to ensure that they operate efficiently, honestly and fairly. These businesses typically deal in superannuation, managed funds, shares and company securities, derivatives, and insurance (para. 8-10).

In terms of its regulatory and enforcement powers, the ASIC is in charge of

… make[ing] rules aimed at ensuring the integrity of financial markets; stop the issue of financial products under defective disclosure documents; investigate suspected breaches of the law and in so doing require people to produce books or answer questions at an examination; issue infringement notices in relation to alleged breaches of some laws; ban people from engaging in credit activities or providing financial services; seek civil penalties from the courts; [and] commence prosecutions [that]...are generally conducted by the Commonwealth Director of Public Prosecutions, although there are some categories of matters which [the ASIC] prosecute [themselves] (para. 11).

APRA was established in 1998, and is predominantly seen as a prudential regulator. APRA “oversees banks, credit unions, building societies, general insurance and reinsurance companies, life insurance, friendly societies and most members of the
superannuation industry” (APRA, 2011: para.1). APRA’s mission is “to establish and enforce prudential standards and practices designed to ensure that, under all reasonable circumstances, financial promises made by institutions [are] supervise[d] [and] met within a stable, efficient and competitive financial system” (para. 3). For the most part, APRA’s funding comes from the “industries that it supervises,” and it “has three main regulatory tools: authorization or licensing powers, supervision and monitoring powers, and powers relating to the assumption of control of insolvent or otherwise troubled firms” (APRA, 2011: para.1; Pan 2009: 36).

Japan

Japan continues to have a complex system of securities regulations. “Until 1998, the Ministry of Finance (MOF) supervised almost the entire Japanese financial system, making the MOF effectively Japan’s single regulator” (Pan, 2009: 49). In the process, the MOF created the Securities Exchange Surveillance Commission (SESC) in 1992, to address the series of scandals related to securities firms that plagued Japan’s financial industry in the early 1990s (SESC, 2011: 2; Pan, 2009: 49). The SESC “was establish[ed] within the ambit of the Ministry of Finance for the purpose of ensuring fair transactions in both securities and financial futures markets[,] and maintaining the confidence of investors in these markets” (p. 2).

As Japan’s “financial difficulties continued,” regulators “engaged in several attempts at regulatory reform” (Pan, 2009: 49). In 1998, the Japanese Financial Supervisory Agency (JFSA) “was established as an administrative organ (external organ of the Prime Minister’s Office) responsible for inspection and supervision of private sector financial institutions and surveillance of securities transaction[s]” (JFSA, 2011: 2). Initially, “[t]he JFSA …had responsibility for the inspection and supervision of all financial
institutions… [i]n this respect, the JFSA began as a prudential regulator” (Pan, 2009: 49). However, starting

[i]n 2000, the government increased the powers of the JFSA beyond prudential supervision to include business conduct regulation. Renamed the Financial Services Agency, the JFSA took over the Financial System Planning Bureau of the MOF and secured new powers to draft laws and promulgate business conduct rules, mandate disclosures by financial institutions, carry-out inspections and sanction financial institutions. The JFSA also was given responsibility to regulate the Japanese securities markets…(p. 49).

With the implementation of the Financial Instrument and Exchange Act (FIEA) in 2007, the SESC role was expanded (SESC, 2011: 2). The new legislative framework allowed

the JFSA to delegate… most of it supervisory power to the Securities Exchange Surveillance Commission (SESC). The SESC can now conduct investigations of illegal activity such as insider trading, market manipulation, loss compensation or guarantees, and violations of disclosure regulations. With these additional powers, the JFSA has become a powerful single regulator – arguably the most powerful single regulator in the world after the UK FSA – having regulatory responsibility for all of Japan’s financial markets with the exception of certain prudential supervisory duties that it shares with the Bank of Japan (Pan, 2009: 49; also see SESC, 2011: 2).

Japan’s financial system is also comprised of “exchange and independent SROs” (see Carson, 2011: 29). “Japanese exchanges (primarily the Tokyo Stock Exchange and Osaka Securities Exchange) regulate their own markets, securities dealers that trade on the exchange, and companies listed on the exchange” (p. 29). There is also the Japan Securities Dealers Association (JSDA), which “is an association functioning as a self-regulatory organization (SRO) and as an interlocutor for the securities industry” (JSDA, 2011: para. 1).

As a fully empowered SRO, [the] JSDA extensively regulates market intermediaries. Its self-regulatory functions encompass rule-making, enforcement, inspection, disciplinary actions, accreditation of sales
representatives, and dispute mediation” relating to its members (JSDA, 2011: para. 2).

As a trade association, the “JSDA also provides vehicles for policy dialogue among the industry, the government and other related parties, conducts and promotes investor education, and implements studies for further activating the market” (para. 3). In addition to the JSDA, “the Financial Futures Association of Japan regulates broker-dealers in the financial futures industry and the Japan Securities Investment Advisors Association regulates investment advisers” (Carson, 2011: 29).

**Hong Kong**

Hong Kong has slowly moved away from self-regulation of the securities markets, and has chosen to implement alternative forms of regulation (See Jordan & Hughes, 2007: 209-212 & 218-223). “As an international financial centre, Hong Kong’s markets are large and complex…To meet the markets’ sophisticated needs, several regulatory authorities keep a watchful eye on the money business” (Securities and Futures Commission (SFC), 2009: 1). At present, Hong Kong has a “three tier system” of financial market regulation (Arner, Hsu, & Da Roza, 2010: 2).

Under the first tier, the Financial Secretary is responsible for overall policy and the Financial Services and the Treasury Bureau (‘FSTB’) is responsible for translating policies into regulation. Under the second tier, specialist regulatory agencies are responsible for regulation and supervision of financial services business. This tier includes the Hong Kong Monetary Authority (‘HKMA’ – regulating banking and banks), the Securities and Futures Commission (‘SFC’ – regulating the securities and futures markets), the Office of the Commissioner of Insurance (‘OCI’ – regulating insurance business), and the Mandatory Provident Fund Schemes Authority (‘MPFA’ – regulating the pensions industry). Under the third tier, self-regulatory organizations are responsible for oversight of the activities of their members, albeit under the supervision of the relevant specialist regulatory agency and, increasingly pursuant to legislation (p. 2).
While this framework is “strong in individual sectors, gaps and overlaps remain a factor in Hong Kong’s regulatory system” (Arner, Hsu, & Da Roza, 2010: 1). To address conflict-of-interest issues that arises from these overlaps, and to ensure coordination among the different regulators, Hong Kong has a Cross-Market Surveillance Committee, comprised of members from Financial Services and the Treasury Bureau (FSTB), HKMA, SFC, Hong Kong Stock Exchange, OCI and MPFA, to promote the exchange of information (p. 47).

The SFC and HKMA have also “entered into a memorandum of understanding[,] laying out which agency should have the lead regulator role in response to certain financial crises” (Pan, 2009: 47).

Since its inception in 1989, the SFC has been “the principal regulator of Hong Kong’s securities and derivatives markets” (Hong Kong Stock Exchange and Clearing Limited (HKEx), 2010: para. 5; SFC, 2009: 3). More specifically, the SFC’s main objectives …are to maintain and promote the fairness, efficiency, competitiveness, transparency and orderliness of the industry; provide protection to the investing public; minimize crime and misconduct in the industry; and reduce systemic risks in the industry. [The SFC also] has the statutory duties to help maintain Hong Kong’s position as an international financial centre, to facilitate innovation in financial products, and to avoid restrictions on competition (Arner, Hsu, & Da Roza, 2010: 4-5).

In 2000, the SFC “assumed responsibility for supervision of broker-dealers (member regulation) from the exchanges…as part of an overall government policy to consolidate and demutualize Hong Kong SAR, China’s exchanges… and…takes an active role in enforcing the rules” of the market (Carson, 2011: 29).

Among these exchanges is the Hong Kong Stock Exchange and Clearing Limited (HKEx), whose “self-regulatory role” is limited in scope in that it is only allowed “to
supervise compliance with its trading and listing rules, which are mostly business or operational rules” (Carson, 2011: 29). The HKEx “is the frontline regulator of all listed and prospective listed companies” (Arner, Hsu, & Da Roza, 2010: 5). The HKEx’s reluctance to relinquish authority could not withstand the combined pressures of the Asian financial crisis of 1997 (which gave government regulators the upper hand), the dramatic shift in regulatory authority in the UK from the [London Stock Exchange] (LSE) to the [Financial Service Authority] (FSA) in 2000 (the UK market had long provided inspiration and technical expertise for Hong Kong) and the upsurge in mainland Chinese listings (which prompted heightened regulatory concerns) (Jordan & Hughes, 2007: 211).

As the SFC’s role in regulating the financial markets expanded, the “HKEx’s surveillance role [became] quite limited” (Carson, 2011; 29). Consequently, the “SFC …remains responsible for supervising, monitoring, and regulating the activities of HKEx” (Arner, Hsu, & Da Roza, 2010: 5).

The development of these ad hoc regulatory agencies led commentators to characterize Hong Kong’s financial system as “fragmented” (Pan, 2009: 48). Some commentators even went as far as to describe Hong Kong’s financial system as one largely developed “through trial and error[,] and resulting in a confusing matrix of sectoral laws and agencies with many gaps and inconsistencies” (Arner, Hsu, & Da Roza, 2010: 45). To date, Hong Kong has ignored calls to reform its fragmented regulatory framework to a “more coherent system based upon specific objectives and well-defined roles” (Arner, Hsu, & Da Roza, 2010: 45; also see Pan 2009: 48).

**Brazil**

The Comissão de Valores Mobiliários (CVM) works with the National Monetary Council (Conselho Monetário Nacional – “CMN”) and the Brazilian Central Bank (Banco
Central do Brasil – “Central Bank”) to effectively regulate Brazil’s markets (BM&FBovespa, 2011: para.1). CVM is the main regulator and is “primarily responsible for regulating and overseeing the Brazilian capital markets” (BM&FBovespa, 2011: para. 4).²⁹

CVM’s key responsibilities are to oversee the activities of publicly held companies, organized-over-the-counter (OTC) markets, exchange markets, and commodities and futures markets, as well as members of the securities distribution system, such as fund managers and asset managers” (para. 4).³⁰

In an attempt at regulatory reform, “Brazil modernized the legal framework for its securities markets in 2007 when CVM, ..., issued a new regulation that created the regulatory basis for demutualization of exchanges and established new self-regulatory powers ” (Carson, 2011: 30). In 2008, Bovespa, once the largest single exchange in Latin America, “merged with BM&F, Brazil’s commodity futures exchange, to form BM&FBovespa, an integrated securities and commodities exchange” (p. 30). “While all three regulators have some regulatory authority over BM&FBovespa, …CVM is the most relevant regulator for BM&FBovespa” (BM&FBovespa, 2011: para. 5).³¹

Part of BM&FBovespa’s mandate “[a]s a securities operator… is to implement specific regulations for the registration and trading of securities in its organized market” (BM&FBovespa, 2011: para: 4).³² “With the demutualization of Bovespa, the exchange created a new entity, Bovespa Market Supervision (BSM), to perform SRO functions”(Carson, 2011: 30). “BSM’s operations and governance are fully independent of BM&FBovespa” (p. 30). BSM has a broad mandate and its

³¹ See Regulation tab in BM&FBOVESPA (2011).
self-regulation activities comprise (i) the monitoring of transactions, entities authorized to operate on the market, and organization and management by the securities market operator itself; and (ii) ensuring that the securities market operator is performing its duty to enforce compliance by securities issuers with the applicable legislation and regulations (BM&FBOvespa, 2011: para. 4).

In addition to BM&FBOvespa and BSM, Brazil used to have “two industry associations that performed important self-regulatory functions” (Carson, 2011: 31). The National Association of Investment Banks (ANBID) and the National Association of Financial Market Institutions (ANDIMA), “merged in 2009 to form ANBIMA (Brazilian Financial and Capital Markets Association)” (Carson, 2011: 31). ANBIMA is a good example of industry associations that have developed SRO functions on a voluntary basis. ANBIMA does not have a statutory mandate, and membership is voluntary, although it does have memoranda of understanding (MOUs) with the regulator, CVM, concerning its regulatory responsibilities. Currently, ANBIMA is a self-governing member organization without independent directors or formal separation of industry association and SRO functions (p.31).

ANBIMA represents “players operating in financial and capital markets” (ANBIMA, 2011: para.1). More specifically, ANBIMA “represents more than 325 institutions, among banks commercial, multiple and investment banks, asset management companies, brokerage houses, securities dealerships and investment consultants” (ANBIMA, 2011: para.1). ANBIMA also carries out self-regulatory functions, provides certification, market infrastructure and transparency services, and promotes investor education. The association has adopted codes that set rules for trading, pricing, clearing, and settlement in OTC debt markets. It has also adopted five codes that set out rules for members’ activities in investment funds, public offers, private banking, and custody, as well as certification requirements (Carson, 2011: 31).

What is unique about Brazil’s case is that it is one of the few countries which adhered to the principles of securities regulation specified by The International Organization of Securities Commissions (IOSCO) (see BM&FBovespa, 2011: 4).\textsuperscript{34} The IOSCO’s “principles of securities regulation… are based upon three objectives: [t]he protection of investors; [e]nsuring that markets are fair, efficient and transparent; and [t]he reduction of systemic risk (IOSCO, 2003: 2). Brazil has made a serious effort to ensure that its current legislation and the supervisory and regulatory bodies governing its financial and capital markets faithfully reproduce IOSCO’s recommendation in their entirety, and in some cases [,] take them to higher levels through the implementation of even more detailed and rigorous rules” (BM&FBovespa, 2011: 4)\textsuperscript{35}

**United Kingdom**

Until 1997, the U.K. “relied almost entirely on self-regulation” to regulate the financial service industry (Carson, 2011: 25-26). Some of the previous regulators include, but are not limited to the following: the Personal Investment Authority (PIA), who used to regulate firms and independent financial advisors in the insurance and investment (pension, savings, and trusts) industries (Sharingpensions, 2012: 7). The Securities and Investment Board (SIB), who regulated the activities of the SROs in the investment markets (Sharingpensions, 2012: 7). The Financial Intermediaries, Managers and Brokers Regulatory Authority, (FIMBRA), whose members used to sell life insurance, unit trust and provide investment advice to retail customers. The Life Assurance and Unit Trust Regulatory Organisation (LAUTRO), who used to regulate companies in the insurance industry (Life-Assurance.org, 2012: para.1). There was also

\textsuperscript{34} See “IOSCO’s Recommendations” tab in BM&FBOVESPA (2011).
\textsuperscript{35} See “IOSCO’s Recommendations” tab in BM&FBOVESPA (2011).
the Securities and Futures Authority, who was the principal regulator of firms in the investment markets (e.g., stocks, bonds, futures, and commodity markets) (Investment Regulation, 2012: para.1). Other major frontline regulators were “the Bank of England, which was responsible for regulating banks” and “the Investment Managers’ Regulatory Organization ... each had a role in regulating securities offerings and investment firms” (Pan, 2009: 30 emphasis added). Added to these, were the exchange SROs such as the London Stock Exchange (“in its role as Listing Authority”) and the London International Financial Futures and Options Exchange (LIFFE), who were the regulators of participating firms on these exchanges (p. 30). Like Hong Kong, the U.K. was strong in sectoral regulation, with each sector of the financial market being governed by its own regulator.

This “complex structure” of the market regulation created “tensions between the statutory oversight body and the frontline regulators” (Davies, 2004: 3). During the 1990s, new companies were “emerging in each sector of the marketplace” (p. 3). These new companies sought to define “their strategies as being deliberately different from those [of] the existing companies, and indeed marketed themselves in opposition to the incumbents,” (p. 3) “in a well defined marketplace” (Jordan & Hughes, 2007: 219). The prior “commonality of interest” between companies was no longer present, and “self-regulation” as a regulatory strategy was “significantly weakened” (Davies, 2004: 3-4). Moreover, bad market practices that were inconsistent with the rules of the financial industry, served to weaken public confidence in the regulatory system (p. 4).36 The entire

36A particular example is the “selling of personal pensions in the UK in the early [19]90s”(Davies, 2004: 4). The “FSA engaged in a massive clean-up exercise involving the payment of around £11 billion of compensation to almost 2 million mis-sold investors (p. 4 emphasis added). “The mis-selling was defined in relation to the rules in place at the time” (p. 4). It was “clear that the whole industry was operating in a way [that] was not...consistent with the rules” of the marketplace.
financial industry “needed to clean up its act”; self-regulation “proved incapable of doing that” (p. 4). Consequently, “[t]he United Kingdom government jettisoned self-regulation in response to the entry of new market players who did not play by ‘club’ rules and in an effort to raise standards across an entire industry which was no longer homogenous” (Jordan & Hughes, 2007: 220; also see Pan, 2009: 29-32).

The FSA, which was created in 1997, is an independent regulatory body that “regulates the financial services industry in the U.K.” (FSA, 2011: para1). “The FSA was set up by government” and “is responsible for the overall scope of [the U.K.] regulatory activities and powers” (para. 2). Subsequent to the FSA coming into existence, “[t]he UK government…transferred all significant powers of the former SROs to the FSA” (Carson, 2011: 26). The FSA is in charge of rule-making and enforcement, and currently “regulate[s] most financial services markets, exchanges and firms... [The FSA] set the standards that they must meet and can take action against firms if they fail to meet the required standards (FSA, 2011: para. 1).”

The new regulatory regime in the UK “represented a wholesale departure from the historical reliance on self-regulation in the … financial markets” to a more “universal financial regulator” (Carson, 2011: 26). In a release to the European Union in 2000, the FSA noted that it ‘do[es] not think that it would be appropriate to leave the setting, monitoring, and enforcement of EU legislative requirements to one or more self-regulatory organizations. Today’s markets require a more independent regulatory authority to provide all participants with a more objective approach to regulation’ (p.26).

See tab “Who we regulate” (FSA, 2011).
The U.K. was also of “the view that commercial exchanges should not assume public mandates, including regulation of participating firms” (Carson, 2011: 26). The FSA as the super regulator of the U.K. financial industry, not only streamlines industry regulation into one authority, but has the unique advantage of being in a position to set industry standards and make sure that its members comply with those standards.

**United States**

Closer to home, self-regulation in the securities industry seems likely to survive in the U.S. and probably Canada (see Jordan & Hughes, 2007: 217-219). Self-regulation as a regulatory strategy “was enshrined in the [U.S.] federal securities laws with oversight by the Securities and Exchange Commission” (Karmel, 2000: 2). Inherent in this statement is that “the SEC would oversee the SROs, but would only intervene if it determined that the SROs were failing to carry out their respective regulatory missions” (Pan, 2009: 18). However, while self-regulation as a regulatory strategy remains, there seems to be “a gradual shift in influence from self-regulatory bodies to greater government oversight and direct intervention” (Jordan & Hughes, 2007: 223). The SEC has been a major influence in the push for greater government oversight, which is captured in recent legislation and events (Carson, 2011: 24-25). When the Sarbanes–Oxley Act (SOX) was first implemented in 2002, it established an overall framework for regulating the financial market, while leaving detailed oversight to the SEC (Green, 2005: 10). The SEC in turn, allowed the SROs - NYSE and NASD (now FINRA) - to draft and implement rules that met the requirements of SOX and the SEC (p. 10). This trend seems to have continued with the recent NYSE and NASD merger.

While the SEC engages in a significant amount of rulemaking, the SEC also relies heavily on the work of SROs, which are allowed to generate rules and policies for broker-dealers and trading markets. All securities
firms doing business in the United States are members of FINRA. In addition, market rules are enforced by FINRA (in the case of [National Association of Securities Dealers Automated Quotations] (NASDAQ) and NYSE [r]egulation (in the case of the New York Stock Exchange) (Pan: 2009: 39).

While FINRA is allowed to enforce market rules, it stills receives its authority from the SEC. Since its inception, the SEC “has taken an active role in reviewing the regulatory actions” and “governance structure of FINRA” (Pan, 2009: 18; Carson, 2011: 25). This arrangement between the SEC and FINRA has been referred to as a “peculiar mix of private sector self-regulation and delegated governmental regulation” (Karmel, 2008: 1). “This mix arises because today (1) the SROs have limited independence from the SEC, (2) membership in an SRO is mandatory, and (3) SROs exercise authority in areas that the SEC effectively delegates to them” (Carson, 2011: 24). Although the U.S. has historically been seen as a country with a strong self-regulatory model, the SEC’s control over the governance structure of FINRA reduces its ability to function and operate as a fully independent SRO.

Canada

The absence of a federal regulator in Canada means that self-regulation plays a critical role in policing its securities market (Jordan & Hughes, 2007: 218). However, Prime Minister Stephen Harper and finance minister Jim Flaherty have been pushing for a “common regulator,” endowed with the legislative authority to police Canada’s securities industry (Flaherty, 2007: para. 47). At the 2007 Asia-Pacific Economic Cooperation (APEC) Summit, Prime Minister Harper called for “improved regulation” and the need to “create a common regulator” to govern the securities industry (Harper, 2008: para. 11). In February of 2008, the federal government announced that the Hockin Panel was to be put in charge with the mandate to provide recommendations that will
harmonize and better coordinate securities regulation in Canada (see Hockin Panel, 2009a). In June of 2009, the federal government announced that Doug Hyndman, the Chair of the BCSCn, would be responsible for “leading the transition to a Canadian securities regulator” (Hyndman, 2009b: para. 1)\(^{38}\). In May of 2010, Flaherty unveiled a draft bill that was sent to the Supreme Court of Canada (SCC), “where the federal government …attempt[ed] to secure a ruling that it has the constitutional authority to create a single regulator” (Howlett & McFarland, 2010: para. 3)\(^{39}\). In April of 2011, the SCC heard arguments as to whether or not the proposed *Canadian Securities Act* that would establish a single Canadian securities regulator was within the legislative authority of the federal government. In December of 2011, the SCC rejected the federal plan by ruling that “Ottawa’s proposed legislation is unconstitutional” (Hasselback and Shecter, 2011: para. 1; also see *Securities Act, 2011 SCC 66*)\(^{40}\).

\(^{38}\) The arguments against a National Securities Commission are probably as strong or stronger than the ones for a National Securities Commission (for some of the debates and discussions see Crawford Panel, 2006, Hamilton, 2007a, 2007b; Hyndman, 2006, 2007b, Urquhart, 2008; British Columbia Securities Commission, 2008; McFarland, 2008; Lortie, 2010). Commentators (Bhattacharya, 2006; MacNeil & Solomon, 2008) who herald the U.S. Securities and Exchange Commission as a model for Canada, likely spoke before the breaking news that Bernard Madoff was arrested in December of 2008, on allegations that he ran a $50 billion Ponzi scheme in the United States under the watchful eye of the SEC (Miedema & Izumi, 2008: p. F.2). Moreover, Harry Markopolos, a former “investment manager” testified in the U.S. Congress that he has been trying to bring this fraud to the attention of the SEC since 2000; but, “the SEC staff was neither willing nor able to uncover what Mr. Madoff was really doing” (Younglai & Wutkowski, 2009: D3). Allen Stanford, “the chief of the Stanford Financial Group” was accused by the SEC in February of 2009, for “conducting a massive ongoing fraud” in the sale of about $8 billion of high-yielding certificates of deposit held in the firm’s bank in Antigua” (see Krauss, Zweig, Creswell, 2009: para. 3). In March of 2012, he was convicted by a U.S. federal jury of 13 counts of fraud (Krauss, 2012: para.1). In June of 2012, he was “sentenced to 110 years in prison” (Lozano, 2012: para. 1). Also, see “Just Like With Madoff, the SEC Blew It On The Stanford Fraud” (Weisenthal, 2009).

\(^{39}\) All of the provinces, “with the exceptions of Quebec, Manitoba, and Alberta have endorsed the concept of federal legislation” to regulate Canada’s securities market (Kitching, 2009: 10). Kitching went on to note that “in the event that the federal government enacts [the ] legislation, with the support of the remaining provinces,...it remains to be seen whether Quebec, Manitoba, and Alberta would be able to operate outside a single regulator system” (p. 11).

\(^{40}\) In 2012, “[t]he federal government announced...that it will head back to the drawing board” with the “hopes to create a national body, more limited in scope and in collaboration with the
In a final report released in January of 2009, the Hockin Panel noted that the SROs “should continue to play a critical role in the regulation of Canada’s capital markets” (Hockin Panel, 2009a: 46). Likewise, the Purdy Crawford Panel on a Single Canadian Securities Regulator\(^1\) (“Crawford Panel”), reported that attempts would be made to “facilitate communications between the capital markets regulator and other Canadian financial services regulators, stock exchanges and self-regulatory organizations” (Crawford Panel, 2006: 8). Further down the Panel’s reported that SROs are listed as one of “the matters … to be addressed in the Canadian Securities Act” (Crawford Panel, 2006: 32, 34). These references suggest (at least on the surface), that SROs will continue to regulate their members and the marketplace (where applicable), but they will still hold them responsible by monitoring their activities with regulatory oversight (Hockin Panel, 2009a: 46). Further evidence that SROs in the securities industry in Canada are here to stay can be seen in the Transition Plan (2010). The Transition Plan reiterated that, “[t]he Proposed [Securities] Act maintains provisions for the CSRA to recognize these organizations and rely on them to regulate their members and participants” (Canadian Securities Transition Office, 2010: 15).

In spite of these trends, the critical question for regulators is how to maintain “the appropriate balance among all affected factions” involved in implementing regulatory standards (CFA, 2007: 2)? The “balance” it is argued, “must nurture the positive aspects of self-regulation,” while not giving “the self-regulated members so much discretion that provinces, that would play a role in monitoring long-term risks to financial markets” (Young, 2012: para. 1 & 2).

\(^1\) The Crawford Panel was established in May of 2005, by the Ontario Minister “responsible for securities regulation in the province” (Crawford Panel, 2006: 1). Working independently from government, “the “Panel [was] charged with recommending a model for a common securities regulator for Canada” (p. 1). “The Panel’s terms of reference are to recommend a securities regulatory framework that features a common securities regulator, a common body of securities law and a single fee structure” (p. 1).
they will, if left unchecked, ultimately corrupt the system by favouring their own interests over the public good” (p.2).

**Arguments for Self-Regulation**

**Public Interest**

It is argued that “the granting of self-government...can only be justified as a safeguard to the public interest” (McRuer Report, 1968 as cited in Brockman & McEwen, 1990:3). To safeguard the public’s interest and maintain the general integrity of a system of self-government, an SRO would be required to “investigate and discipline the unethical behaviour of its members” (p. 3; see also CFA, 2007: 2). But, while the “‘protection of the public’ interest is used as a justification for the existence of SROs’, legal scholars have charged that “the call for self-regulation comes from the professions themselves and not the vulnerable public” (Brockman & McEwen, 1990: 3).

**Industry Expertise**

Another plausible argument in favour of SROs is that industry experts are more informed about the operations of their occupations, and are equipped with “specialized knowledge” to police their own members more effectively than the state (Brockman & McEwen, 1990: 3). This assertion is important when dealing with complex industries. According to the International Organization of Securities Commissions (IOSCO),

> [s]elf-regulatory bodies have a keen interest in and a thorough knowledge of [the] industry and the regulatory framework within which they operate. In an environment characterized by a variety of different markets and different types of participants, a specialized and thorough knowledge is very beneficial (2007: 4).
The IOSCO went on to note that “[a]n SRO’s expertise, experience, authority and commitment also will allow it to design, implement and evaluate the compliance programs necessary to be effective” (p. 4). Equipped with industry expertise and coupled with a plethora of codes and rules that need to be monitored, industry regulators are in a better position to effectively enforce regulatory standards than state regulators (see Braithwaite, 2002: 135). Put another way, “it will generally be more efficient to rely on an SRO’s extensive knowledge, experience and expertise rather than trying to reproduce it within the statutory regulator” (IOSCO, 2007: 4). As such, industry regulators’ specialized knowledge of their industry’s culture, makes them more effective investigators than government regulators, who are “forced to be generalists” in the regulatory process (Braithwaite, 1982: 1468).

Efficient Regulation

The flexibility of SROs enhances their ability to detect and address problems in rapidly changing industries (IOSCO, 2007: 6-7; also see Braithwaite, 1982: 1468 -1470). SROs are “better informed about business practices and the potential for misconduct (organizational ‘hot spots’)” (Simpson, 2002: 100). They are better positioned to “tailor their rules and surveillance techniques to the specific characteristics of [a particular industry]” (IOSCO, 2007: 12). “Others assert that self-regulation is an easier and cheaper system through which the public can seek a remedy, and that SROs can set and enforce higher standards than government regulation or regulation through criminal or civil proceedings” (Brockman & McEwen, 1990: 3). Given this versatility, it can be

42 See endnote number 7 in (Braithwaite, 2002: 135). In other works, Braithwaite and his colleagues provide empirical evidence to support this claim. See John Braithwaite (2002); John Braithwaite and Brent Fisse (1983); Fisse and Braithwaite (1987); and Ian Ayres and John Braithwaite (1992).
argued that “SROs by their very nature have greater flexibility to adapt regulatory requirements to a rapidly changing ... environment” (IOSCO, 2007: 3).

**Effective Compliance**

Perhaps a more formidable argument in favour of SROs is “that they enforce standards which would not otherwise be enforced” by the state (Brockman & McEwen, 1990: 3). Fiscal pressures and general incompetence invariably prevent government regulators and the criminal justice system from “regularly checking for professional and occupational misconduct, such as crooked bookkeeping, occupational safety hazards, environmental quality lapses and faulty product designs” (Braithwaite, 1982: 1467; also see Rosoff, Pontell, & Tillman, 1998: 204-236). Such misconduct can be prevented if industries and professional associations, in general, take on some or all of the “legislative, executive, and judicial regulatory functions” as part of their regulatory mandate (Ayres & Braithwaite, 1992: 103). In principle, self-regulation purports to do this. As legislators, industry regulators “are able to devise their own regulatory rules; as self-regulating executives, [industries are in a better position] to monitor themselves for noncompliance [with these rules]; and as self-regulating judges, [industry regulators] can punish and correct episodes of noncompliance” (p. 103). Consequently, self-regulation is able to achieve greater inspectorial depth, because they are better able to “scrutinize a wider variety of behaviour and thereby ensure a higher standard of conduct than if the public had to rely on government regulation” (Brockman & McEwen, 1990: 3).

**Arguments against Self-Regulation**

**Lenient Enforcement**

Despite the advantages of self-regulation, the evolving nature of some industries
and professions makes “these justifications for self-regulat[ion]... ring somewhat hollow” (Jordan & Hughes, 2007: 212). By far, the most common criticism is that SROs are “too lenient on their members, and rather than widening the net of social control as they claim, they are accused of ‘funnelling out’ so many complaints that they are ineffective in controlling” their members (Brockman, 2004: 55-56). Brockman notes two aspects to this criticism. First, “professional SROs are not designed to, or do not, deal with the majority of clients’ complaints, which are about quality of professional services, not misconduct” (p. 56). Second, when “a complaint does make it through the SRO’s disciplinary system, the penalty is so light as to amount to nothing more than a ‘slap-on-the-wrist’” (p. 56).

This last point was reinforced by a Toronto Star series on white-collar securities crime enforcement in Canada. The reporter notes that “cases not pursued by criminal authorities can easily slip through the cracks, though in some cases wrongdoers will get a regulatory wrist-slap for criminal offences more deserving of jail time” (Hamilton, 2007a: para. 37).

**Deflects Criminal Complaints away from the Justice System**

Brockman (2004) identifies another criticism of self-regulation. It is alleged that “self-regulation deflects criminal complaints away from the criminal justice system, protecting members from criminal prosecution” (Brockman, 2004: 57). Central to this argument is that, “self-regulating professions take legitimate complaints of crime and have them ‘funnelled away’ from the criminal justice system” (Brockman, 2004: 57). The lack of urgency to refer white-collar securities crime cases to the criminal justice system, coupled with the “conflicts inherent in having the regulated regulate themselves,” makes self-regulating systems “ultimately impractical at best and grossly self-serving at worst” (CFA, 2007: 3).
Inability to Adapt to Changing Market Structure

A somewhat parallel but hardly synonymous criticism comes from those who charge that the evolving nature of the financial industry makes it very difficult to regulate through self-regulation (see Pritchard, 2003: 32-39; CFA, 2007: 3 & 13). Over the last decade, the advancement of technology has caused the securities markets to become more electronic (CFA, 2007: 3). The access to high-speed “internet has transformed the availability of data and methods of trading” (p.3). In addition, “low-cost global transfers of funds have brought about changes that are straining the capacity of …[the] current self-regulatory system to monitor itself” (p.3). This problem is compounded by the fact that SROs in the financial industry are still reflective of older market structures, and have yet to build and staff their operations with the expertise needed in order to operate in a sophisticated and well-integrated securities market (p.3). This has left SROs bereft of the technical expertise needed to adequately police and enforce industry standards (p. 3). Proof of this inefficiency has already been shown in “the spate of government-induced litigation and enforcement cases involving members of established SROs, who have been charged with violating fundamental rules of practice on which the SRO system is based” (p.3).

SROs and Industry Regulation

What we know of self-regulation has generally been applied to study other industries under a variety of names – de-regulation43, co-regulation44, responsive regulation45, meta-regulation46, and enforced regulation47 (Brockman, 1998: 591). A lot of

43 See Ayres & Braithwaite (1992) and Braithwaite (2001).
44 See Hutter (1997).
45 See Braithwaite (2002).
work has been written about how corporations can effectively regulate themselves (See Braithwaite, 1984, 1985a; Fisse and Braithwaite 1987; 1993; Braithwaite, Makkai, Braithwaite, and Gibson, 1993; Tyler and Degoey, 1996; and Murphy, 2004). There are also studies that “examine the politics of regulatory legislation and rule making” (see Bernstein, 1955; Mitnick, 1980; Wilson, 1980; Bryer, 1993 as cited in McCaffrey & Hart, 1998: 8). Others such as Braithwaite and Fisse (1983) and Rees (1988; 1994), look at how industries move away from command-and-control regulations, to regulations that give the employees the opportunity to be partners in the regulatory process.


**SROs, Securities Commissions and Securities Regulation**

While SROs are ubiquitous in their usage, there is a paucity of scholarly work that documents their effectiveness in securing compliance with law and ethical standards in the securities industry. Most of the work that has been assembled to date focuses on securities fraud enforcement by the securities commissions and police forces. The

---

47 See Braithwaite (1982).
following section discusses these studies and their relevance to SROs in the larger context of securities regulation.

One of the first studies to look at securities crime enforcement by a national regulator is Shapiro’s (1984) ethnographic account of the SEC. Through a “multifaceted methodological approach” that involved a combination of direct observations, formal and informal interviews with SEC’s personnel, and an examination of “526 randomly selected files…that covers the years 1948 to 1972,” Shapiro was able to gain insight into how the SEC detects, investigates, and prosecutes white-collar securities crimes (Johnson & Leo, 1993: 72-73, 75). While the SEC drew on “both criminal and civil, as well as administrative enforcement mechanisms,” Shapiro noted that the SEC was doing a poor job in referring cases for criminal prosecution (Shapiro, 1985: 182). According to Shapiro,

out of every 100 suspects investigated by the SEC, 93 have committed securities violations that carry criminal penalties. Legal action is taken against 46 of them, but only 11 are selected for criminal treatment. Six of these are indicted[,] 5 will be convicted and 3 sentenced to prison (Shapiro, 1985: 182).

Shapiro noted that, “the experience of litigation was relatively rare” for civil offenders: “80 percent settled charges by consent, 12 percent litigated, and 8 percent were enjoined by default” (Shapiro, 1984: 156).48 She went on to argue that, “the outcomes of administrative proceedings were favourable to SEC enforcers” (p. 157). “For about a third of the parties named in [the administrative] proceedings, charges were litigated

48 The SEC’s trend to settle rather than litigate civil cases continues. Recently, the SEC settled a civil suit with Bernie Madoff, “which will force him to pay a civil fine and return money raised from investors” (Gordon, 2009: 1). Madoff also “waive[d] an indictment and plead guilty to criminal charges” (McCool & Graybow, 2009: E3). Madoff was later sentenced to a “maximum 150-year term in prison” (Neumeister & Hays, 2009: para. 5).
through hearings” and “61 percent settled charges by consent, and 7 percent by default” (p. 157).

Shapiro’s (1984) work, while dated, is still relevant to securities enforcement. At the time of her study, it was seen as “impractical and counterproductive” to subject every securities law violation to “formal proceedings” (Shapiro, 1984: 147). As such, the SEC had discretion to refer cases to other agencies49, some of them being the SROs (p. 147). This being the case, Shapiro noted that, “about a third50 of the cases referred were sent to self-regulatory [organizations]"51 (p. 147).

McCaffrey and Hart (1998) examined the regulatory activities of the SEC, NASD, and NYSE, and pointed out that the SEC “increased its own attention to broker-dealer firms in the 1980s and 1990s” and consequently, “directed the SROs to do the same” (p. 78). It is possible that the combination of referred cases (Shapiro, 1984: 147) and the increased attention given to broker-dealer firms, combined to “intensify” the regulatory activities of SROs in the 1980s and 1990s in the U.S. (McCaffrey & Hart, 1998: 78). Given that the SROs were “backed by the SEC…their regulatory programs became more severe” (p. 78).

McCaffrey and Hart (1998: 17) noted three patterns of enforcement against individuals and firms. First, in terms of disciplinary actions for individuals,

49 The “other agencies” that Shapiro referred to in her study are “federal regulatory agencies, the Justice Department, state securities commissions, private social control or self-regulatory agencies (the stock exchanges, the Better Business Bureau, and the NASD), [and] foreign agencies (Shapiro, 1984: 55).
50 Shapiro (1984) did not provide any other information as to where the one-third of cases that were referred to the SROs came from. One can only assume therefore, that her reference to “a third” of the cases being referred is from the 526 randomly selected cases that were used in her study.
51 Here Shapiro is referring to “private social control or self-regulatory agencies (the stock exchanges, the Better Business Bureau, and the NASD) (see Shapiro, 1984: 55).
firms with larger retail operations, such as Merrill Lynch, Shearson, Prudential, Paine Webber, Smith Barney, and Dean Witter, [were] involved in many proceedings, usually as a current or former employer of a respondent” (p. 17). Firms such as Salomon, Goldman Sachs, Nomura, or Bear Stearns – which deal primarily with institutional investors - [were] involved in far fewer disciplinary cases” (p.17).

According to McCaffrey and Hart, one plausible reason for the larger retail operations being involved in many proceedings, is that they “employed or formerly employed brokers facing customers’ complaints” (Pp. 153 & 155). Firms that dealt “mainly with institutional investors were involved in fewer cases because institutional investors usually are powerful enough to deal with the firm informally should problems arise” (p. 155). The implication from these findings is that the SROs’ disciplinary mechanisms may not be stringent enough, in that they allowed broker-dealers to continue working in the industry while under investigation. Choosing to deal with firms informally is probably an indication that institutional investors do not identify with the SROs’ enforcement policies, and prefer to settle the case with the firm instead of the SRO (see McCaffrey & Hart, 1998: 155-157).

Second, McCaffrey and Hart (1998) noted that, “firms whose employees tend to have many disciplinary problems do not necessarily have heavy sanctions themselves, nor does a firm with few[er] cases necessarily avoid heavy sanctions” (p. 17). For example, “Merrill Lynch had numerous employees involved in disciplinary actions, but…faced relatively less regulatory difficulty than some institutionally oriented firms” (p. 155). Merrill Lynch being one of the more popular and larger member firms of the SROs, seems to benefit from its position. Given this outcome, it appears that NASD and the NYSE paid little or no attention to the fact that Merrill Lynch was involved in previous disciplinary actions in their penalty hearings. One can only speculate then, on whether the size of a company influences sanctions and the roles that aggravating (for example
prior records) and mitigating factors play in the imposition of penalties.

Third, in terms of disciplinary actions for the firm itself, the authors noted that the fines being handed out by the SEC, NYSE, and NASD varied “within [the] types of business” that the firms were involved in (McCaffrey and Hart, 1998: 17). “Of the firms with extensive retail operations, Merrill Lynch and Smith Barney faced fewer regulatory sanctions than Shearson, Prudential Securities, and Paine Webber” (p. 17). Generally, “firms dealing primarily with institutions avoided major fines in the period, with some exceptions” (p. 17).

DeMarzo, Fishman, and Hagerty (2005: 687) “analyze[d] one regulatory task of an SRO [the NYSE], enforcing antifraud rules so agents will not cheat customers.” More specifically, DeMarzo et al. “model contracting/enforcement as a two-tier problem” (p. 687). First, the authors note that “an SRO chooses its enforcement policy,” that is, “the likelihood of an investigation and a penalty schedule for fraud” (Pp. 687-688). Further, the authors assume that the SRO’s “objective is to maximize the welfare of its members, the agents” (p. 688). The authors show that the SRO is more likely to choose “a … lax enforcement policy,” meaning “less frequent investigations” … than what customers would choose” (p. 687-688). Second, DeMarzo et al. “also consider government oversight, meaning that the government observes the SRO’s enforcement policy and can then choose to do its own enforcement” (p. 689). The authors “assume [that] the government’s objective is to maximize customer expected utility” (p. 689). DeMarzo et al. found that “the threat of government enforcement leads to more aggressive enforcement by the SRO” (p. 689).

However, this calculated approach to enforcement by SROs in the securities industries exposes “the SROs and member firms to hard questions when major
violations surface" (McCaffrey & Hart, 1998: 43). Government regulators can most certainly scrutinize the SRO and inquire on “how decisively the…SRO remedied the violation and whether the case illustrates a wider breakdown in the …SROs [disciplinary] system” (p. 43). In such a scenario, “government oversight [whether it is central like the SEC or decentralized as in the provincial securities commissions in Canada] of self-regulation can benefit customers by leading the SRO to engage in more aggressive enforcement” (DeMarzo et al., 2005: 702). The SRO would retaliate proactively by “choos[ing] an enforcement policy that is just aggressive enough to pre-empt the government from doing its own enforcement” (p. 702).

Bhattacharya (2006) compared the enforcement of securities laws between the SEC and OSC, and found that the SEC “enforces securities laws much more vigorously than the [OSC]” (Bhattacharya, 2006: 3). Bhattacharya notes that when the data is “scaled by the size of the stock market …the SEC prosecutes 10 times more cases for all securities laws violations than the OSC prosecutes,” and prosecutes “20 times more cases involving insider trading laws than the OSC” (p.3, 22). He also notes that, “the SEC resolves the [insider trading] cases faster than the OSC, and fines 17 times more per insider trading case than the OSC does” (p. 3). The average time it takes the SEC to resolve an insider trading case is 3.0 years compared to the OSC’s 3.9 years (p. 22).

Bhattacharya’s (2006) results must be viewed in the context of the time period in which the study was done. As seen in Shapiro (1984) and McCaffrey & Hart’s (1998) studies, the Unites States’ SROs were given a more substantial role in securities enforcement in the 1980s and 1990s. However, events at the beginning of the 21st Century questioned the effectiveness of United States’ SROs in regulating the securities market. Beginning in 1999 and ending in late 2001, a series of corporate scandals (“the
scandals”) sent the U.S. economy into a mini recession. Both the SEC and the SROs (NASD and NYSE) responsible for policing America’s securities markets were seen as ineffective regulators (Gray et al., 2005: 2). Bhattacharya’s (2006) report for the Task Force seems to ignore this point and gives the impression that the Unites States’ two-tiered model of securities regulation, while not perfect, is doing a reasonable job in the enforcement of securities law violations.

The SEC’s increased enforcement of securities and trading laws reported by Bhattacharya (2006), can be attributed to a number of factors. Of particular interest is the time interval covered by Bhattacharya’s (2006) study. Bhattacharya’s (2006: 21) study was based on data collected from 1997 to 2005 for the OSC and from 1995 to 2005 for the SEC. When one takes a closer look at Bhattacharya’s (2006) data, it is evident that the number of litigations carried out by the SEC increased dramatically in 1999 and maintained that approximate level in the following years (p. 23). It should also be noted that it was around 1999/2000 that news concerning the scandals was emerging. Given the public outrage that occurred after the scandals, it makes intuitive sense to view Bhattacharya’s study with the scandals in mind. The data presented by Bhattacharya (2006) shows that the number of insider trading cases that the SEC dealt with increased from 21 in 1998 to 47 in 1999 and up to 57 in 2003, before they started to decrease (38) again in 2004 (Bhattacharya, 2006: 23). With the exception of 1996, all of the other years for which data is reported shows the number of insider trading cases to

---

52 Between 1999 to 2001, corporate America witnessed an unprecedented level of accounting and corporate frauds, involving some of the largest corporations in the United States (U.S.). Executives from Enron, Tyco, WorldCom, Global Crossing, Quest, Aldelphia, and ImClone, were all involved in corporate scandals that included “insider trading, fraudulent accounting, fictional business entities, bribery, lavish executive perquisites, and outright theft” (Bradford, 2007: 1).

53 The U.S. model is described by Jordan and Hughes as one that is characterized by "overlapping oversight and shared responsibilities" (2007: 20).
be in the teens and 20s (p.23). As such, one plausible explanation for the increase in the SEC’s enforcement as documented by Bhattacharya (2006) can be attributed to the scandals, which led the SEC to intensify enforcement, and not necessarily from its model of “overlapping oversight and shared responsibilities” (Jordan & Hughes, 2007: 223) with the SROs.

One must also take stock of the fact that Bhattacharya’s data is solely based on the incident of public enforcement between the SEC and the OSC. Without a doubt, “the incidence of public enforcement actions in Canada is significantly lower than that observed in the United States” (Lortie, 2010: 30). Lortie argues that

\[ \text{the ratio of public enforcement actions between both countries is 18.0 compared to a U.S./Canada ratio of 10.9 for population and 11.4 for total domestic market capitalization (2008).} \]

Such a ratio is often presented as proof that the Canadian securities regulatory regime is not fulfilling its enforcement role, a shortcoming which in their view can only be corrected by the takeover of securities regulation by the Federal Government. The argument is potent but flawed (p. 30).

According to Lortie, researchers “who have engaged in international comparisons of enforcement intensity hold the view that the results of such comparisons are problematic in several ways” (p. 30). One of the problems noted by Lortie is that “[l]awfulness of populations may vary” from country- to- country (p.30). Lortie went on to argue that there are 1.6 million adults incarcerated in the United States compared to 33,100 adults in Canada (a ratio of 48.3 to 1). Despite this huge discrepancy, no one can pretend that Canada is a less law-abiding society or that our cities are more dangerous places to live. Countries may structure their regulatory oversight differently, one emphasizing ex-ante supervision[,] while the other relies on ex-post sanctioning and litigation. There exists abundant academic literature arguing that the U.S.

---

54 See Lortie (2010:30) for a table showing the incident of public enforcement action between Canada and the United States.
securities regulation is excessively tilted toward enforcement actions (p. 30).

While the incident of public enforcement of securities crime in Canada can be classified as being low when compared to the U.S., Canada outperforms the U.S. when other indicators are used to measure securities regulation. As a matter of fact, more recent "[c]omparisons made by international institutions rank Canada amongst the best with respect to the quality of securities regulations and investor protection" (Lortie, 2010: 5). According to Lortie,

Canada was ranked second in terms of the quality of overall securities regulation in the OECD 2006 report “Going for Growth”, ahead of the USA (4th), the UK (5th) and Australia (7th). Compared to 178 economies, Canada was ranked 5th in terms of investor protection in the World Bank *Doing Business 2008* Report, ahead of the United States (7th), the United Kingdom (9th) and Australia (51st) (p. 5).

What is important about these findings is that Canada ranks ahead of both the U.S and the U.K in “overall securities regulation,” and “investors protection.” Canada is often compared to both the U.S and the U.K, because they each have a single federal regulator. Furthermore, the finance ministers of Alberta and Quebec, two provinces that are diametrically opposed to a single federal regulator, argued that “the current system is recognized as one of the best in the world” (Morton & Bachand, 2010: para. 4). Merton and Bachand note that “Canada has vibrant, healthy, safe, and globally-competitive capital markets that continue to attract record levels of investment from around the world” (para. 4). Thus, if one was to look at the “quality of overall securities regulation” as a measure of efficiency, Canada “ranks with the best” (Lortie, 2010: para. 8).

In responding to the argument that Canada’s regulatory system is “fragmented” comprising of “13 regulators and 13 sets of rules,” Morton and Bachand note that
“Canada does have 13 securities regulators, but nobody actually deals with 13
regulators and has not for at least one decade” (Morton & Bachand, 2010: para. 6-7).

They contend that

[0]ver the past 10 years, the provinces and territories have harmonized
and streamlined securities laws, rules and standards, and created what is
known as a passport system. As a result, market participants now only
have to deal with one provincial regulator to have access to markets
across Canada…Canada’s regulatory regime already is a national
system, just not a centralized system. All of this meets the needs of the
local market and local industry, while ensuring international access to a
robust national economy (para. 8-9).

Therefore, in comparing the SEC with the OSC, and thereby making inferences that
Canada’s securities enforcement is “third world” (Hamilton 2007a: para. 13),

Bhattacharya (2006) is missing a more fundamental point in his study. The enforcement
records of the OSC cannot be equated to mean that the entire Canadian securities
regulatory system (which includes the other provincial commissions, SROs, and the
RCMP) is “third world”. Granted that the OSC “regulates over 80 per cent of securities”
in Canada (Flaherty, 2007: para. 49), its enforcement records do not represent the
enforcement records of the other provincial securities commissions and the IDA. Yes,
the RCMP is not doing a good job in policing securities fraud; yes, the IDA may not be
dealing effectively with investors’ complaints; and yes, the OSC has been consistently
cited for weak enforcement (see Hamilton, 2007a, 2007b; Baines, 2008; MacNeil &
Solomon, 2008); but to label Canada as “a first-world country with second-world capital
markets and third-world enforcement”55 (Hamilton 2007a: para. 13) on a study based on
the OSC’s enforcement data, only serves to mislead readers.

55 This statement was made by Utpal Bhattacharya, and was referenced by Hamilton (2007a).
SROs, Criminal Justice System and Securities Regulation

Sliter (1994) examines the role of the RCMP in securities fraud enforcement and charges that the RCMP’s officers are ill-equipped with the skills required to tackle securities fraud cases (see Sliter, 1994: 95-108). Sliter’s (1994) study, while dated, is still relevant to securities fraud enforcement in Canada. At the time of writing, Sliter notes that the “RCMP has tried to police a complex and specialized field with a very generalized policing strategy” (Sliter, 1994: 108). He puts forward a few reasons for this phenomenon. First, the RCMP “have staffed the policing positions with ‘generalist’ police officers and followed this up with little or no securities industry related training” (p. 108). Second, the RCMP “maintained a transfer policy that was, and is, a direct impediment to effective securities fraud enforcement” (p. 108).

It seems as though the problem of high turn-over rates of RCMP officers being an impediment to securities enforcement, has not waned since Sliter’s (1994) work. A report by Nick Le Pan notes that, “of the 71 [Regular Members] (RM) that have held IMET positions, 24 have left the program56 since its inception in 2003” (2007: 39 emphasis added). “Of those, some 8 had less than 20 years service… [and] over half this turnover moved to other RCMP sections” (p. 39). Moreover, “all the Officers in Charge of IMET units (OICs) that started the Program have left (within four years) and in three locations the program will be on its third OIC soon” (p. 39). The result of IMET’s high turnover rate is “discontinuity, which can cause delays, and a dearth of senior officers equipped to supervise and push through investigations” (Hamilton, 2007b: para.

56 Throughout his report, Le Pan (2007) refers to IMET as “the Program.” While this was not explicitly stated, Le Pan in his Report to William Elliott, the Commissioner, notes that “pursuant to his mandate, he completed his review of the Integrated Market Enforcement Teams (IMETs) and is pleased to submit his report and recommendation to enhance the program” (Le Pan, 2007: 2).
To address the issue of the RCMP being “generalists” in a specialized field, when the IMET started in 2003, their plan “was to combine the resources of the RCMP, city police, provincial securities regulators, federal prosecutors and private forensic accountants for a coordinated assault on securities crime” (Baines, 2008: para. 10). To accomplish this task, “the first IMETs were established in 2003 in Toronto and Vancouver” (RCMP, 2006: 3). Along with “a national support centre in Ottawa, the program now has nine teams across the country: three in Toronto; and two each in Montreal, Vancouver and Calgary” (p. 3). In 2011, eight years after IMET’s inception, twenty-six individuals were charged, and only five were convicted (RCMP, 2011: para: 16).

Hamilton (2007a, 2007b) carried out an investigation of the OSC’s enforcement of securities law violations and charged that both the OSC and criminal justice system are ill-equipped to tackle securities fraud. In particular, Hamilton “catalogued a quagmire of issues” ranging “from ill-equipped prosecutors and inexplicable delays, to an overarching defeatist mentality that is sapping confidence from a fragmented system perceived as weak” (Hamilton, 2007b: para. 2). Hamilton went on to argue that legislative handcuffs, accountability by the provincial regulators, inept prosecutors and lawyers, and a lack of judges trained in securities law enforcement are some of the causes that lead to weak white-collar securities crime enforcement in Canada (Hamilton, 2007b).

To address this problem, Le Pan recommends that, “the RCMP consider creating the possibility of paying retention pay to IMET Commissioned Officers… who commit to staying in their position for, say an additional two or three years, and where there is a demonstrated need for continuity” (Le Pan, 2007: 50).
While these studies give some insight into the enforcement of securities crime by SROs in the United States, the OSC, and the RCMP, little if anything is known about the enforcement practices of the IDA. Moreover, there is a dearth of information on the disciplinary process of registered individuals and the background of the investors.\textsuperscript{58} My study will attempt to address this gap by not only looking at the enforcement activities against Member firms and registered individuals, but also the demographics and backgrounds of investors. My contribution to the literature is an analysis that combines multiple methods of data collection that will allow for an examination of the enforcement of complaints by the self-regulatory body at the front-end of Canada’s three-tier regulatory system - the IDA.

\textsuperscript{58} Boyd’s (2005) study is the only Canadian study to date that looks at the background of investors who are likely to be victims of securities fraud.
Chapter 4: The Evolution of the IDA – From Self-Discipline to Self-Regulation with Oversight

Self Discipline

The development of the IDA can be characterized as one that evolved from pure self-regulation to mandated self-regulation (Coleman, 1989: 506). The foundation of the Association's mandate began in 1913, when securities trading firms that were previously responsible for disciplining their members, got together and created the Bond Dealers section within the Board of Trade of the City of Toronto (p. 508). In 1915, when the Minister of Finance “announced his first war loans ... he did not even bother to consult” with the bond dealers (Armstrong, 1997: 83). “When the results came in from the second loan,” the Minister noted that, “more than three-quarters of the applications received,” came “from the bond dealers” (Coleman, 1989: 508-509). To “assist in future war loans,” the Minister encouraged the Bond Dealers section of the Toronto Board of Trade to join with bond dealers from across the country, “to form their own association” and “assist in the distribution of war bonds” (Coleman, 1989: 509; Sorell, Nicholas, Federico, 2003: 65).

In 1916, the Bond Dealers Association of Canada (the “BDAC”) was formed and opened its doors to “dealers, trading in bonds and any other security” (Armstrong, 1997: 84; Sorell et al., 2003: 65). The objective of the Association was to “improve the savings and investment processes and provide protection for ... investor[s]” (IDA, 2002: para 12). More specifically, the Association was established

59 The title and sub-headings used to trace the evolution of the IDA was taken from Coleman’s (1989) article (see Coleman 1989: 508-520).
to promote the general welfare and influence of bond dealers, financial institutions and investors generally interested in Government, municipal, and corporation securities; to secure united protective action and to cooperate with municipal and other corporations in regard to legislation and sound financing; to afford opportunity for discussion and personal exchange of views on subjects of importance to the financial and commercial interests of the Dominion of Canada; and to afford mutual protection against loss by crime (Coleman, 1989: 509).

Initially, it could be said that the Association existed in name only. “Its members … were not regulated by any Canadian securities legislation or, in any meaningful sense, by the BDAC itself” (Sorell, 1994 as cited in Sorell et al., 2003: 65-66). Even though there was a constitution that summoned the executive committee to discipline its members, “the [A]ssociation was scarcely involved in regulating members’ behaviour” (Coleman, 1989:509). The Association’s “staff was minimal” and had a “constitution [that] provided the executive committee with the power to summon any member whose behaviour it deemed to be detrimental to the interests of the [A]ssociation” (p. 509). This “provision” was “unexceptional” since “most Canadian trade associations had…a similar clause where the emphasis is on protecting the [A]ssociation and its reputation rather than the public” (p. 509-10). Securities firms were left at their peril to discipline employees and ensure “proper business conduct” (p. 510).

Pure Self-Regulation

Beginning in the late 1920s, securities regulation began to change (Coleman, 1989: 510). Responsibilities shifted from individual firms monitoring themselves, to “pure self-regulation” (p. 510). Pure self-regulation entails the development of “norms” that are “used, and enforced by industry organizations” (p. 506). Though not mandated, “the state may consult these organizations, whether stock exchanges or associations, from time to time on related policy issues” (p. 506). However, this type of self-regulation had
its limitations and hardly “touched [OTC] markets” (Armstrong, 1997: 6). Worthless stocks were being “peddled by smooth talking conmen,” to unsophisticated investors who all wanted a share in the market (Pp.6-7). Public pressure soon led to the creation of the U.S. type Blue Sky laws in Canada (p. 7). 60 Blue Sky laws were implemented in many Canadian provinces “that empower[ed]…officials to vet the quality of new offerings in order to protect investors” (Armstrong, 2001: 6). In response to the Blue Sky laws, in 1923, the Association “established a Vigilance Committee” whose “mandate was to detect sellers of worthless securities and to educate the public about investing” (Sorell et al., 2003: 65).

A number of significant changes occurred in the years to follow, which affected the way the Association did its business (Coleman, 1989: 511). In 1924, the Association changed its name to the Investment Bankers Association of Canada (the “IBAC”) (Armstrong, 1997: 109). In 1928, the government of Ontario implemented the Ontario Securities Fraud Prevention Act (Armstrong, 1997: 135). The aim of the Act was “to control traders in securities and hence had direct relevance…for the IBAC” (Coleman, 1989: 510). In 1929, the IBAC “introduced stringent membership requirements to fill the void in the Ontario Securities Fraud Prevention Act, which included a registration requirement for brokers and salespeople, but did not establish any standards” (Sorell et al., 2003 65-66). “Membership in the [A]ssociation was made contingent upon firms having at least two years [of] experience in the industry and the recommendations of two existing members in good standing” (Coleman, 1989: 511). More importantly, the Association “revised its disciplinary policy” and shifted its emphasis “from behaviour

60 The Blue Sky laws were laws that were passed in each state in the U.S. to regulate securities trading and prevent fraud (See Alvarez & Astarita, 2001). For a discussion on the origins of the Blue Sky laws in the United States and Canada, see Mahoney (2001) and Armstrong (1997).
deleterious to the Association to inappropriate business conduct whatever the impact on the Association” (Sorell et al., 2003: 66; Coleman, 1989: 511). This was done to “actively enforce securities legislation in an attempt to pre-empt more intrusive state regulation” (Sorell et al., 2003: 66). However, the Association’s efforts to avoid state intrusion were short lived. When the stock market crashed in 1929, it was “blamed upon misconduct by insiders and a number of prominent brokers were arrested and convicted of criminal offences” (Armstrong, 1997: 7). To avoid the reoccurrence of such scams, the OSC was formed in 1930 and created “a new version of the Securities Fraud Prevention Act” (Armstrong, 1997: Sorell, et al., 2003: 66).

Having abandoned the Blue Sky laws, the new version of the Act became “a model for all the provinces” in Canada, with the exception of New Brunswick (Coleman, 1989: 510). In addition to giving the government more “power to clamp down on dishonest practices,” the Act required that all firms under the Association’s umbrella needed to submit annual audited financial statements to the Commission for verification (Armstrong; 1997: 141; Sorell, 1994 as cited in Sorell et al., 2003: 66). The IBAC however, found this to be an added burden and was successful in obtaining “an exemption from this provision for Association members,” because the requirement “places an increased responsibility on the Association to see that proper standards are maintained” (Coleman, 1989: 511 emphasis added). The IBAC however, “was forced to negotiate with the Ontario government regarding its supervision of the industry” and “eventually” extracted from the OSC, “a commitment to industry disciplinary control rather than government regulation” (Sorell et. al., 2003: 66). This stage in the IDA’s evolution process “was a period of limited but pure self-regulation in the sense that the initiatives were taken by the Association and…were implemented on its own without any delegation of state authority” (Coleman, 1989: 511).
Negotiated Self-Regulation

The early 1930s saw the emergence of a period of negotiated self-regulation (Coleman, 1989: 511). Negotiated self-regulation occurs when “[t]he industry voluntarily negotiates the development, use, and enforcement of norms with an outside agency, whether government or consumer” (Coleman, 1989: 506). The “[i]ndustry organizations are formally incorporated into the processes, making relevant policy, and becom[ing] the instruments for disciplining firms” (p. 506). By now, the Ontario government was taking a leading regulatory role in the securities market, which forced the Association “to negotiate the terms of industry governance” with them (Armstrong, 1997: 213; Coleman, 1989: 511). The OSC wanted to “institute some sort of examination for members and sales persons to ensure they had adequate expertise,” and have a “voluntary audit system” in place that would make members more transparent to the public (p. 512). It was clear from these recommendations that the OSC was of “the opinion that if the Association were to assume some disciplinary control over its members, the investment banking industry would be much more efficiently governed than if [they] were to promulgate any number of statutory regulations” (p. 512 emphasis added). The OSC’s position was more in tune with the “philosophy of governments” during the time that “industry self-regulation is the preferred mode of industry governance, but state regulation will to be used if industry fails to assume this responsibility” (p. 512).

In 1934, the Association changed its name from the IBAC to the IDA (Armstrong, 1997:373). In 1937, the Association, responding to pressures from its members who feared that the newly formed (1934) Securities and Exchange Commission in the U.S. would increase government regulation, proposed an amendment to its constitution (Sorell et al., 2003: 66; Armstrong, 2001: 7). The main objective of the proposed
amendment was to allow the Association to “monitor” its “members’ internal financial affairs” (Coleman, 1989: 512). The Association had hoped that these amendments would “stave off” excessive “government regulation” (Sorell et al., 2003: 66). Unfortunately, “unsavoury market practices” such as “high-pressure share selling, insider dealing, and price manipulation, as well as out-and-out fraud” at the time, led to “diminished public confidence” in the investment banking system and changes were desirable (Armstrong, 1997: 285; Sorell et al., 2003: 66).

In the late 1930s, the Association constitution was amended to reflect the following changes (Coleman, 1989: p. 513). Membership requirements were further strengthened and the Association was “empowered” “to select and pay a firm to be the Association auditors” (p. 513). Strict rules were also imposed on financial statement reporting requirements (p. 513). These amendments to the Association’s constitution “had an immediate impact on the members of the Association” (p. 513). Audit reports revealed capital deficiencies with member firms, as well as “certain unsatisfactory practices” (p. 513). While the Association amendments may have irked some members and increased their operating costs, “there is no doubt that its application has greatly added to the protection of the Public and the prestige of [its] members” (p. 513). The amendments also had the effect of allowing the Association to negotiate “an informal arrangement with government authorities enabling it, rather than the state, to regulate members' behaviour” (p.514). The government therefore had “no reason to involve itself further in monitoring the internal affairs of the Association’s members” (p.514).

**Mandated Self-Regulation**

The informal arrangement between the OSC and the IDA was short-lived (Coleman, 1989: 514). In the 1940s, securities crime began to rise in Ontario to the
extent that the province had gained an international reputation for stock fraud (see Dey & Makuch, 1979). This prompted the “Ontario government to rewrite the Securities Act in 1945, requiring ‘full, true, and plain disclosure’ of all material facts about a new issue of securities sold in a ‘primary distribution’ from a company’s treasury” (Armstrong, 2001: 7-8). However, critics argued that government intervention would “disrupt the efficient functioning of the market and interfere with capital flows” (p. 8). There were also arguments that governments were ill-equipped to police the capital markets at the time (p.8). Since the IDA already had the power to secure compliance from its members, the government thought that it was in the best interest of the market to allow the IDA to regulate the industry (p. 8). This independence led to a period of mandated self-regulation (p. 8). Mandated self-regulation is when “an industry is ordered or designated by the government to develop, use, and enforce norms” (Coleman, 1989: 506). The “industry…becomes formal, legally recognized, [and an] instrument for the implementation of public policy” (p. 506).

To reflect this change, the Ontario Securities Act was amended in 1947 and “recognized members of the IDA as ‘investment dealers’ and gave the IDA a mandate to regulate their conduct” (Sorell et al., 2003: 66). “The Act also required the IDA to submit its rules and regulations governing audits of its members to the OSC for approval” (p. 66). Added to the disclosure requirements, the Act “sought to lessen government control over firms in the industry by transferring more responsibility over business conduct to the industry itself (Coleman, 1989: 514). In effect, the amendments to the Act “meant that the IDA had been given an explicit mandate by the state to regulate the business conduct of its members, superseding the informal understanding that was established before” (p. 514 emphasis added). The IDA saw the mandate as one way to “ward off direct government regulation” in their affairs (p. 514).
During the subsequent two decades, “the [IDA] and the government were to work out the implications of this mandate and to put in place” the membership rules that were designed to strengthen its regulatory structures (Coleman, 1989: 515). More emphasis was placed on having a standard education requirement for members to enter the investment industry; the amount of capital required for membership in the Association increased; a national contingency fund was also set up to protect and offset investors losses; and more importantly, the administration and investigation of complaints became more formalized (p. 515). The new rules stated that

members could be reprimanded, fined, suspended or expelled for any one of several reasons: any business conduct or practice unbecoming a member of the Association; any failure to comply with or carry out provisions of any By-laws, regulations or rules of the Association; ‘failure to comply with or carry out the provisions of any applicable Federal or Provincial Statutes relating to the sale of securities or of any rules or regulations made pursuant thereto’ (note that the Association is responsible for enforcing government statutes); and when the Association is of the opinion that the business or financial arrangements of such members are objectionable (p. 515 emphasis added).

At this stage, according to Coleman, the IDA encompasses the four elements of modern day self-regulation: “stringent membership requirements, monitoring of business conduct, educational prerequisites, and a national contingency fund” (p. 516).

In the late 1960’s, “events in Ontario [led to] political pressure [that later altered this] arrangement” (Coleman, 1989: 517). During this time, the OSC detected an increase in “misleading advertisement and high-pressure sales methods designed to dupe” investors (Armstrong, 2001: 9). It was also found that promoters of the mining and oil industries “were marketing shares by manipulating prices through carefully crafted rumors and leaks” (p. 11). This coupled with the fact that insiders were profiting from inside information, began to attract criticisms from creditors and security holders
These incidents led to calls for a change in the Securities Act and in the late 1960’s the Act was once again amended (Armstrong, 2001: 9; Sorell, 1994 as cited in Sorell et al., 2003: 66). The 1960’s amendment, while giving greater power to the OSC over the Toronto Stock Exchange, did “remain faithful to the principle of self-regulation” (Armstrong, 2001: 9). However, the amendments in the 1960s left the Association weakened, and minimized its role in monitoring the markets. The Association, sensing the intervention of state regulation, once again responded “over the next ten years by redesigning and formalizing its self-regulatory apparatus” (Coleman, 1989: 518).

These changes did not come easily. After considerable internal debate and a study by a management consulting firm, the IDA decided to combine the functions of trade association and self-regulatory organization, two roles that had long since been differentiated in the US system. The organizational changes that followed strengthened the control of the association over its members while leaving it as a powerful partner in a concertation policy network (p.518).

In 1969, the Association “redefined its objectives to make explicit reference to its self-regulatory role and reorganized itself by establishing a separate public information division with several experts and policy advisors” (Sorell et al., 2003: 66).

From the late 1970s to the early 1980s, the IDA underwent a series of changes that were reflected in its board composition and internal affairs. First, it “created the position of president and established a board of directors, composed primarily of senior executives from member firms, but also including ‘public directors’ to reflect a non-industry perspective and represent the interests of public investors” (Sorell et al., 2003: 66). Second, “the various changes in the Association’s scope of activity …resulted in a more differentiated internal organization” (Coleman, 1989: 518). More specifically, “the Association …developed a more complex structure for member regulation, for managing its own internal affairs, and for dealing with the public and governments” (p. 69).
The Association also set up “specialized sections for financial administrators, money market dealers, and young members,” and added new committees to deal with issues surrounding “tax policy, pension reform, steering, capital coordinating, capital gains tax exemption, trade in services, and securities industry capital markets” (p. 520).

Third, the Association increased its membership fees and “instituted… an underwriting levy paid on transactions in the industry” that led to an increase in revenue (p. 520).

Finally, by the late 1980s, “the [A]ssociation drew on its expanded staff and increased finances to develop a more strategic and planned approach to its activities” (p. 520). In particular, the Association pursued “two overriding goals” (p. 520). First,

the [A]ssociation fought in every forum available to maintain the long-standing distinction in Canada between market and financial intermediaries. It enlisted in this struggle the stock exchanges and any other allies it could find. In the end, the [A]ssociation lost this fight but its consistency and the quality of its research and arguments present a marked contrast to the work of two decades ago (p. 520).

Second, and more importantly,

the president of the IDA has argued since the beginning of his tenure that the [A]ssociation is a more effective advocate for its members because of its self-regulatory activities. “If we are not responsibly and effectively engaged in compliance and self-regulation, we become yet another lobby and the industry will lose its constructive influence on Securities Commissions and the Federal Government (p. 520).

**Regulation by Oversight**

Beginning “in the late 1980s and early 1990s,” the OSC began to take a “greater role in overseeing the IDA” (Sorell *et al*., 2003: 67 emphasis added). Further amendments to the *Securities Act* also gave the OSC formal power to grant SROs status and “delegate regulatory responsibilities to them” (p. 67). In 1994, the IDA applied for
SRO status and was granted “recognition on a temporary basis, pending the completion of its review of the IDA’s application, and the determination of appropriate regulatory standards for recognition and oversight” (p. 67). Of particular concern were the “conflicting roles of the IDA as a trade association and regulator” (p. 67). In addressing these concerns, the OSC “staff concluded that through monitoring and oversight by the OSC, the risks associated with this dual role could be minimized” (p. 67).

After establishing the criteria that the IDA had to meet in order to be recognized as an SRO, “the OSC conducted its review of the IDA’s enforcement and compliance capacities and operations, as well as the IDA’s rules including its constitution, by-laws, regulations and policies” (Sorell et al., 2003: 67). The OSC concluded that the IDA’s enforcement operations and monitoring procedures were generally acceptable, subject to a few comments. Staff advocated more transparency in [the] IDA’s disciplinary proceedings, as well as the allocation of additional resources to sales compliance and the implementation of a risk based approach to member branch office reviews (p. 67).

While the OSC “found the IDA rules generally appropriate, there were a number of areas of concern which were addressed by the IDA giving undertakings to effect changes” (p. 67). In addition, the OSC also canvassed the self-regulatory roles the IDA had historically played in the securities marketplace and noted the significant amount of supervision which the OSC already exercised over the IDA as a result of previous negotiations. After considering these factors, the OSC concluded that it would be in the public interest to grant recognition to the IDA. The OSC granted a final order formally recognizing the IDA as an SRO on October 27, 1995 (Pp. 67-68).

Over the next decade, the IDA was seen as the “national self-regulatory organization and representative of the Canadian securities industry,” and was
“responsible for the market conduct and capital adequacy of its member firms” (IDA, 2002: para. 1; Mohindra, 2002: 11). Up to this point, the OSC usually conducted “piecemeal reviews” of the Association; however, beginning in the late 1990s, the OSC became more “comprehensive” in its “examination” of the Association’s activities (Mohindra, 2002: 30). The Association had a broad mandate that generally consisted of administering and fostering a “fair, efficient and competitive” market, along with “protecting investors and ensuring the integrity of the marketplace” (IDA, 2002: para. 15). However, many were of the opinion that securities regulation in Canada was too complex with many SROs’ regulatory functions duplicating one another (Wise Persons’ Committee, 2003: 25). More specifically, it was argued that the IDA’s member regulations and RS market regulations were not in line with each other’s objectives (Jenah, 2007b: 5).

Other important changes that altered the regulatory functions of the IDA were to follow. At the end of 2000, the BCSCn conducted an audit of the Pacific District Office of the IDA for the period covering January 1, 2000 to November 30, 2000 (BCSCn, 2001a: 1). Commission staff found that the IDA has made significant progress in improving its regulation of member conduct in the Pacific District since staff’s previous audit report issued in 1997. However, with the recent addition of a number of members whose member conduct was regulated previously by the former Vancouver Stock Exchange, the IDA faces significant new challenges to regulating member conduct in the Pacific District (BCSCn, 2001b: 1).

In 2002, the Capital Markets Division of the BCSCn conducted a follow-up audit of the IDA’s Enforcement Department for the period covering September of 2000 to December of 2002 (BCSCn, 2002: 2). Commission staff found that
Overall, the IDA implemented a significant number of the previous recommendations to improve its effectiveness in meeting its regulatory responsibilities. Significant change has been accomplished with the implementation of new systems and the development of better processes for handling complaints and managing priorities. However, enforcement results have still lagged below historic levels particularly in corporate actions brought against firms. The most significant factors contributing to the lack of results appear to be key staff vacancies and file backlogs (p. 2).

In 2004, the IDA and the OSC underwent a lengthy legal process to block the release of an internal audit carried out by the OSC on the IDA in 2000 (see Watts, 2004). When the Ontario Information and Privacy Commission ordered the OSC to publicly disclose the findings of the audit under the Freedom of Information Act, the OSC noted that their staff would not feel comfortable in making “frank and candid” assessments of a fellow regulatory body, while the IDA charged that they would be “reluctant to co-operate with the OSC” if the report went public (Watts, 2004: para. 4; Howlett, 2004: para.5).

So what exactly were the IDA and the OSC hiding? In 2005, when the audit was eventually released, the IDA was seen as lacking sufficient resources to carry out its daily operations. In particular, the audit was critical of the IDA’s enforcement division. The audit found a growing backlog of enforcement cases; no screening process for complaints and a bloated case review process. The audit also found a “significant number of changes to penalty recommendations” by the former Senior Vice-President of member regulation. The OSC called for an emergency resources allocation to help clear the backlog and an overhaul of the department’s other processes (Langton, 2005: para. 8 emphasis added).

The IDA has since taken steps to address some of the problems and recommendations that were highlighted in the audit report (see Langton, 2005).
In 2006, “the Alberta Securities Commission (ASC) conducted an oversight review” of the IDA, Prairie Region “for the period of January 1, 2004 to August 31, 2006” (ASC, 2007: 3). Two notable problems were found with enforcement. First, ASC staff were informed “that hearing panels are often difficult to convene because of scheduling issues, conflicts of interest and other factors affecting the availability of panel chairs,” which in turn “limits the number of hearings and results in hearing delays” (Pp. 19-20). Second and more important, is that ASC staff found inconsistencies in the settlement agreements. IDA’s “documentation” noted that “eight forgery files were prosecuted during the review period” (p. 20). ASC’s staff

…reviewed two of these concluded litigation files and another file that was concluded after the completion of [their] fieldwork. In one file, the individual entered into a settlement agreement with Enforcement Counsel which included a reprimand and costs of the investigation as terms. This settlement agreement was rejected by the Hearing Panel for being too lenient. The Panel determined that the settlement did not correlate with the severity of the charge. Counsel negotiated and agreed upon a new settlement that included a penalty, close supervision and costs of the investigation. The Hearing Panel accepted this re-negotiated settlement agreement…In another file involving similar circumstances, the ultimate designated person of a firm forged a signature and misled IDA staff. The IDA issued a warning letter and closed the file (p. 20).

It is important to note that “[t]hese two cases had similar fact patterns and yet the action taken by the IDA was inconsistent from one case to the next” (p.20). Furthermore, “[o]nly one of these cases was brought before a hearing panel and the settlement reached in this case did not fall with the IDA’s prescribed guidelines for Forgery” (p. 20).

In 2006, the IDA parted from its role as a trade association advocate. Trade association advocacy was now left in the care of the newly formed Investment Industry Association of Canada (IIAC) (Jenah, 2007b: 3). Second, a Steering Group was set up to look into ways to consolidate the regulatory activities of the IDA and RS into one self-
regulatory system that would better regulate the markets and its participants (IDA, 2007a: 2-3). In the same year, the Steering Group announced that it had approved, in principle, a proposal that purported to merge the IDA and RS into a new SRO (Pp. 2-3). In 2007, member firms of the IDA voted overwhelmingly (98.3% of cast votes) for a resolution to combine the IDA and RS into a single regulatory organization (IIROC, 2008a: para. 3). In March of 2008, the new SRO was created as the Investment Industry Regulatory Organization of Canada (para. 4). In May of 2008, the CSA approved IIROC and in June of 2008, IIROC was officially established as the “national self-regulatory organization that oversees investment dealers and trading activity on debt and equity marketplaces in Canada” (para. 1). The new mandate of IIROC gives them the authority to “set and enforce standards for [their] members … trading on Canadian marketplaces,” and implement policies that “will protect investors, enhance market integrity and promote confidence in the [securities] system” (Jenah, 2008).^{61}

As the national body that oversees the activities of investment dealers in Canada, IIROC is subject to regulatory oversight by the provincial and territorial securities commissions. According to the Memorandum of Understanding (MOU) regarding the oversight of IIROC, the Oversight Program entails the following:

(i) reviewing information filed by IIROC;

(ii) reviewing and approving new and amended rules, policies and other similar instruments (Rules) and By-laws of IIROC; and

(iii) performing periodic reviews of IIROC’s self-regulatory activities and regulation services (OSC, 2008: 1).

^{61} This direct quote is from the “forward” of Jenah’s (2008) submission to the Expert Panel on Securities Regulation. There is no page number.
The MOU notes that, “the purpose of the Oversight Program is to ensure that IIROC is acting in accordance with its public interest mandate, specifically by complying with its terms and conditions of recognition” (p. 1). Whether or not this oversight will lead to more enforcement is yet to be determined.
Chapter 5: Methodology

Data Collection

Researchers studying white-collar crime face many challenges. Two major problems are the absence of primary data on white-collar crime and gaining access to secondary data that already exists (see Friedrichs, 2010: Ch. 2; Croall, 2001, 14-16; Rosoff et al., 1998; 12-16). Given these shortcomings, criminologists have made good use of data from government agencies, annual reports, newspapers, journals, case studies, police and court records, “to generate some useful studies” (Friedrichs, 2010: 38-44; Hagan, 2007: 257). My dissertation gathered data from three sources – the IDA’s Enforcement and Annual Reports, the IDA cases, and the appeal cases from the IDA to the ASC, the BCSCn, and the OSC.

62 Primary data probably exist; it is just that researchers do not have access to these data.
63 Primary data sources “refer to raw data unaccompanied by any analysis or interpretation,” while “secondary data sources…consist of analyses, synthesis, and evaluations of the information” (Lutzker & Ferrall, 1986 as cited in Hagan, 2007: 254). For example, “the [Uniform Crime Report (UCR)] itself would constitute a primary data source, whereas an existing research study that used the UCR and other sources to predict crime trends would be a secondary source” (Hagan, 2007: 254). Palys and Atchison (2008: 228) note that archival data can also be classified as secondary data. According to Palys and Atchison, “archival measures comprise any information that is contained in ‘hard copy’ records or documents” (p. 226). These include, “written or tape records of speeches, photographs, newspapers, books, or private materials such as diaries and letters…running records and statistical compendia produced by all levels of government and many public agencies” (Pp. 226-227). Palys and Atchison argue that “archival data are necessarily secondary data that are unlikely to have been prepared for research purposes … the information was prepared by someone else, and for some other purpose than for supplying evidence that might be useful to a researcher” (p. 228).
64 A few studies to date have employed secondary data in the study of white-collar crime. For example, Piquero and Davis’s (2004: 646) analyzed data collected by the U.S. Sentencing Commission concerning organizations convicted in federal criminal courts, “to test whether extralegal organizational characteristics influenced sentence outcomes.” Weisburd, Waring, and Chayet’s (2001) study on the criminal careers of white-collar criminals prosecuted in America’s federal court, also relied on secondary data. Similarly, Wheeler, Weisburd, and Bode (1982) used data from the federal district court, with the intent of providing a broad and heterogeneous view of the white-collar crimes that were convicted in the Unites States. Keane (1993) used secondary data collected by Clinard and Yeager’s (1980) and Clinard, Yeager, Brissette, Petrashek, and Harries (1979), to study the impact of financial performance on the frequency of corporate crime.
Data Source One: Annual Reports

Data from the IDA’s Annual Reports were used to examine the funnel metaphor from 2002 to 2007. The IDA’s Annual Reports are readily accessible from IIROC’s website. More specifically, data from the Annual Reports were used to examine the processing of complaints from initial reporting to the Case Assessment Group, to final disposition by investigation and prosecution staff. Data on case assessments were collected to show the sources, number and types of complaints reported for a particular year, the most frequent types of complaints reported for a particular year, and the number of cases assessed (that are open on January 1, received during the year, closed during the year, and remain open at the end of the year). Data on the number of investigations opened and closed by the IDA’s investigation staff across Canada, along with the top four offences for investigation, were collected for further analysis. Data on the number of cases opened and closed by prosecution, the outcome of these cases and the top four offences that prosecution dealt with, were obtained and analyzed. Data comparing the penalties of cases that were sent to a formal disciplinary hearing for both Member firms and individuals were also gathered for further analysis. Data on the fines, costs and disgorgement of ill-gotten gains from Individual registrants and Member firms, were obtained in order to compare them with the total fines, costs and disgorgements imposed by the IDA in each calendar year.

Data Source Two: IDA’s Tribunal Cases

The IDA’s cases that were used in my dissertation were retrieved from Quicklaw. Quicklaw is a comprehensive legal database that covers decisions of cases from courts, tribunals, and regulatory bodies across Canada. Quicklaw is also convenient and readily accessible. It has a user friendly interface that documents and synthesizes the cases in
a manner that makes them easily downloadable into Microsoft Word documents. In addition to its easy access and user friendly interface, Quicklaw provides researchers with a quick and useful way to peruse cases and conduct research on a variety of socio-legal issues. "In Canada, Quicklaw provides a global database of Securities Regulation Tribunal Decisions including settlements, decisions, and orders from the following agencies: [the] Alberta Securities Commission 1994; [the] BC Securities Commission 1987; [the] Ontario Securities Commission 1982; [the] Investment Dealers Association 1984-2008; and [the] Mutual Fund Dealers Association of Canada 2009" (BCSCn, 2011a: para. 3).

Cases decided by the IDA across Canada were identified by typing in the search term; “Investment Dealers Association” into the Securities Regulation Tribunal Decisions database in Quicklaw. The search term “Investment Dealers Association” was sorted by its relevance and retrieved 1,934 cases. I then carefully perused each case to identify the ones that were heard by an IDA hearing panel. Out of the 1,934 cases retrieved from the database, I found 708 that were heard by an IDA hearing panel between 1984 to June of 2008. Once these cases were identified, I then sorted them by the year they were decided (oldest first) and individually downloaded and converted each case to a Microsoft Word file. Each case was then given a number with the first case starting from 1984 being labelled “1”, and the last case ending in June of 2008 being labelled “708”. The other 1,226 cases were cases from regulatory agencies, namely - the Market Regulation Services, the Toronto Stock Exchange, and the ASC, the BCSCn, and the OSC, in which the respective hearing panel made references to the IDA or a case that was decided by the IDA in their decisions.
Rather than using a probability sampling technique to draw a random sample from the 708 cases, I decided to use all of the cases that were heard and reported allegations that were dismissed by the IDA for the following reasons. Although time consuming, it was not impractical for me to code all 708 cases in order to examine for trends over the enforcement period. By using the entire population of cases that made their way into Quicklaw, I also avoided having to deal with issues related to sample size and representation (See De Veaux, Velleman, Bock, 2008: 290-293). Representation is of particular concern, because a random sample could have led to more cases being selected from the District Councils in the provinces with larger populations, and fewer or zero cases being selected from the District Councils in provinces with smaller populations. Second, one of the drawbacks of using random sampling methods is the likelihood of committing a systematic sampling error (Palys, 2003: 130). \footnote{Systematic sampling “errors occur when aspects of your sampling procedure act in a consistent, systematic way to make some sampling elements more likely to be chosen for participation than others” (Palys and Atchison, 2008: 113).} Given the possibility that a random sampling method may lead to cases with little information being included in the sample at the expense of cases with more detailed information, it was best to use all of the cases.

**English and French Cases**

Of the 708 cases, 633 (89\%) of them came from the IDA’s District Councils where the decisions were written in English, while 75 (11\%) came from the Quebec District Council where the decisions were written in both English and French. Of the 75 Quebec cases, 44 (6\%) of them summarized the cases in English, while the remainder of the text was written in French. To translate the French cases, I secured the services of a research assistant, who is a French immersion and SFU graduate. Once the French
language cases were translated, I then combined them with the English language cases and spent about three months doing a first round of coding.

**First Round of Coding**

The purpose of the first round of coding was twofold. First, I wanted to get a better idea of the types of data available on victims, offenders, Member firms and enforcement (offences and penalties imposed). Second, I wanted to provide some mock tables and figures for my dissertation committee in order to show how I would present my findings. In the first round of coding, I randomly selected about two hundred and fifty cases. I made sure that the cases represented five time intervals as follows: 1984-1989, 1990-1995, 1996-2000, 2001-2004, and 2005-2008. I also made sure that the cases represented all ten of the IDA’s District Councils across Canada. By breaking the years into various time intervals, I was able to capture cases heard by an IDA hearing panel for each year from 1984 to June of 2008.

The first round of coding was beneficial because not only did I get a better understanding of the kind of data available, but I soon realized that coding the cases would require presence of mind and attention to details. In addition to information on enforcement, a significant number of cases involved multiple victims, which means that they were lengthy and contained demographic information on each victim. I had to make sure that I traced each victim throughout a case in order to ensure that I captured and coded all of the data related to that particular victim. As such, the first round of coding provided information that allowed me to structure and frame my excel database in a manner that would allow me to capture all of the variables pertaining to cases with more than one victim.
During the first round of coding, I also discovered that some of the cases involved multiple offenders. Cases involving multiple offenders were of three types: those involving only registered representatives; those involving only officers; and those involving Member firms and officers. To address this issue, I coded the offenders that were given the harshest penalties by the IDA.

**Second Round of Coding**

Once all of the issues were sorted out from the first round of coding, I then coded the entire dataset of 708 cases. Data was collected on the investors (“victims”), the registered representatives and Member firms (“offenders”), and the types of offences and penalties imposed. I also gathered data on the aggravating and mitigating factors used in penalty decisions.

**Data on the Victim**

Data was collected in order to examine the demographic profile of the investors (see codebook in Appendix B). Where available, descriptive data on the victim’s gender, age, occupation, relationship to the offender, and investment knowledge were collected in order to obtain a demographic portrait of victims of securities violations. To understand the financial profile of the investors, data on their annual income, liquid net worth, and the amount of losses incurred, were collected. The victim’s investment objective(s), sources and purpose(s) of investment and the type of account(s) that they opened with the Member firm (margin, cash, Registered Retirement Savings Plan (RRSP) etc.) were also recorded.
Data on the Offender: Individual Registrant and Member Firm

Data collected on individual offenders consist of disciplinary actions taken against the registered member, who was currently working or had previously worked for a Member firm. Individual offenders were categorized into three occupational classifications: registered representatives, branch managers, and officers.\(^{66}\) Data on the type of occupation that the registered member was officially employed as, the amount of experience (measured in the number of years) that the individual had in terms of being employed as an investment dealer up to the time that the offence was committed, and the offenders’ current registration status was recorded. Data on whether the offender had prior criminal or regulatory infractions, along with demographic data on the offender’s gender, and the province that the offender conducted his or her business, were also collected for further analysis.

Data were also collected on variables that reflect on Member firm's operations (see codebook in Appendix B). Data collected on Member firms were related to the type of business (retail operations, institutional investment etc) that the firm was involved in,\(^{67}\) and the firm's disciplinary history.

Data on Enforcement Actions

Data reflecting the disciplinary actions taken by the IDA hearing panels on

\(^{66}\) The IDA’s Rulebook outlines the type of employment a registered individual may hold in a member firm. IDA By-law 29.1 states that “[f]or the purposes of disciplinary proceedings pursuant to the By-laws, each Member shall be responsible for all acts and omissions of each partner, director, officer, sales manager, branch manager, assistant or co-branch manager, registered representative, investment representative, and employee of a Member, and each of the foregoing individuals shall comply with all By-laws, Regulations and Policies required to be complied with by the Member” (IDA, 2008c: 121).

\(^{67}\) See (IIROC, 2010a) for a list of IIROC’s dealer member firms by peer group classification.
registered representatives and Member firms were also recorded (see codebook Appendix B). Such data captures a variety of variables related to enforcement and includes the date of the hearing, the type of infraction(s) and the penalties imposed. Disciplinary actions taken against the individual offenders (registered representatives, branch managers, and officers) were coded separately from disciplinary actions taken against the Member firm(s). Even if the firm is not accused in the proceeding, the name of the firm that the respondent belonged to was recorded, in order to see which firms and business types are more likely to have lax internal compliance and disciplinary procedures. The province/District Council that the hearing occurred in was also coded. Data on aggravating and mitigating factors were collected in order to obtain insight into the considerations taken by the hearing panels when imposing sanctions.

**Final Dataset**

Once I had a chance to peruse and code all of the cases, I had to modify the dataset. First, I had to treat some of the variables related to victims as missing data, because they could not be coded for further analysis. A total of 5 cases were treated as missing variables. Out of the 5 cases, there were 3 cases involving 9, 10 and 16 victims respectively. For these cases, I was unable to code the offender’s “relationship to the victim,” because the wording of the cases did not distinguish whether the victims were family members or friends of the offender. In one case, the wording was ambiguous and noted that all of the victims were “either close relatives or friends” of the respondent. As for the other cases, one noted that “six of the eight individuals were either related to, or friends of, [the Respondent];” while in the other case it was noted that “these clients

68 See the IDA’s (2006b) Disciplinary Sanction Guidelines for the type of penalties imposed on both registered members and member firms.
consisted primarily of personal friends and family members of the Respondent.” In one case involving 10 victims, I was unable to determine their exact age and occupation in order to code them. In two other cases involving 29 and 97 victims respectively, I was unable to code any of the variables because the number of victims would have made the dataset unmanageable.

Second, I had to eliminate cases because they were not relevant to my dissertation. These cases were set aside because they were atypical and would not have impacted the results in any way. A total of 39 cases were eliminated because of the following reasons:

- 1 case that dealt with a request to open a proceeding to consider costs;
- 1 case that dealt with a Notice of Reinstatement of a member whose rights and privileges were previously suspended;
- 1 case involving an individual registrant and Member firm was removed because both offenders received the same penalty. Since the rationale for coding cases involving multiple offenders is based on the one that received the harshest penalty, there was no basis to code this particular case;
- 2 cases because the IDA withdrew the Notice of Hearing and ended disciplinary proceedings on the matter;
- 2 cases involving 45 and 54 charges respectively because coding all of the charges was not practical and would have led to an unmanageable dataset;
- 2 cases dealing with the rejection of a settlement agreement by an IDA hearing panel;
- 3 cases dealing with suspension orders to be continued and vacated suspensions;
• 4 cases where the IDA’s hearing panels ordered a stay of proceedings;
• 5 cases dealing with requests for adjournments, adjourned motions, and adjourned hearings;
• 9 cases dealing with penalty hearings, a hearing to set a date, and notices;
• 9 cases were removed because they dealt with procedural issues related to motion applications concerning charges laid, disclosure, jurisdiction, and admissibility of evidence.

Information on the victim, offender, Member firm, and enforcement were not obtainable from these cases. The final dataset consisted of 669 cases, out of which 429 involved identified victims. The total number of identified victims was 1,167. Of the 669 cases, 556 deal with individual offenders and 113 deal with Member firms.

**Data Source Three: Appeals to Securities Commissions**

Data collected on the securities commissions were appeals from the IDA’s disciplinary hearings that made their way into the Securities Regulation Tribunal Decisions Quicklaw database. Quicklaw only maintains appeal cases from the ASC, the BCSCn and the OSC. The appeal cases were identified by typing in the search terms: “Investment Dealers Association” and “securities commissions” and “appeal” into Quicklaw’s database. These search terms were sorted by their relevance and produced 362 cases. I then carefully went through each case to identify the ones that dealt with appeals from an IDA hearing panel. I found 14 appeal cases that dealt with issues related to an IDA decision. The other 348 cases dealt exclusively with the Mutual Fund Dealers Association of Canada, Toronto Stock Exchange, Ontario Information and Privacy Commissioner, the ASC, the BCSCn, the OSC, and the IDA. These cases showed up because the respective hearing panels made references that captured one or
more of the search terms: "Investment Dealers Association," "securities commissions," and "appeal" in their decisions. Data from the appeal cases gave insight into the types of appeals heard by the securities commissions and the decision of those appeals.

**Reliability and Validity Concerns**

**Reliability**

Coding of the variables was relatively straightforward and did not require any reliability tests (test-retest, multiple forms split-half) in order to demonstrate reliability (see Palys & Atchison, 2008: 60-62; also see Hagan, 2007: 300-302). As shown in Appendix B, a well devised coding scheme was developed that allowed for subsequent verification. A codebook, outlining the variables, labels, and numbers assigned to the labels is also provided to show how the variables were coded (see Appendix B). All the variables used in my dissertation are “directly observable” and as such, do not need to be measured and interpreted (See Rothman, 2007: 440).

**Validity**

A few validity concerns in this study relate to the Quicklaw database, generalizability, and variables on the victims. As such, it is important to acknowledge and address these concerns at this stage of the dissertation. Of particular importance is selective deposit. That is, the cases used in my dissertation are the ones that made their way into the Quicklaw database. It is difficult to ascertain whether I have all the cases that were decided by the IDA from 1984 to June 2008, or estimate how many are

---

69 Rothman (2007: 440) notes that “latent variables are those that are not directly observable and involve interpretation by the coder. Examples of observable variables are recorded dates, number of words, dollars used; examples of latent variables are the degree of democracy of a nation and the implied intent of a particular actor.”
missing. That said, *Quicklaw* “obtains its cases and statutes from official sources and standard points of distribution that are already in electronic form, with only a few exceptions” (Halvorson, 2000: para. 11). Based on this statement, one can infer that most of the cases that were decided by the IDA from 1984 to June of 2008, were included in the *Quicklaw* database.

Generalizability, in the traditional quantitative sense relates to sampling and is therefore not an issue in my research. I am not using a sample of cases within the population of cases on *Quicklaw*; I am using all of the cases from 1984 to June of 2008. However, others may question the “transferability” of the study and its application to similar SROs in the securities industry. One possible question may relate to the external validity of the study (Marshall & Rossman, 2006: 202). Such a question may attempt to inquire whether my study can be used to understand the enforcement practices of similar SROs that are charged with enforcing securities breaches in other countries. Since every SRO is unique in both its functions and operations, the findings of my dissertation cannot accurately inform us about the enforcement practices of SROs in the securities industry in other parts of the world (e.g., see Berg, 2001: 36). Rather, my study has the potential to provide explanations on certain issues that can help to understand the enforcement of complaints by SROs in countries where they continue to play a major role in monitoring the operations of market participants in the securities industry (e.g., see p. 36 of Berg).

Another concern relates to missing data for variables describing the demographic profile of the victims. As will soon be made transparent, for some of the variables

---

70 According to Palys and Atchison, “[e]xternal validity refers to the generalizability of results beyond the specifics of the study” (2008: 266).
(investors’ annual income, household net worth, and relationship to the offender), I was only able to obtain data that represents between 15% and 17% of the identified victims. For all of the other victims’ related variables, I was able to obtain data that ranged between 20% and 40%. With the exception of the three variables mentioned above, the data available for the other variables on victims were no different from the response rate of mail-out surveys that is typically around the 20% to 30% range (see Henderson, 1990; Denison and Mishra, 1995). However, some may be hastened to argue that with only 15% to 17% of the data available for investors’ annual income, household net worth, and relationship to the offender, it will limit the generalizability of the results. As such, the key question to ask is whether an increase in the data for these three variables would have made any significant impact on the results? As you will soon see, no information power was lost, because the results from the data available provide sufficient information for a representative analysis on these variables. It is highly unlikely that there would have been any significant changes in the results with additional data on the three aforementioned variables.

To minimize the effects of these concerns, data triangulation will be used to enhance the study’s validity (See Mathison, 1988: 13; Silverman, 2000: 177; Marshall & Rossman, 2006: 202-203). By using multiple data sources, the limitations of one set of data can be offset by another. The data from the cases can be substantiated and verified with data from the annual reports (see Hagan, 2007: 7). This is crucial in my research. Data from the annual enforcement reports only go back to 2002. As such, I will only be

71 Denison and Mishra (1995) justified their 21% response rate by citing Henderson (1990). Henderson (1990) argues that a response rate of 20%-30% is fairly typical of mail-out surveys to a large sample of firms (as cited in Denison and Mishra, 1995: 217). Also see Kliethermes, Parcell, and Franken, who had a 10.41% response rate in their study and noted that there is “no set norm for what is considered an appropriate response rate and that lower response rates may be realized with a mail survey” (2009: 5).
able to examine the funnel process in its entirety for six years (2002-2007). Given this limitation, every attempt will be made to examine the other aspect (‘funnel away’) of the misconduct funnel from the available cases. By using “multiple data-collection procedures”, not only will I be able to offset any potential external validity concerns, but it will “greatly increase the depth of understanding” of the IDA enforcement procedures (e.g., see Berg, 2001: 6).
Chapter 6: Data Analysis with Data from Annual Reports

The IDA Enforcement Process

The IDA’s Disciplinary Sanction Guidelines (“Guidelines”) list the offences for which the Association can discipline its registrants and Member firms (see IDA, 2006b). The Association’s By-law 29.1 gives the Disciplinary Committee the power to discipline registrants or Member firms that have been involved in quasi-criminal offenses. By-law 29.1 and Regulation 1300.17 deal with infractions surrounding conflict of interest. Regulation 1300.1 to 1300.5 and By-law 29.1 deal with improper sales practices. By-law 17 and 29.1 and Regulation 1300, deal with infractions concerning internal control offences. Finally, there are “other” offences ranging from failure to cooperate with the Association’s Guidelines, to conducting business while being suspended (see IDA, 2006b: 14-46 for a list and an explanation of these By-laws).

The Enforcement Department of the IDA, “is responsible for investigating allegations of regulatory breaches by [the] IDA Member firms and their registered employees, and when appropriate, prosecuting registered employees and firms in an IDA administrative hearing” (IDA, 2008b: 2). There are three types of IDA administrative hearings: Settlement, Contested, and Expedited. A Settlement Hearing is one where enforcement

72 It is important to note that the IDA uses the word “offences” instead of “infractions” in its Guidelines. More specifically, the IDA notes that “the list of guidelines for imposing sanctions for specific offences that follow the General Principles is not exhaustive, but rather comprises a list of offences that have been encountered and sanctioned in the past by the discipline panels of the Association and/or other securities regulators” (IDA, 2006b: 5 emphasis added). See Appendix 1 for the list of the Association’s most cited violations. To view the entire IDA’s Rule Book see (IDA, 2008c) at Royal Bank of Canada’s Web site: https://www.rbccm.com/debtproducts/file-434099.pdf
staff and the firm or individual involved in the dispute are able to negotiate a settlement in which the firm or individual admits to certain misconduct and agrees to a corresponding penalty. However, that agreement is not binding until it is accepted by a Hearing Panel. Therefore, [enforcement] staff and the firm or individual must attend a formal hearing, present the agreement to the Hearing Panel and explain why they believe that the panel should accept it. At the Settlement Hearing the panel will consider the settlement and will provide reasons as to why it accepts or rejects the settlement (IIROC, 2011b: para. 7).

Note also, that “[i]n approving a settlement agreement, the appropriate District Council does not determine the penalty, rather it approves or refuses to approve the penalty negotiated between the Association and the respondent” (IDA v. Strocen, 2002: para. 49).

A Contested Hearing will commence “when the firm and/or individual and IIROC have not been able to conclude a settlement agreement” (para. 8).

Contested Hearings resemble trials that take place in regular courtrooms. IIROC Enforcement Counsel must present evidence to prove the allegations contained in the Notice of Hearing. The firm or individual has the opportunity to challenge the allegations being made against them by cross-examining any IIROC witnesses and by presenting their own evidence. After the parties have presented their evidence, each side makes its closing arguments. The Hearing Panel then usually adjourns to decide the case and later issues written reasons explaining its decision. If the Hearing Panel decides that Enforcement Counsel has proven some or all of the allegations in the Notice of Hearing, the Hearing Panel will then hear evidence and argument from both sides as to the appropriate penalty (para. 8).

Expedit ed Hearings “commence with a Notice of Application rather than a Notice of Hearing” (para. 9). In Expedit ed Hearings,

[t]he firm or individuals are usually not informed about the hearing and normally does not attend. Any order that the Hearing Panel may make is usually temporary and is meant to address acute or serious risks that need to be addressed immediately. The respondent has a right to request an immediate review of the decision. The decision of the Hearing Panel will be made public (para. 9).
All hearings are heard by a Hearing Panel, made up of two industry representatives and a member of the public who acts as Chair (IIROC, 2008c: 3).\textsuperscript{73} In 2004, the IDA made amendments to By-law 20 that allowed the “Nominating Committee of each District [to] nominate a public member to serve as Chair of the Hearing Committee” (IDA, 2004: 6).\textsuperscript{74} By-law 20 of the Association’s Sanction Guidelines also gives the Hearing Panel the power to “impose specified penalties where it has been found that an individual registrant or a Member firm fails to comply with the Association’s By-laws, Regulations, Policies and Rulings” (IDA, 2006b: 4).\textsuperscript{75} The range of disciplinary sanctions is set out in sections 20.33 and 20.34 of the Association’s By-Laws and may include one or any combination of the following:

(i) a reprimand;
(ii) a fine up to $1,000,000 for Approved Persons and $5,000,000 for Members per offence or an amount equal to three times the pecuniary benefit obtained as a result of any contravention, whichever is greater;
(iii) suspension of a Member’s rights and privileges or of an Approved Person’s approval to act as a partner, director, officer or employee of a Member, possibly on terms;
(iv) termination of a Member’s membership and the accompanying rights and privileges or revocation of an Approved Person’s approval;
(v) expulsion of a Member from the Association or prohibition of an Approved Person’s approval for any period of time; and
(vi) imposition of terms and conditions on a Member or conditions on a subsequent approval or continued approval of an Approved Person, as the Hearing Panel considers appropriate in the circumstances (IDA, 2006b: 4)

\textsuperscript{73} The public member is not associated with the industry in any way, and he or she is usually a retired judge or lawyer with expertise in securities law (IIROC, 2008c: 4).

\textsuperscript{74} Analyzing the penalties imposed by the Hearing Committee will be separated into time intervals (1984-1993, 1994-2003, and 2004-2008) that will account for any changes in fines over time.

\textsuperscript{75} The “Hearing Panel may also impose penalties where a registrant has failed to comply with applicable securities regulations or engages in any business conduct or practice that such Hearing Panel in its discretion, considers unbecoming of a Member or not in the public interest” (IDA, 2006b: 4).
The IDA’s enforcement process consists of three stages: case assessment (of complaints), investigations, and prosecution by enforcement counsel (see IIROC, 2008c: 1-4).

### The Funnel Process: Funnel in

As mentioned earlier, SROs claim to “funnel in” more cases than the criminal justice system would consider taking in (Brockman & McEwen, 1990: 13). In this section, I will look at the number of events reported to ComSet and complaints processed by the IDA’s Case Assessment Group.\(^{76}\)

#### Events Reported to ComSet

The IDA’s Complaints and Settlement Reporting System (ComSet) is a database maintained by IIROC that requires Member firms to report investors’ complaints and disciplinary actions taken against registrants. All “ComSet reports received in the previous 24 hours are reviewed by the Intelligence and Analyst section each morning” (IDA, 2008b:6). The Intelligence and Analysis Unit reviews these “matters...against a set of established criteria and, where appropriate, matters are referred to case assessment to assess whether an investigation ought to be initiated” (IDA, 2008b: 6).

#### Sources of Events

Policy 8 of the IDA’s Reporting and Recordkeeping Requirements, outlines the events in which all Member firms must report to ComSet (see IDA, 2006d). The types of events recorded on ComSet are civil claims, criminal charges, customer complaints,

\(^{76}\) The IDA refers to the issues reported to ComSet as “events” (see IDA, 2008b: 6).
denial of registration or approval, external disciplinary action, internal disciplinary action, and internal investigation. According to the IDA,

civil claims includes claims pending before a court or tribunal against a registrant; criminal charges is when a Member, or any current or former registrant is charged with, convicted of, pleads guilty or no contest to, any criminal offence, in any jurisdiction, inside or outside of Canada, while in the employ of the Member, or concerning matters that occurred while in the employ of the Member; customers complaints are complaints that are not service related; denial of registration and approval included being denied registration or a license by any regulatory or self-regulatory organization, professional licensing or registration body, in any jurisdiction, inside or outside of Canada, while in the employ of the Member; external disciplinary action are action taken by any regulatory body (excluding the IDA); internal disciplinary action are action taken by the member firm; and, internal investigations requires the Member to conduct an internal investigation where it appears that the Member, or any current or former registrant, while in the employ of the Member, has violated any provision of any legislation or law, or has violated any by-laws, rules, regulations, rulings or policies of any regulatory or self-regulatory organization relating to theft, fraud, misappropriation of funds or securities, forgery, money laundering, market manipulation, insider trading, misrepresentation or unauthorized trading, in any jurisdiction, inside or outside of Canada (IDA, 2006d: 1-4 emphasis added)

Table 6-1 Events Reported to ComSet

<table>
<thead>
<tr>
<th>Types of Events Received</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Count</td>
<td>Percent</td>
<td>Count</td>
<td>Percent</td>
<td>Count</td>
</tr>
<tr>
<td>Civil Claims</td>
<td>629</td>
<td>23.6</td>
<td>499</td>
<td>26.3</td>
<td>383</td>
</tr>
</tbody>
</table>

77 The IDA notes that “service complaints means any complaint by a client which is founded on customer service issues and is not the subject of: i) any legislation or law concerning securities or exchange contracts of any jurisdiction, inside or outside of Canada; or ii) by-laws, rules, regulations, rulings or policies of any securities or financial services regulatory or self-regulatory organization in any jurisdiction, inside or outside of Canada” (IDA, 2006d: 1-2).

78 Unless otherwise stated, the numbers used in this chapter came from the IDA’s Enforcement Annual Reports from 2002 to 2007. The numbers were then converted into percentages, in order to show the proportion of the type of Events and complaints reported and dealt with each year. Note also that the tables and figures in this dissertation may not always total 100% due to rounding up of the numbers rather than errors in the data.
<table>
<thead>
<tr>
<th>Types of Events Received</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Count</td>
<td>Percent</td>
<td>Count</td>
<td>Percent</td>
<td>Count</td>
</tr>
<tr>
<td>Criminal Charges</td>
<td>11</td>
<td>0.4</td>
<td>9</td>
<td>0.4</td>
<td>6</td>
</tr>
<tr>
<td>Customer Complaints</td>
<td>1936</td>
<td>72.5</td>
<td>1276</td>
<td>67.3</td>
<td>1320</td>
</tr>
<tr>
<td>Denial of Registration or Approval</td>
<td>1</td>
<td>0</td>
<td>2</td>
<td>0.1</td>
<td>1</td>
</tr>
<tr>
<td>External Disciplinary Action</td>
<td>10</td>
<td>0.4</td>
<td>20</td>
<td>1.1</td>
<td>22</td>
</tr>
<tr>
<td>Internal Disciplinary Action</td>
<td>26</td>
<td>1</td>
<td>44</td>
<td>2.3</td>
<td>38</td>
</tr>
<tr>
<td>Internal Investigations related to criminal and quasi-criminal offences  79</td>
<td>57</td>
<td>2.1</td>
<td>46</td>
<td>2.4</td>
<td>71</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>2670</strong></td>
<td><strong>100</strong></td>
<td><strong>1896</strong></td>
<td><strong>100</strong></td>
<td><strong>1841</strong></td>
</tr>
</tbody>
</table>

As shown in Table 6-1, most of the events reported to ComSet were Customer Complaints. In total, there were 7,381 customer complaints received from 2003 to 2007. That is an average of approximately 1,476 customer complaints per year. With the exception of 2004, the number of Customer Complaints comprised over 70% of all of the events recorded from 2003 to 2007. From 1,936 (72.5%) Customer Complaints received in 2003, the number decreased to 1,276 (67.3%) in 2004 and then increased steadily.

79 Since internal investigations comprise any violations of “provision of any legislation or law,” or violations of “any by-laws, rules, regulations, rulings or policies of any regulatory or self-regulatory organization,” an argument can be made that the offences listed under internal investigations in Policy 8 of the IDA’s Reporting and Recordkeeping Requirements were both criminal and quasi-criminal in nature (see IDA, 2006d: 4).
from 1,320 (71.7%) in 2005, to 1,429 (76.4%) in 2007. The number of Customer Complaints must be interpreted with caution. Customer Complaints reported on ComSet were complaints that were reported by Member firms and do not include complaints that were reported directly to the IDA. This coupled with the fact that service related complaints were not recorded on ComSet, works to undercount the number of customer complaints that occurred.

To put these numbers into context, assume that the 7,381 customer complaints received were against different registrants. At the end of December 31, 2007, there were 21,897 individual registrants with IDA Member firms that were approved to trade and offer investment advice to investors (IDA, 2007c: 4). When one does the math, the number translates to approximately 34% of registrants that have had complaints registered against them between 2003 and 2007.\(^80\) As such, when one looks at the aggregate complaints over the six year period, the chance of an investor ending up with an individual broker who has had a previous complaint is approximately 1 in 3. However, this finding goes against a claim made by the then Senior Vice-President, Member Regulation of the IDA, who in 2005 noted that “from the analysis of clients’ complaints reported to the IDA on ComSet … 93% of all registrants have no complaints made against them” (Burke, 2005: 1, footnote 1). How is this possible when the chances of getting a broker with a previous complaint are roughly 1 in 3?

To test Burke’s claim, I conducted an analysis of the number of customer complaints reported on ComSet per year from 2003 to 2005, against the number of individual registrants registered to trade at the time with the IDA. Since I was unable to

\(^{80}\) To arrive at 34%, I divided the number of complaints (7,381) by the total number of individual registrants (21,897).
find the number of registrants registered with the IDA in 2003, 2004, and 2005, for illustrative purposes, I used the number of registrants (21,897) that were registered in 2007 as an estimate for the previous years. To do the calculation, I first added the number of customer complaints from Table 6-1 for 2003, 2004, and 2005 for a total number of 4,532 complaints. I then divided 4,532 by 3 (years) to get an average of 1,511 complaints per year. Dividing 1,511 customer complaints by 21,897 individual registrants resulted in approximately 7% of individual registrants that had complaints against them in any given year, or 93% were complaint free in any given year. As such, it is important to acknowledge that Burke is looking at complaints per year, and therefore the number of individual registrants with previous complaints will be much lower, as opposed to when the complaints are looked at over a 6 year period, in which case the number of individual registrants with previous complaints is bound to be more.

With the exception of Civil Claims, which actually declined from 629 (23.6%) in 2003 to 279 (14.9%) in 2007, no other matter reported to ComSet comprised more than 6% in any particular year. That said, this should not detract from the fact that the percentage of Internal Investigations relating to the more serious criminal and quasi-criminal offences increased (except in 2004) from a low of 57 (2.1%) in 2003, to a high of 107 (5.7%) in 2007. However, the actual number of Criminal Charges reported to ComSet were fewer than 12 (less than .5%) for any given year. This finding points to the possibility that Member firms were more inclined to conduct their own investigations and deal with registrants internally, rather than turning them over to the IDA, securities commissions, and/or the criminal justice system.

There was no particular trend in the number of events reported to ComSet pertaining to External and Internal Disciplinary Actions. The number of External
Disciplinary Actions that were referred to an external regulatory body increased continuously from 10 (0.4%) in 2003, to 25 (1.3%) in 2006, before decreasing to 15 (0.8%) in 2007. Internal Disciplinary Actions taken by Member firms against registrants increased from 26 (1%) in 2003, to 44 (2.3%) in 2004, then steadily decreased to 38 (2.1%) in 2005, 31 (1.6%) in 2006, and 29 (1.6%) in 2007.

Table 6-2  Subject Nature of ComSet Events Reported

<table>
<thead>
<tr>
<th>Type of Events Reported</th>
<th>2003</th>
<th></th>
<th>2004</th>
<th></th>
<th>2005</th>
<th></th>
<th>2006</th>
<th></th>
<th>2007</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Count</td>
<td>Percent</td>
<td>Count</td>
<td>Percent</td>
<td>Count</td>
<td>Percent</td>
<td>Count</td>
<td>Percent</td>
<td>Count</td>
<td>Percent</td>
</tr>
<tr>
<td>Unsuitable Investment</td>
<td>1249</td>
<td>46.8</td>
<td>776</td>
<td>40.9</td>
<td>732</td>
<td>39.8</td>
<td>779</td>
<td>40.3</td>
<td>734</td>
<td>39.3</td>
</tr>
<tr>
<td>Unauthorized and Discretionary Trading</td>
<td>338</td>
<td>12.7</td>
<td>231</td>
<td>12.2</td>
<td>313</td>
<td>17</td>
<td>226</td>
<td>11.7</td>
<td>203</td>
<td>10.9</td>
</tr>
<tr>
<td>Misrepresentation</td>
<td>120</td>
<td>4.5</td>
<td>79</td>
<td>4.2</td>
<td>92</td>
<td>5</td>
<td>94</td>
<td>4.9</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Disputed fees, commissions, and charges</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>130</td>
<td>7</td>
</tr>
<tr>
<td>Transfer of Accounts</td>
<td>36</td>
<td>1.4</td>
<td>38</td>
<td>2</td>
<td>32</td>
<td>1.7</td>
<td>79</td>
<td>4.1</td>
<td>76</td>
<td>4.1</td>
</tr>
<tr>
<td>Others</td>
<td>927</td>
<td>34.7</td>
<td>772</td>
<td>40.7</td>
<td>672</td>
<td>36.5</td>
<td>754</td>
<td>39</td>
<td>727</td>
<td>38.9</td>
</tr>
<tr>
<td>Total</td>
<td>2670</td>
<td>100</td>
<td>1896</td>
<td>100</td>
<td>1841</td>
<td>100</td>
<td>1932</td>
<td>100</td>
<td>1870</td>
<td>100</td>
</tr>
</tbody>
</table>

Table 6-2 indicates that Unsuitable Investments and Unauthorized and Discretionary Trading were the events most reported to ComSet. The reporting of Unsuitable Investments decreased from 1,249 (46.8%) in 2003 to 734 (39.3%) in 2007. Reports concerning Unauthorized and Discretionary Trading fluctuated throughout the five year period. From 338 (12.7%) in 2003, the number of Unauthorized and Discretionary Trading reports decreased to 231 (12.2%) in 2004 and increased again to 313 (17%) in 2005, and decreased steadily to 226 (11.7%) in 2006 and 203 (10.9%) in 2007. The “Others” category in Table 6-2, “ refers to 21 different types of allegations

81 Data on disputed fees, commissions and charges were only available for 2007.
that can be identified as regulatory, civil or criminal in nature and may cover any of the thousands of types of requirements under IDA rules, marketplace rules, securities law or other legislation" (IDA, 2008b: 7). In interpreting the data presented in Table 6-2, “[i]t should be noted that the events reported on ComSet have not been initially assessed for validity of the underlying allegation” as such, “many matters when assessed are in fact found to be unwarranted or that there is insufficient evidence to establish the allegation” (p. 7).

**Case Assessment**

The “Case Assessment Group is responsible for receiving cases from the public, ComSet and other regulators” (IDA, 2008b: 9). In the Case Assessment Group, the IDA Officers will initiate the opening of a file. They are then responsible to assess if the matter is within the jurisdiction of the IDA or some other agency. If the matter is not in the jurisdiction of the IDA, they will make a direct referral to the agency that does have jurisdiction. If the matter is not law enforcement or a regulatory issue, the matter may be referred back to the firm to resolve. If it is merely an information request, the caller will be directed to the appropriate IDA department or otherwise referred. Where matters are regulatory and in the IDA’s jurisdiction, Case Assessment officers will conduct a preliminary investigation. The preliminary investigation will determine if there is likelihood of evidence and a case that is viable. If the matter is merely a technical breach with no harm to investors or others, the matter may be closed with a cautionary letter. In other cases, Case Assessment officers will request relative documentation from the client and the firm (IDA, 2008b: 9).

**Table 6-3**  Types and Percentage of Complaints (by Issue) Opened by the Case Assessment Group from January 01 – December 31

<table>
<thead>
<tr>
<th>Complaints of File Open by Issue</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adequacy of books and records</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>N</td>
<td>16</td>
<td>9</td>
<td>6</td>
<td>4</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td>%</td>
<td>1.5</td>
<td>0.6</td>
<td>0.5</td>
<td>0.3</td>
<td>0.4</td>
<td>0.5</td>
</tr>
<tr>
<td>Capital deficiency</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>N</td>
<td>13</td>
<td>12</td>
<td>4</td>
<td>6</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td>%</td>
<td>1.2</td>
<td>0.8</td>
<td>0.3</td>
<td>0.5</td>
<td>0.4</td>
<td>0.3</td>
</tr>
<tr>
<td>Complaints of File Open by Issue</td>
<td>2002</td>
<td>2003</td>
<td>2004</td>
<td>2005</td>
<td>2006</td>
<td>2007</td>
</tr>
<tr>
<td>---------------------------------</td>
<td>--------</td>
<td>--------</td>
<td>--------</td>
<td>--------</td>
<td>--------</td>
<td>--------</td>
</tr>
<tr>
<td></td>
<td>N</td>
<td>%</td>
<td>N</td>
<td>%</td>
<td>N</td>
<td>%</td>
</tr>
<tr>
<td>Churning and excessive trading</td>
<td>7</td>
<td>0.7</td>
<td>16</td>
<td>1.0</td>
<td>14</td>
<td>1.1</td>
</tr>
<tr>
<td>Client priority rule violation</td>
<td>3</td>
<td>0.3</td>
<td>1</td>
<td>0.1</td>
<td>3</td>
<td>0.2</td>
</tr>
<tr>
<td>Conflict of interest</td>
<td>10</td>
<td>0.9</td>
<td>24</td>
<td>1.5</td>
<td>11</td>
<td>0.8</td>
</tr>
<tr>
<td>Failure to comply with policy 8</td>
<td>0</td>
<td>0.0</td>
<td>5</td>
<td>0.3</td>
<td>4</td>
<td>0.3</td>
</tr>
<tr>
<td>Falsification/forgeiry of documenta</td>
<td>17</td>
<td>1.6</td>
<td>25</td>
<td>1.6</td>
<td>15</td>
<td>1.1</td>
</tr>
<tr>
<td>Files with No Violation Assigned</td>
<td>1</td>
<td>0.1</td>
<td>0</td>
<td>0.0</td>
<td>2</td>
<td>0.2</td>
</tr>
<tr>
<td>Inaccurate information on registrant application</td>
<td>6</td>
<td>0.6</td>
<td>3</td>
<td>0.2</td>
<td>4</td>
<td>0.3</td>
</tr>
<tr>
<td>Inaccurate information on Termination Notice</td>
<td>2</td>
<td>0.2</td>
<td>2</td>
<td>0.1</td>
<td>0</td>
<td>0.0</td>
</tr>
<tr>
<td>Inappropriate personal financial dealings</td>
<td>19</td>
<td>1.8</td>
<td>47</td>
<td>3.0</td>
<td>26</td>
<td>2.0</td>
</tr>
<tr>
<td>Insider trading/self dealing</td>
<td>7</td>
<td>0.7</td>
<td>11</td>
<td>0.7</td>
<td>12</td>
<td>0.9</td>
</tr>
<tr>
<td>Internal control violations</td>
<td>26</td>
<td>2.4</td>
<td>23</td>
<td>1.5</td>
<td>20</td>
<td>1.5</td>
</tr>
<tr>
<td>Manipulation &amp; wash trading</td>
<td>17</td>
<td>1.6</td>
<td>25</td>
<td>1.6</td>
<td>19</td>
<td>1.5</td>
</tr>
<tr>
<td>Margin Issues</td>
<td>51</td>
<td>4.8</td>
<td>27</td>
<td>1.7</td>
<td>4</td>
<td>0.1</td>
</tr>
<tr>
<td>Misappropriation of funds or securities</td>
<td>3</td>
<td>0.3</td>
<td>10</td>
<td>0.6</td>
<td>4</td>
<td>0.1</td>
</tr>
<tr>
<td>Misrepresentation</td>
<td>30</td>
<td>2.8</td>
<td>145</td>
<td>9.2</td>
<td>114</td>
<td>8.7</td>
</tr>
<tr>
<td>Money Laundering</td>
<td>1</td>
<td>0.1</td>
<td>2</td>
<td>0.1</td>
<td>2</td>
<td>0.2</td>
</tr>
<tr>
<td>Other</td>
<td>0</td>
<td>0.0</td>
<td>208</td>
<td>13.8</td>
<td>2</td>
<td>0.2</td>
</tr>
<tr>
<td>Poor performance</td>
<td>27</td>
<td>2.5</td>
<td>57</td>
<td>3.6</td>
<td>17</td>
<td>1.3</td>
</tr>
<tr>
<td>Principal/agent issues</td>
<td>0</td>
<td>0.0</td>
<td>0</td>
<td>0.0</td>
<td>2</td>
<td>0.2</td>
</tr>
<tr>
<td>Prospectus, exemptions and related matters</td>
<td>7</td>
<td>0.7</td>
<td>7</td>
<td>0.4</td>
<td>5</td>
<td>0.4</td>
</tr>
</tbody>
</table>
Complaints of File Open by Issue

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>N</td>
<td>%</td>
<td>N</td>
<td>%</td>
<td>N</td>
<td>%</td>
</tr>
<tr>
<td>Service issues</td>
<td>101</td>
<td>9.4</td>
<td>90</td>
<td>5.7</td>
<td>121</td>
<td>9.2</td>
</tr>
<tr>
<td>Supervision</td>
<td>12</td>
<td>1.1</td>
<td>31</td>
<td>2.0</td>
<td>40</td>
<td>3.1</td>
</tr>
<tr>
<td>Theft or fraudulent activities</td>
<td>31</td>
<td>2.9</td>
<td>29</td>
<td>1.8</td>
<td>18</td>
<td>1.4</td>
</tr>
<tr>
<td>Trading outside jurisdiction</td>
<td>4</td>
<td>0.4</td>
<td>5</td>
<td>0.3</td>
<td>3</td>
<td>0.2</td>
</tr>
<tr>
<td>Transfer of accounts</td>
<td>40</td>
<td>3.7</td>
<td>30</td>
<td>1.9</td>
<td>27</td>
<td>2.1</td>
</tr>
<tr>
<td>Unauthorized or discretionary trading</td>
<td>119</td>
<td>11.1</td>
<td>420</td>
<td>26.7</td>
<td>311</td>
<td>23.7</td>
</tr>
<tr>
<td>Undetermined</td>
<td>99</td>
<td>9.2</td>
<td>21</td>
<td>1.3</td>
<td>38</td>
<td>2.9</td>
</tr>
<tr>
<td>Unsuitable investment</td>
<td>243</td>
<td>22.7</td>
<td>281</td>
<td>17.8</td>
<td>30</td>
<td>1.9</td>
</tr>
<tr>
<td>Uniform Termination Notice</td>
<td>145</td>
<td>13.5</td>
<td>2</td>
<td>0.1</td>
<td>0</td>
<td>0.0</td>
</tr>
<tr>
<td>Violation of Commissions' or other SROs' Orders</td>
<td>7</td>
<td>0.7</td>
<td>2</td>
<td>0.1</td>
<td>1</td>
<td>0.1</td>
</tr>
<tr>
<td>Violation of IDA's orders</td>
<td>9</td>
<td>0.8</td>
<td>5</td>
<td>0.3</td>
<td>1</td>
<td>0.1</td>
</tr>
<tr>
<td>Total</td>
<td>1073</td>
<td>100</td>
<td>1575</td>
<td>100</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

In total, there were 7,765 complaints “funnelled in” by the Case Assessment Group between 2002 and 2007. That is an average of about 1,294 complaints per year. The most common complaints opened by the Case Assessment Group over the six year period were complaints relating to improper sales practices, misrepresentation, and service related issues. As shown in Table 6-3, complaints related to unsuitable investments decreased by close to half from 2002 when there were 243 (22.7%), to only 140 (11.5%) in 2007. Even though complaints decreased, unsuitable investments were

82 The figure reported in Table 6-3 for service related issues, might not reflect the true number of complaints because Policy 8 clearly states that service related complaints should not be reported on ComSet (see IDA, 2006d). As such, the service related complaints processed by the Case Assessment Group are probably the ones that were reported directly to the IDA from the public and other regulatory bodies.
still among the top two complaints opened by the Case Assessment Group throughout the five year period. On the other hand, complaints related to unauthorized and discretionary trading increased by more than half from 119 (11.1%) in 2002, to 301 (24.7%) in 2007. Service related complaints such as the mishandling of cheques and other customer related issues, fluctuated throughout. With the exception of 2003, when they were 90 (5.7%) and 2006 when they were 63 (4.8%), the number of service related complaints opened by a Case Assessment Group were over 100 in all of the other years.

Complaints related to misrepresentation of facts to clients and/or Member firms fluctuated throughout the six year period. From 30 (2.8%) in 2002, the number of complaints increased to 145 (9.2%) in 2003, decreased to 114 (8.7%) in 2004 and 99 (7.8%) in 2005, before increasing again to 117 (8.9%) in 2006 and 129 (10.6%) in 2007. As shown in Table 6-4 below, with the exception of 2002 (uniform termination notice), unauthorized and discretionary trading and unsuitable investments remained the top two complaints, while misrepresentation and service related issues round off the top four for the six year period.

Table 6-4  Top Four Complaints Received by the Case Assessment Group from 2002-2007

<table>
<thead>
<tr>
<th>Year</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>Unsuitable Investments</td>
<td>Uniform Termination Notice</td>
<td>Unauthorized and discretionary trading</td>
<td>Service issues</td>
</tr>
<tr>
<td>2003</td>
<td>Unauthorized and discretionary trading</td>
<td>Unsuitable investments</td>
<td>Misrepresentation</td>
<td>Service issues</td>
</tr>
<tr>
<td>2004</td>
<td>Unauthorized and discretionary trading</td>
<td>Unsuitable investments</td>
<td>Service issues</td>
<td>Misrepresentation</td>
</tr>
<tr>
<td>2005</td>
<td>Unauthorized and discretionary trading</td>
<td>Unsuitable investments</td>
<td>Service issues</td>
<td>Misrepresentation</td>
</tr>
<tr>
<td>2006</td>
<td>Unauthorized and discretionary trading</td>
<td>Unsuitable investments</td>
<td>Misrepresentation</td>
<td>Service issues</td>
</tr>
</tbody>
</table>
### Case Assessment Summary

Table 6-5 shows the number of files opened and closed by the Case Assessment Group from 2002 to 2007. With the exception of 2007, the IDA was able to deal with and close more than 85% of the complaints opened by the Case Assessment Group during that period. By combining the number of complaints received from ComSet with those from the public and other regulatory agencies, the IDA is in a better position to “funnel in” and deal with more complaints. Investors have more avenues to report misconduct and as such, the IDA is able to “funnel in” more complaints that may not have otherwise come to their attention. It is expected that the complaints with enough evidence for charges to be laid, will make their way down the disciplinary process and “[in] the long run…should actually increase consumer satisfaction and decrease the number of complaints” (see Brockman, 2004: 72).

### Table 6-5  Total Files Opened and Closed by Case Assessment Group from 2002-2007

<table>
<thead>
<tr>
<th>Year</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>Unauthorized and discretionary trading</td>
<td>Unsuitable investments</td>
<td>Misrepresentation</td>
<td>Service issues</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>As at</th>
<th>Open at Jan 1</th>
<th>Received During Period</th>
<th>Total open files during period</th>
<th>Closed During Period</th>
<th>Open at End of Period</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec 31 2002</td>
<td>134</td>
<td>1073</td>
<td>1207</td>
<td>1037 (85.9%)</td>
<td>170 (14.1%)</td>
</tr>
<tr>
<td>Dec 31 2003</td>
<td>170</td>
<td>1506</td>
<td>1676</td>
<td>1521 (90.8%)</td>
<td>155 (9.2%)</td>
</tr>
<tr>
<td>Dec 31 2004</td>
<td>155</td>
<td>1254</td>
<td>1409</td>
<td>1230 (87.3%)</td>
<td>179 (12.7%)</td>
</tr>
<tr>
<td>Dec 31 2005</td>
<td>199</td>
<td>1237</td>
<td>1436</td>
<td>1279 (89.1%)</td>
<td>157 (10.9%)</td>
</tr>
<tr>
<td>Dec 31 2006</td>
<td>183</td>
<td>1269</td>
<td>1452</td>
<td>1260 (86.8%)</td>
<td>192 (13.2%)</td>
</tr>
<tr>
<td>Dec 31 2007</td>
<td>196</td>
<td>1155</td>
<td>1351</td>
<td>1100 (81.4%)</td>
<td>251 (18.6%)</td>
</tr>
</tbody>
</table>
The Funnel Process: Funnel Out

Once the cases enter the system, there is the possibility that offenders may escape disciplinary actions by being “funnelled out” and thus, “escap[ing] the net of social control” (Brockman, 2004: 73; Brockman & McEwen, 1990: 15). There is also the possibility that offenders may be given lenient penalties by the disciplinary committee (Brockman, 2004: 73). But before a complaint reaches the disciplinary committee, complaints must first go through two additional hurdles: investigation and prosecution stages (e.g., see Brockman, 2004: 73). At the investigation stage, the IDA’s investigative staff must establish that the case has sufficient evidence before it can be sent to Enforcement Counsel for prosecution (IIROC, 2008c: 2).

Investigation

It can be argued that the “funnelling out” of complaints starts at the Case Assessment stage. As mentioned earlier, some complaints may not be “within the jurisdiction of the IDA,” or some may not be “a regulatory issue [that] "warrants further investigation” (IDA, 2008b: 9). Complaints that fall into these categories are either closed or sent to the appropriate body (p.9). That said,

Once the preliminary investigation is completed by the Case Assessment Group, a recommendation is made to senior management to either close a matter with no action, to issue a cautionary letter, or refer the matter to investigations. IDA investigators are formed into multidisciplinary teams that include individuals with various backgrounds and skills (IDA, 2008b: 12).

The team consists of

forensic accountants, professional investigators who have worked with policing agencies, revenue agencies, and securities commissions or in private practice, industry specialists, and lawyers. Files are assigned to a lead investigator who will prepare an investigation plan and then conduct
the investigation by reviewing and analyzing documentation including financial statements; obtaining further documents from firms and individuals; conducting interviews; and, ultimately, interviewing potential respondents (p.12).

Once the investigation is completed, "a detailed investigation report will be prepared with recommendation[s] that the matter be closed with no further action due to lack of evidence; issu[ance of] a cautionary letter; or refer[al of] the matter to Prosecution for possible formal disciplinary action" (p.12).

**Investigation Summary**

**Table 6-6**  
Total Files Opened and Closed by Investigation Unit from 2002-2007

<table>
<thead>
<tr>
<th>As at</th>
<th>Open at Beginning of Period (Jan 1)</th>
<th>Received During Period</th>
<th>Total open files during period</th>
<th>Closed During Period</th>
<th>Open at End of Period</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec 31 2002</td>
<td>182</td>
<td>138</td>
<td>320</td>
<td>214 (66.9%)</td>
<td>106 (33.1%)</td>
</tr>
<tr>
<td>Dec 31 2003</td>
<td>106</td>
<td>166</td>
<td>272</td>
<td>162 (59.6%)</td>
<td>110 (40.4%)</td>
</tr>
<tr>
<td>Dec 31 2004</td>
<td>112</td>
<td>129</td>
<td>241</td>
<td>156 (64.7%)</td>
<td>85 (35.3%)</td>
</tr>
<tr>
<td>Dec 31 2005</td>
<td>85</td>
<td>212</td>
<td>297</td>
<td>134 (45.1%)</td>
<td>163 (54.9%)</td>
</tr>
<tr>
<td>Dec 31 2006</td>
<td>163</td>
<td>154</td>
<td>317</td>
<td>188 (59.3%)</td>
<td>129 (40.7%)</td>
</tr>
<tr>
<td>Dec 31 2007</td>
<td>130</td>
<td>148</td>
<td>278</td>
<td>141 (50.7%)</td>
<td>137 (49.3%)</td>
</tr>
</tbody>
</table>

As shown in Table 6-6, the number of files closed by the investigation unit was rather inconsistent throughout the five year period. In 2002, the number of files closed was at its highest, reaching a peak of 214 (66.9%) and then decreasing to 162 (59.6%) in 2003. While the number of files closed in 2004 was 156, the percentage of files closed that year increased to 64.7%. In 2005, the number of files closed decreased drastically.

---

83 In interpreting these findings, it is important to point out that some of the files that were closed in a particular year were in fact open in the previous year. For example, some of the files that were closed in 2003, were really opened in 2002.
to 134 (45.1%), then increased again to 188 (59.3%) in 2006, before declining to 141 (50.7%) in 2007. The inconsistency shown above should not detract from the fact that the number of cases continued to shrink as they were processed through the IDA’s enforcement system.

The nature of the complaints changed, as the cases moved from the Case Assessment Group to Investigations. As mentioned before, the top four complaints handled by the Case Assessment Group were unauthorized and discretionary trading, unsuitable investments, misrepresentation and service issues (see Table 6-4). As can be seen in Table 6-7 below, while unauthorized and discretionary trading and unsuitable investments remained in the top four, they were no longer the top two complaints dealt with by the Investigation staff throughout the six year period. Rather, the top two complaints for each year were a mixed bag comprised of unauthorized and discretionary trading and unsuitable investments, as well as issues related to supervision, inappropriate personal financial dealings and theft and fraudulent activities. Other complaints that made up the top four that were sent to investigation were forgery, manipulation and wash trading, and conflict of interest. Noticeably missing from the top four complaints were misrepresentation and service related complaints. Since service related complaints are not seen as regulatory issues by the IDA, it is expected that they would not make it through to the Investigation unit. Misrepresentation of facts to clients, on the other hand, is seen as a regulatory issue and constitutes one of the regulatory offences under the IDA's Sanction Guidelines (see IDA, 2006b: 46). One can only speculate that complaints regarding misrepresentation were disposed of at the case assessment stage, either because there was not enough evidence to build a case or the matters were classified as technical breaches with no harm to investors and closed with a cautionary letter (see IDA, 2008b: 9).
Table 6-7  Top Four Issues Referred to Investigation from 2003-2007

<table>
<thead>
<tr>
<th>Year</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>Unsuitable investments</td>
<td>Unauthorized and discretionary trading</td>
<td>Supervision</td>
<td>Falsification/forgery</td>
</tr>
<tr>
<td>2004</td>
<td>Supervision</td>
<td>Inappropriate personal financial dealings</td>
<td>Unauthorized and discretionary trading</td>
<td>Supervision</td>
</tr>
<tr>
<td>2005</td>
<td>Supervision</td>
<td>Unsuitable investments</td>
<td>Unauthorized and discretionary trading</td>
<td>Manipulation and wash trading</td>
</tr>
<tr>
<td>2006</td>
<td>Supervision</td>
<td>Theft and fraudulent activities</td>
<td>Unsuitable investments</td>
<td>Unauthorized and discretionary trading</td>
</tr>
<tr>
<td>2007</td>
<td>Supervision</td>
<td>Unauthorized and discretionary trading</td>
<td>Conflict of Interest</td>
<td>Unsuitable investments</td>
</tr>
</tbody>
</table>

IDA Internal Prosecution

Files referred from Investigations are then reviewed by the IDA Enforcement Counsel (IIROC, 2008c: 2). The IDA

Enforcement Counsel undertakes a full review of the file to assess the evidence available, potential credibility and weight of witness statements, and any other factors which could be used to prove a case. Counsel will then determine if there is sufficient evidence to meet the legal test to prove a case and whether there is a reasonable probability of successful prosecution. If the matter does meet the test, there may be a recommendation to close the matter with a warning letter. If there is insufficient evidence, the matter may be closed with no further action or referred back to investigation for further inquiries. If there appears to be sufficient evidence and there is a reasonable probability of proving the case in a contested hearing, Counsel will prepare their recommendation for senior management (IDA, 2008b: 35-36).

Counsel recommendations will include

the sanction that is being recommended should a finding against the firm or individual be proven. Senior managers will review the recommendation and provide instructions to enforcement counsel. Where appropriate, counsel may contact the respondent’s counsel to determine if there is an

---

84 Prosecution refers to an internal department of the IDA, and not criminal prosecution.
interest to settle the matter without need to resorting to a contested hearing. If there is, a settlement agreement may be negotiated and, ultimately, put before a hearing panel for their acceptance or rejection. If rejected, the matter may be renegotiated and brought back to another panel or the matter may proceed to a contested hearing (p. 36).

**Prosecution Summary**

Table 6-8  Results of Cases that were Referred to Enforcement Counsel for Prosecution from 2002-2007

<table>
<thead>
<tr>
<th>As at</th>
<th>Open at beginning of period (Jan. 1)</th>
<th>Receive d during period</th>
<th>Total files opened</th>
<th>With No Action</th>
<th>With Action &amp; Warning Letters</th>
<th>Stayed</th>
<th>Dismissal</th>
<th>Total closed during period</th>
<th>Open at End of Period</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec 31 2002</td>
<td>209</td>
<td>86</td>
<td>295</td>
<td>41</td>
<td>147</td>
<td>17</td>
<td>1</td>
<td>188</td>
<td>107</td>
</tr>
<tr>
<td>Dec 31 2003</td>
<td>107</td>
<td>137</td>
<td>244</td>
<td>31</td>
<td>90</td>
<td>12.7%</td>
<td>1</td>
<td>121</td>
<td>123</td>
</tr>
<tr>
<td>Dec 31 2004</td>
<td>121</td>
<td>88</td>
<td>209</td>
<td>17</td>
<td>101</td>
<td>8.1%</td>
<td>1</td>
<td>121</td>
<td>88</td>
</tr>
<tr>
<td>Dec 31 2005</td>
<td>87</td>
<td>71</td>
<td>158</td>
<td>14</td>
<td>63</td>
<td>8.9%</td>
<td>1</td>
<td>84</td>
<td>74</td>
</tr>
<tr>
<td>Dec 31 2006</td>
<td>73</td>
<td>118</td>
<td>191</td>
<td>10</td>
<td>69</td>
<td>5.2%</td>
<td>1</td>
<td>82</td>
<td>109</td>
</tr>
<tr>
<td>Dec 31 2007</td>
<td>106</td>
<td>70</td>
<td>176</td>
<td>12</td>
<td>59</td>
<td>6.8%</td>
<td>1</td>
<td>71</td>
<td>97</td>
</tr>
</tbody>
</table>

Once a complaint reaches Prosecution, it faces further hurdles (see Brockman, 2004: 73). At the Prosecution stage, the IDA Enforcement Counsel will consider the recommendations made by the Investigation unit and decide how to proceed with them. As shown in Table 6-8, Enforcement Counsel continued to “funnel out” investors’ complaints by closing a significant amount of complaints at the Prosecution stage.

85 The number of cases stayed and/or dismissed for 2007 was not recorded in the IDA’s 2007 annual report. One can only assume that for various reasons, the IDA chooses not to record these because the number of cases left open at the end of 2007 should have been calculated as follows: (176-71 = 105 instead of 97).
without further action. Enforcement Counsel was at its busiest in 2002, when they closed 188 (63.7%) of the cases. The number of cases closed decreased to 121 (49.6%) in 2003, and although the same number of cases were closed for 2004, the percentage increased to 57.9%. Thereafter, the number of cases closed decreased from 84 (53.2%) in 2005, to 82 (42.9%) in 2006, and to 71 (40.3%) in 2007. Of the cases that were closed during the six year period, most were closed “with actions and warning letters.” The highest number of cases closed with “actions and warning letters” was in 2002 and 2004, when 147 (49.8%) and 101 (48.3%) cases were closed respectively. Only a small number of cases were closed with no further action, with the highest number being 41 (13.9%) in 2002. As was seen in the Case Assessment and Investigation stages, Enforcement Counsel continued with the trend to dispose of complaints informally.

Table 6-9 shows the types of complaints that were referred to Prosecution. While unsuitable investments were one of the top four complaints dealt with at both the Case Assessment and Investigation stages, it was noticeably missing as one of the top four complaints that made their way to Prosecution. A few reasons have been put forth for this outcome. It is noted that unsuitable investments can be measured in shades of grey. In other words, there may not be the necessary clear and cogent evidence that would result in a hearing likely to be successful. The result is that the matters may be resolved through informal resolution or closed with no action. In other circumstances complaints about suitability are not in fact about suitability at all but merely reflective of general market conditions… (Condon and Puri: 2006: 33).

In other scenarios, “enforcement counsel may review a number of allegations that have been investigated and use discretion as to which complaints to proceed with and which files to close” (p.33). There are also instances where the
decisions about prosecuting are effectively made for the regulator. This occurs when clients withdraw their complaints or refuse to attend as witnesses. Case law suggests that in the absence of a client witness it is very difficult to prove a case of suitability. Where witnesses are compensated, the monetary incentive for them to provide assistance in a regulatory hearing disappears, and in many of those circumstances the regulator is unable to proceed with the prosecution (p. 33).

There is also the possibility that the complaint might not be related to suitability issues at all. “During the course of investigation,” Enforcement Counsel may uncover evidence that would suggest the matter is not a suitability matter but instead a different type of misconduct, or that there are more serious allegations that subsume the suitability complaints. In such cases[,] many suitability matters may in fact be contained in the more serious allegations or it might be converted to other types of regulatory breaches such as conduct unbecoming (p. 34).

All of the above are possible explanations as to why complaints related to unsuitable investments are disposed of before they reach the Prosecution stage of the IDA’s enforcement process.

**Table 6-9  ** Top Four Issues Referred to Prosecution from 2003-2007 by Hearing Panels

<table>
<thead>
<tr>
<th>Year</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>Unauthorized and discretionary trading</td>
<td>Supervision</td>
<td>Falsification/forgery</td>
<td>Capital deficiencies</td>
</tr>
<tr>
<td>2004</td>
<td>Unauthorized and discretionary trading</td>
<td>Supervision</td>
<td>Falsification/forgery</td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>Supervision</td>
<td>Unauthorized and discretionary trading</td>
<td>Capital deficiency</td>
<td>Inappropriate personal financial dealings</td>
</tr>
<tr>
<td>2006</td>
<td>Supervision</td>
<td>Capital deficiencies</td>
<td>Falsification/forgery</td>
<td>Unauthorized and discretionary trading</td>
</tr>
<tr>
<td>2007</td>
<td>Theft and fraudulent activities</td>
<td>Supervision</td>
<td>Capital deficiency and Manipulation and wash trading</td>
<td>Unauthorized and discretionary trading</td>
</tr>
</tbody>
</table>
**Imposition of Penalties**

**Table 6-10 Penalties Assessed on Individual Offenders by Hearing Panels**

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fines</td>
<td>$2,292,000</td>
<td>$2,401,250</td>
<td>$4,147,000</td>
<td>$2,142,500</td>
<td>$3,092,500</td>
<td>$1,817,712</td>
<td>$15,892,962</td>
</tr>
<tr>
<td>Costs</td>
<td>$323,400</td>
<td>$531,035</td>
<td>$773,015</td>
<td>$392,797</td>
<td>$490,744</td>
<td>$478,718</td>
<td>$2,989,709</td>
</tr>
<tr>
<td>Disgorgement</td>
<td>$34,740</td>
<td>$312,996</td>
<td>$573,881</td>
<td>$653,862</td>
<td>$507,055</td>
<td>$133,669</td>
<td>$2,216,203</td>
</tr>
<tr>
<td>Total Decisions</td>
<td>46</td>
<td>41</td>
<td>64</td>
<td>42</td>
<td>32</td>
<td>42</td>
<td>267</td>
</tr>
<tr>
<td>Average Fine</td>
<td>$49,826</td>
<td>$58,567</td>
<td>$64,797</td>
<td>$51,012</td>
<td>$96,641</td>
<td>$43,279</td>
<td></td>
</tr>
<tr>
<td>Median Fine</td>
<td>$25,000</td>
<td>$30,000</td>
<td>$25,000</td>
<td>$35,000</td>
<td>$27,500</td>
<td>$35,000</td>
<td></td>
</tr>
<tr>
<td>Average Cost</td>
<td>$7,030</td>
<td>$12,952</td>
<td>$12,078</td>
<td>$9,352</td>
<td>$15,336</td>
<td>$11,398</td>
<td></td>
</tr>
<tr>
<td>Median Cost</td>
<td>$5,000</td>
<td>$5,000</td>
<td>$7,500</td>
<td>$8,362</td>
<td>$5,000</td>
<td>$10,000</td>
<td></td>
</tr>
<tr>
<td>Warning Letters</td>
<td>76</td>
<td>27</td>
<td>19</td>
<td>8</td>
<td>22</td>
<td>8</td>
<td>160</td>
</tr>
<tr>
<td>Suspensions</td>
<td>10</td>
<td>2</td>
<td>7</td>
<td>11</td>
<td>14</td>
<td>15</td>
<td>59</td>
</tr>
<tr>
<td>Conditions</td>
<td>25</td>
<td>19</td>
<td>37</td>
<td>30</td>
<td>28</td>
<td>26</td>
<td>165</td>
</tr>
<tr>
<td>Permanent Bars</td>
<td>6</td>
<td>9</td>
<td>17</td>
<td>14</td>
<td>9</td>
<td>9</td>
<td>64</td>
</tr>
</tbody>
</table>

Table 6-10 shows the total decisions completed by the IDA’s disciplinary committee for the period of 2002 to 2007. Judging from the number of cases completed, the IDA continued to informally process complaints before they reached a hearing panel. On average, only about 45 cases per year made their way to a disciplinary hearing between 2002 and 2007. This is a striking contrast to the number of complaints that were initially processed by the Case Assessment Group in Table 6-3, for the time interval being examined.

Table 6-10 also shows the penalties sanctioned and imposed by the IDA’s hearing panels from 2002-2007. With the exception of 2004 and 2006, when the total fines imposed were $4,147,000 and $3,092,500 respectively, the total fines imposed for the other years never exceeded $2.5 million. There was no discernable trend with the average fines imposed. Rather the average fines imposed fluctuated from a low of
$49,826 in 2002 to a high of $96,641 in 2006, and then went down to $43,279 in 2007. The median fine imposed throughout the period was within the $25,000 to $35,000 range, which constitutes only about 2.5% to 3.5% of the $1,000,000 maximum fines that can be imposed on individual offenders per offence.

The total costs for the investigations and prosecutions of the cases that offenders were ordered to pay to the Association, fluctuated throughout the six year period. Total costs were at their highest in 2004 at $773,015. This is not surprising, considering that the 64 disciplinary hearings conducted for 2004 were the highest number of cases heard over the six year timeframe. With the exception of 2006, when the average cost was $15,336, at no point throughout the six year period did the average cost exceed $15,000. On the same token, the median cost remained relatively constant throughout and never exceeded $10,000. One of the implications of these findings is that individual offenders cooperated with the investigation and as such, the IDA did not have to expend too many resources to investigate the offence(s) and prepare evidence for a hearing.

Of the other monetary penalties, disgorgement in 2004, 2005, and 2006 stands out. Disgorgement of commission or the act where an offender is required to repay the ill-gotten gains from his or her misconduct increased steadily from 2002 to 2005, before declining in 2006 and 2007. Disgorgement increased significantly from $34,740 in 2002 to $312,996 in 2003. From 2003, disgorgement increased to $573,881 in 2004 and $653,862 in 2005, before decreasing to $507,055 in 2006 and $133,669 in 2007. Notice also that with the exception of 2004 and 2006, there was no significant variation in the total number of cases heard; yet, there were considerable fluctuations in the amount of disgorgement imposed by hearing panels during the six year period. Given that disgorgement is seen as a sanction and not as a form of restitution under the Guidelines,
one can infer that there were a lot of offences committed in 2004, 2005 and 2006 where
the offenders profited from their misconduct (see IDA, 2006b: 12).\textsuperscript{86}

In addition to fines, costs and disgorgement, warning letters and terms and
conditions were the most frequent penalties imposed, followed by permanent bans from
the Association and a period of suspension from working in the industry. Of these, a
permanent ban is considered to be the most severe (see IDA, 2006b: 12). While a
permanent ban can be seen as both a specific and a general deterrent, and that the IDA
succeeded in getting rid of the individual from the industry, only 64 (or roughly 6
permanent bans per year) were imposed over the six year period.

\textbf{Table 6-11 Penalties Assessed on Member Firms}

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fines</td>
<td>$4,110,000</td>
<td>$191,654</td>
<td>$20,583,577</td>
<td>$1,046,596</td>
<td>$1,930,651</td>
<td>$1,045,000</td>
<td>$28,907,478</td>
</tr>
<tr>
<td>Costs</td>
<td>$337,675</td>
<td>$73,535</td>
<td>$280,069</td>
<td>$227,000</td>
<td>$98,241</td>
<td>$85,000</td>
<td>$1,101,520</td>
</tr>
<tr>
<td>Disgorgement</td>
<td>0</td>
<td>0</td>
<td>$20,978,577</td>
<td>$506,596</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Total Decisions</td>
<td>6</td>
<td>6</td>
<td>10</td>
<td>13</td>
<td>11</td>
<td>6</td>
<td>52</td>
</tr>
<tr>
<td>Average Fine</td>
<td>$685,000</td>
<td>$31,942</td>
<td>$2,068,358</td>
<td>$80,507</td>
<td>$175,514</td>
<td>$174,167</td>
<td>$21,485,173</td>
</tr>
<tr>
<td>Median Fine</td>
<td>$450,000</td>
<td>$50,000</td>
<td>$47,500</td>
<td>$50,000</td>
<td>$50,000</td>
<td>$50,000</td>
<td></td>
</tr>
<tr>
<td>Average Cost</td>
<td>$56,279</td>
<td>$12,256</td>
<td>$28,007</td>
<td>$17,462</td>
<td>$8,931</td>
<td>$14,167</td>
<td></td>
</tr>
<tr>
<td>Median Cost</td>
<td>$5,500</td>
<td>$12,173</td>
<td>$17,500</td>
<td>$35,000</td>
<td>$4,000</td>
<td>$15,000</td>
<td></td>
</tr>
<tr>
<td>Permanent Suspensions</td>
<td>2</td>
<td>0</td>
<td>0</td>
<td>2</td>
<td>0</td>
<td>1</td>
<td>5</td>
</tr>
</tbody>
</table>

\textsuperscript{86} There could also be other reasons why the IDA decided to order disgorgement. According to
the IDA’s Sanction Guidelines, “a Hearing Panel may require a respondent to pay an amount
equal to three times the profit made or the loss avoided by the respondent as a result of the
commission of the contravention in question, including any commissions earned, or other benefits
obtained from the impugned transactions” (IDA, 2006b: 12). A “Hearing Panel may consider
imposing a fine and requiring disgorgement even when a registrant is permanently barred in
egregious cases involving significant harm to clients and/or to the integrity of the securities
industry as a whole” (p. 12).

\textsuperscript{87} “Permanent suspension will end up in a termination or a winding up of the firm. Firms that wind
up are voluntarily released from the membership - expulsions are non-voluntary” (IDA, 2006e:
19).

114
Table 6-11 shows the penalties that were imposed on Member firms. On average, there were roughly 9 Member firm disciplined per year. Of striking contrast from all of the years is 2004, when the total fines imposed on Member firms were the highest at $20,583,577. With the exception of 2002, the total fines imposed on Member firms did not exceed $2 million dollars for any other year. Seeing that the total fines fluctuated significantly over the six year period, one would expect the average fines imposed to follow the same pattern. The average fines peaked at $2,058,358 in 2004; but, did not exceed the $1 million mark for any of the other years over the six year period. The median fines were at their highest in 2002, when they peaked at $450,000. With the exception of 2004, the median fines remained relatively stable at $50,000 for the other years. Even though the number of Member firm cases heard in 2004 was one more than the average, the disparity in fines over the six year period is partly due to the number of firms that were fined for market-timing offences in that year, for which harsher fines were imposed.

There was no discernable pattern in the costs that delinquent firms were ordered to pay to the Association during the six year period. As shown in Table 6-11, the costs awarded to the IDA were at their highest in 2002, when they were $337,675. The costs then decreased in 2003 to $73,535 and increased again to $280,069 in 2004. Thereafter the total costs decreased to $227,000 in 2005, $98,241 in 2006, and down to $85,000 in 2007. The average cost was at its highest in 2002 at $56,279. With the exception of 2004, the average costs did not exceed $20,000 for any of the other years. The median costs increased from $5,500 in 2002 to $35,000 in 2005, before decreasing again to $4,000 in 2006 and $15,000 in 2007. Since the average costs incurred by the IDA to

<table>
<thead>
<tr>
<th>Terminations</th>
<th>2</th>
<th>1</th>
<th>0</th>
<th>0</th>
<th>3</th>
<th>0</th>
<th>6</th>
</tr>
</thead>
<tbody>
<tr>
<td>Warning</td>
<td>16</td>
<td>13</td>
<td>5</td>
<td>8</td>
<td>11</td>
<td>4</td>
<td>57</td>
</tr>
</tbody>
</table>

| Letters      | 16| 13| 5 | 8 | 11| 4 | 57|
investigate and prosecute a case were on the lower side for most years, one can infer that the delinquent Members cooperated fully with the investigation, which saved the IDA from incurring further unnecessary expenses.

Another significant penalty given out was disgorgement. While data on disgorgement was only provided for two years, the amount of $20,978,577 imposed in 2004 was proportionate to the total fines of $20,583,577 imposed on Member firms for that year. One explanation for the linear relationship between total fines and disgorgement for 2004 is that the Member firms charged with market-timing offences had to disgorge the commissions earned from the misconduct.

Of the non-monetary penalties, warning letters were the most frequent sanctions imposed. From 2002 to 2007, the IDA’s hearing panels handed out 57 warning letters. That is an average of about 10 warning letters per year for Member firms. On the other hand, only 5 firms received permanent suspensions and 6 were terminated. A termination or a permanent ban on a Member firm is a serious penalty and is usually reserved for cases where

the public itself has been abused; where it is clear that a respondent’s conduct is indicative of a resistance to governance; the misconduct has an element of *criminal or quasi-criminal* activity; or there is reason to believe that the respondent could not be trusted to act in an honest and fair manner in all their dealings with the public, their clients, and the securities industry as a whole (IDA, 2006b: 12 emphasis added).

How am I supposed to interpret these findings? Am I supposed to believe that only 6 firms were involved in cases that deserved termination notices? Given that a considerable number of the complaints opened by the Case Assessment Group had criminal or quasi-criminal element to them, it is difficult to comprehend why only 6 firms were terminated. Or is it that the IDA will only go after its Members who violate rules
that warrants insignificant penalties such as warning letters? Whatever the reason, there was a litany of scandals involving brokerage firms in Canada within the last 10 years, and the fact that only 6 of them were terminated between 2002 and 2007 indicates that the IDA is reluctant to get tough with its Members.

Collection of Fines

Table 6-12  IDA’s Fine Collection

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Fines Levied</td>
<td>Fines Collected</td>
</tr>
<tr>
<td>April 1 2001-March 31, 2002</td>
<td>$4,309,000</td>
<td>$358,546</td>
</tr>
<tr>
<td>April 1, 2002-March 31, 2003</td>
<td>$3,581,500</td>
<td>$1,419,000</td>
</tr>
<tr>
<td>April 1, 2003-March 31, 2004</td>
<td>$2,875,904</td>
<td>$608,837</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$10,766,404</strong></td>
<td><strong>$2,386,383</strong></td>
</tr>
<tr>
<td>April 1 2005-Mar 31, 2006</td>
<td>$6,438,004</td>
<td>$966,000</td>
</tr>
<tr>
<td>April 1, 2006-March 31, 2007</td>
<td>$4,084,717</td>
<td>$2,429,000</td>
</tr>
<tr>
<td>April 1, 2007-March 31, 2008</td>
<td>$1,926,417</td>
<td>$1,828,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$12,449,138</strong></td>
<td><strong>$5,223,000</strong></td>
</tr>
</tbody>
</table>

Table 6-12 shows the total fines levied and the total collected by the IDA from April of 2001 to March 31, 2008, for both individual registrants and Member firms. The total fines levied and collected for the fiscal year of April 1, 2004 to March 31, 2005 are missing because the data was not available. In order to address the problem of individual registrants and Member Firms paying their fines at the end of the fiscal year in which fines were imposed, a lump-sum method was used to compare the fines levied and fines collected over the two (each being three years) time intervals. As shown in

88 These numbers only take into account investigation fines levied on individual offenders and Member firms. They did not take into account “the market-timing cases that resulted in several firms paying large fines” in 2005 and 2006 (see Baines, 2007: para. 26).
Table 6-12, the IDA was only able to collect 22% of all fines imposed from April 1, 2001 to March, 31, 2004. The percentage of fines collected increased to approximately 42% from April 1, 2005 to March, 31, 2008. What is clear from the findings is that for the entire time interval examined, the IDA at no point collected more than 50% of all of the fines that were imposed on the individual registrants and Member firms combined.

Collecting fines imposed on individual offenders is a reoccurring problem with the IDA. While Member firms almost always pay their fines, individual offenders charged with serious offences hardly ever pay theirs (FAIR Canada, 2011a: para. 3 and 5). The Canadian Foundation for Advancement of Investor Rights (“FAIR Canada”) “note[d] that the SROs' record of fine collection is quite good in respect of fines assessed against [M]ember firms with close to 100% collection rates” (2011a: para. 5). In the fiscal year April 1, 2007 to March 31, 2008 for example, the IDA “collected 85.7% of fines from firms and 31.38% of fines …from individual registrants” (IDA, 2008d: 14). The IDA’s inability to collect fines [from individual offenders] detracts from the credibility of the self-regulatory system which plays an important regulatory role in the Canadian securities industry. It also undermines securities regulation more broadly, particularly when the investing public hears of egregious cases where an individual who is the subject of a successful disciplinary action is able to dodge their punishment by simply walking away, and in some cases continues to work in the investment industry (FAIR Canada, 2011a: para. 4 emphasis added).

As such, the imposition of penalties on offenders “does not, in and of itself, prevent these individuals from continuing to harm investors,” and eventually only works to remove them from both the debt and equity markets (para.4).
Summary

This chapter examined the processing of initial complaints by the IDA’s Case Assessment Group to final disposition by Prosecution staff. To accomplish this task, I utilized the misconduct funnel to show the number of complaints “funnelled in” by the Case Assessment Group and how the number of complaints shrink as they are “funnelled out” by Investigation and Prosecution staff. I then did a lump sum analysis to determine the amount of fines collected by the IDA from 2002 to 2007. In the next chapter, I will look at the demographic profile of the victims, and characteristics of the offenders (individual and Member firm), along with the enforcement profile of the IDA.
Chapter 7: Data Analysis with Data from the IDA's Cases

This is the first of two chapters that will examine data from the IDA’s cases that were retrieved from Quicklaw’s database. In this chapter, I will use data from the cases to conduct a quantitative analysis on variables related to the victims, the offenders and the IDA’s enforcement process. In chapter 8, I will conduct a qualitative analysis with data from the IDA’s cases to examine the aggravating and mitigating factors that were considered in the imposition of the penalties.

Demographic Profile of Victims

In this section, where applicable, I will use descriptive statistics to compare the results of the IDA study with the 1999 Angus Reid Survey on the typical Canadian investor, and Boyd’s (2005) study on the Eron mortgage fraud.89 The 1999 Angus Reid survey was based on 1,500 Canadian investors (See Boyd, 2005: 12, footnote number six). Boyd’s (2005: 11) study was based on a “random sample of 559 respondents taken from a population of 2,800 investors in the Eron Mortgage fraud.”

89 The values in the tables and figures for this section are shown in percentages.
**Number of Investors per Case in the IDA Study**

![Graph showing distribution of number of investors per case in the IDA study.](image)

*Figure 7-1 Victims per Case*

Figure 7-1 shows the number of investors per case found through *Quicklaw* in the IDA study. Close to 88% of the cases contained anywhere between 0 to 5 victims. Of the remaining cases, 9.3% contained anywhere between 6-10 victims, while only 2.1% contained 11 to 15 victims. Less than 1% of cases contained between 16 to 20 and 21 to 25 victims. As can be seen below in Table 7-1, on average, there are 3 victims per case, with most cases dealing with only 1 victim. Given that the 1% of the cases with between 16 to 20 and 21 to 25 victims is pulling the average in the higher direction, the median number of 2 victims per case seems like a much more accurate summary.

---

90 There were three cases comprising 18, 29, and 97 victims respectively that were not included in Figure 7-1 either because they were eliminated, or if coded, they would have made the dataset unmanageable to work with.
Table 7-1  
Investors per Case in the IDA Study

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>N Valid Cases</td>
<td>429</td>
<td></td>
</tr>
<tr>
<td>N Missing Cases</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Mean</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Median</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Mode</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Minimum</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Maximum</td>
<td>24</td>
<td></td>
</tr>
<tr>
<td>Number of identified victims</td>
<td>1167</td>
<td></td>
</tr>
</tbody>
</table>

**Gender**

Of the 1,167 investors, data on gender was available for 1,026 (87.92%) of them. The gender of the other 141 (12.8%) investors could not be identified, because in some cases the IDA referred to the victims by their initials rather than their names. Out of the data in which the gender of the investors was identified, 581 (57%) were male, while 445 (43%) were female. The proportion of female victims in the IDA study is slighter higher than the proportion of females in the Eron study, where 39% were female (see Boyd, 2005: 12). The Eron study covered a period of four years, from 1993 (time of investment) to 1997 (time of collapse) (p. 12). Thus, the proportion of male and female victims reported in the Eron study was for the four year period in which they invested.

For a more accurate comparison that will reflect the Eron study timeline, I split the IDA study into two time intervals: from 1986 to 1997, and from 1998 to June of 2008. When I split the data, I found that the proportion of women affected in the IDA study increased by 7 percentage points from the first to the second time interval. More specifically, there

---

91 Boyd (2005) did not directly state that 39% of the investors in the Eron study were females. Rather he noted that “about 61per cent” of the investors were male (Boyd, 2005: 12). Since there was no mention of victims’ gender that cannot be identified, one can therefore deduce that 39% of the investors in the sample were females.
92 I split the time-interval starting from 1986, because the first case dealing with victims was in 1986.
were 224 (61%) male and 142 (39%) female victims between 1986 and 1997, while there were 357 (54%) male and 303 (46%) female victims between 1998 and June of 2008. Notice also that the proportion of male and female victims affected from 1986 to 1997 in the IDA study is the same as the proportion of male and female victims affected in the Eron study.

A few reasons have been presented to explain this outcome. Women are increasingly taking an active part in managing family finances and have the “disproportionate responsibility” of having to plan “for child and elderly care” within the family (see TD Waterhouse: 2006: para 5; Heminway, 2009: 310). Most women also live longer than men and more often than not, are married to men who are older than them (Nice, 2010: para. 5-7). These factors, along with the fact that the female labour force participation has been on the increase in Canada since the 1980’s, combines to explain the increasing number of women setting up financial plans to secure their financial independence (see Canadian Labour Congress, 2008: 3-4; TD Waterhouse, 2006: para. 6).

**Age**

As can be seen in Table 7-2, the age of the investors at the time of their investment in the IDA study, was remarkably different from the age of the investors in the Eron and the Typical Canadian Investor’s studies. The majority (60%) of the investors in the IDA study were over the age of 55, while 39% and 30% of investors in the Eron and the Typical Canadian Investor’s studies were over the age of 55. More than one-third or 36% of the investors in the IDA study were over 65 years of age, compared to 14% of Eron and 15% of the Typical Canadian Investors in the same age category. The findings of the IDA study compared to the Eron and Typical Canadian Investor’s
studies suggest that older individuals are much more likely to be the victims of securities infractions than their younger counterparts. Consequently, with only a few or no working years remaining, the infractions would have a greater impact on the lives of the IDA investors.

Table 7-2  Age of Investors in the Three Studies

<table>
<thead>
<tr>
<th>Age</th>
<th>IDA Study N=255</th>
<th>Eron’s Investor at the Time of investment</th>
<th>Typical Canadian Investor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under 45</td>
<td>22</td>
<td>25</td>
<td>52</td>
</tr>
<tr>
<td>45-54</td>
<td>18</td>
<td>25</td>
<td>17</td>
</tr>
<tr>
<td>55-64</td>
<td>24</td>
<td>25</td>
<td>15</td>
</tr>
<tr>
<td>65+</td>
<td>36</td>
<td>14</td>
<td>15</td>
</tr>
<tr>
<td>N/A</td>
<td>0</td>
<td>11</td>
<td>1</td>
</tr>
<tr>
<td>Total percent</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

**Investors’ Occupation and Knowledge**

Using Statistics Canada’s “National Occupational Classification for Statistics 2006 (NOC-S 2006),” investors’ job type will be classified into the following occupations: Management Occupations; Business, Finance and Administrative Occupations; Natural and Applied Sciences and Related Occupations; Health Occupations; Occupations in Social Science, Education, Government Service and Religion; Occupations in Art, Culture, Recreation and Sport; Sales and Service Occupations; Trades, Transport and Equipment Operators and Related Occupations; Occupations Unique to Primary Industry; and Occupations Unique to Processing, Manufacturing and Utilities (Statistic Canada, 2010).  

---

93 These figures “refer to the typical Canadian investor at the time of the Eron collapse” in 1997 (see Boyd, 2005: 12).
94 Statistics Canada does not include employees who are self-employed, unemployed or retired in
Figure 7-2  Investors’ Occupational Classification

For the first time in Canada, data is available to show the occupational classification of investors who were victims of securities infractions. As Figure 7-2 shows, 30% of investors were retired at the time of investment, while 18% worked in Management. Investors who worked in Business, Finance and Administration and Health services comprised 9% respectively. Other noteworthy occupational classifications were Sales and Services (8%), and Social Services, Education, Government, and Religion (6%). Investors who were self-employed comprised 7% of the victims. Of the remaining occupation classifications, none of them surpasses 5%.

The data is limited by missing data and the fact that many security infractions are probably never discovered and if they are discovered, many are not complained about or processed through the IDA’s enforcement system.
Not only were a significant proportion of the investors retired, but most of them were classified as unsophisticated. The IDA hearing panels referred to an unsophisticated investor as someone with “limited investment knowledge” and “no previous investment experience” in the securities industry (e.g., see IDA v. Schillaci, 2004: para. 31; IDA v. Tebbutt, 1990: para. 9; also see IDA v. Balanko, 2007: para. 88). As shown in Figure 7-3, 62% of the IDA’s investors were classified as unsophisticated and had limited investment knowledge. Of the others, 22% had average investment knowledge, while only 16% described themselves in the New Account Application Form (NAAF) as sophisticated investors. 96 When determining a sophisticated investor, consideration is usually given to an investor’s education, occupation, business experience, income, previous investment exposure, investment knowledge, understanding of securities and the dynamics of the security industry, and experience in securities trading. The main test is whether the investor possesses the intelligence and experience to independently evaluate a broker’s suggestions (Goldin, 2010: 298).

From the information provided so far, the investors who are more often taken advantage of therefore, are the elderly with “limited financial literacy” (e.g., see Heminway, 2009: 307).

96 Similarly, 17 percent of Eron investors classified themselves as being “sophisticated” investors (see Boyd, 2005: 16).
Investors’ Investment Knowledge

Purpose of Investment

Table 7-3 compares the purpose of investment from the IDA’s study to that of Eron. Given that 30% of the investors in the IDA study were already retired, and that 4% were unemployed at the time of investment, it is not surprising that 31% invested because they wanted money for their basic needs, compared to the 12% of Eron’s investors who invested for the same purpose. What is noticeable, however, is that 58% of Eron’s investors invested to fund their future retirement in comparison to 15% of IDA’s investors. The fact that most of the Eron investors were working at the time of investment, explains their desire to set up financial plans to fund their retirement needs (Boyd, 2005: 12). Note also, that 20% of the investors in the IDA study wanted a higher rate of return on their investments compared to only 1% of the Eron investors. This finding points to the possibility that vulnerable investors were lured by promises of higher returns, only to be swindled of their investments by their financial advisors.

The “Other” category of 6% in the IDA’s study consisted of investors who opened accounts for various purposes. Some opened accounts to facilitate private placement of securities and to reduce their income taxes; others opened accounts to provide security
and cover the operating expenses of companies they owned; while some invested to transfer-in funds from other accounts, and to deposit securities received from inheritances.

Table 7-3  Purpose of Investment in the IDA and Eron Studies

<table>
<thead>
<tr>
<th>Purpose of Investment</th>
<th>IDA Study (N=228)</th>
<th>Eron Study</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fund future retirement</td>
<td>15</td>
<td>58</td>
</tr>
<tr>
<td>Enhance current lifestyle</td>
<td>-</td>
<td>19</td>
</tr>
<tr>
<td>Income for basic needs</td>
<td>31</td>
<td>12</td>
</tr>
<tr>
<td>For children/grandchildren</td>
<td>4</td>
<td>3</td>
</tr>
<tr>
<td>Extra income</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Diversify investment portfolio</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>Higher rate of return than other investment</td>
<td>20</td>
<td>1</td>
</tr>
<tr>
<td>Trust Funds</td>
<td>10</td>
<td>-</td>
</tr>
<tr>
<td>Purchase Property</td>
<td>9</td>
<td>-</td>
</tr>
<tr>
<td>Other</td>
<td>6</td>
<td>1</td>
</tr>
<tr>
<td>DK/NA</td>
<td>*</td>
<td>1</td>
</tr>
<tr>
<td>Total Percent</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

*Not available

Sources of Investment

The IDA investors dipped into various sources to fund their investments. As Table 7-4 shows, an alarming 57% of the investors in the IDA study borrowed money to invest, in comparison to only 6% of Eron’s investors who invested with borrowed money. Whereas 68% of Eron’s investors took out money from their savings and retirement savings to invest, only 11% of the IDA investors were able to withdraw funds from their saving accounts to fund their investments. These differences can be attributed to the perception and nature of the investments. The Eron investors were led to believe that there was security in real estate, [and that] Eron’s business appeared legitimate, based on, among other things, the fact that Eron had been in
operation for three years with apparently stellar earnings for its clients. Many Eron investors did not see themselves as investors: 34 per cent thought that they were not investing, but lending money – providing a loan with a guaranteed rate of return (Boyd, 2005: 17).

Being given the assurance that there was less risk in investing with Eron, it does not come as a surprise that 68 percent of the investors would use their savings and retirement savings to fund their investments. After all, it makes good financial sense for investors to use their own money to fund their investments, rather than with loans that they would have to repay with interest. The fact that the majority of the IDA investors borrowed money to invest can be partly attributed to their financial advisors who encouraged their clients to invest with borrowed funds, with promises of higher returns. Given that only 10% of the investors in the IDA study, and 4% in the Eron study, received money from a recent windfall or inheritance to fund their investments, it is clear that investors were willing to “jeopardize their financial security,” by either dipping into their savings or borrowing funds to invest “because of their apparent concerns for their financial futures” (Boyd, 2005: 13).

With the exception of investors who mortgaged their primary residence to obtain funds to invest, there was no significant difference in the other categories. The funds from the 7% of investors belonging to the “Other” category in the IDA study could not be easily categorized for coding purposes. The “Other” category in the IDA study included funds that came from excess cash or “play money,” liquidated belongings, total net worth, and total assets. Some investors deposited securities and transferred their “holdings” from other firms into their new accounts.

Table 7-4  Sources of Investment in the IDA and Eron Studies

<table>
<thead>
<tr>
<th>Sources of Investment</th>
<th>IDA Study (N=435)</th>
<th>Eron Study</th>
</tr>
</thead>
<tbody>
<tr>
<td>Savings</td>
<td></td>
<td>5</td>
</tr>
</tbody>
</table>

129
<table>
<thead>
<tr>
<th>Type of Accounts</th>
<th>6</th>
<th>32</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retirement savings</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash in other investment</td>
<td>9</td>
<td>8</td>
</tr>
<tr>
<td>Borrowed funds</td>
<td>57</td>
<td>6</td>
</tr>
<tr>
<td>Mortgage primary residence</td>
<td>1</td>
<td>5</td>
</tr>
<tr>
<td>Recent windfall or Inheritance</td>
<td>10</td>
<td>4</td>
</tr>
<tr>
<td>Sold Property</td>
<td>5</td>
<td>4</td>
</tr>
<tr>
<td>Mortgage other property</td>
<td>0</td>
<td>1</td>
</tr>
<tr>
<td>Other</td>
<td>7</td>
<td>2</td>
</tr>
<tr>
<td>DK/NK</td>
<td>*</td>
<td>1</td>
</tr>
<tr>
<td>Total Percent</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

*Not available

**Type of Accounts**

Margin and cash accounts were the most frequent type of accounts opened by investors. As shown in Figure 7-4, margin accounts made up 41% of all accounts opened by investors. This is partly due to

the raging bull market of the past several years, [which led] many brokers [to]… seized the opportunity of loading up their clients with as many investments as possible. When clients don’t have the money available to fund such investments, brokers aggressively promote the leveraging principle (i.e., borrow money and use that money to invest with) (Goldin, 2010: 46).

Moreover, margin accounts give the clients “extra buying power, which generates more commissions for their financial advisor” (p. 201). The “brokerage house [also] charges [the clients] interest on [the] margin loan, which generates more income for [the] brokerage house (p. 201). Trading in margin accounts is a very risky proposition.

Using a margin account means borrowing money from the Brokerage House to finance purchases, and use the securities in their account as collateral for the loan. Carrying a debit balance means using leverage and investing with *borrowed* money. A margin investor profits only if the investment increases in value more than the cost of borrowing. If the market moves in the opposite direction, the investor will be responsible for the full amount of the loss (IDA. V. Babb, 2000: para: 51 emphasis added).
Margin accounts were opened for investors even though many did not know what a margin account was and how it operated. In one instance, a client noted that she did not fully understand what a margin account involved, at the time the margin account was opened. Furthermore, over time she became concerned about [the] account statements as [she] did not understand the meaning of the negative signs on the account statements (*IDA v. Latta*, 2004: para. 6).

Similarly, in another case, the client “signed a Margin Agreement, but did not know what [a] margin was[,] as the Respondent had not explained the meaning of margin nor any of its associated risks to her” (*IDA v. Xiao*, 2004: para. 21). When one considers that both the investment advisor and Member firm benefits from the opening of margin accounts, it does not come as a surprise that they would encourage investors to open and operate margins accounts to fund their investments. The use of leverage also shows the level of risk that investors are willing to take in order to secure their financial futures.

Cash accounts comprised 30% of all of the accounts opened by investors to fund their investments. The implication of this finding is that while investors overwhelmingly borrowed money to invest, a significant proportion of them used cash to settle trades in their accounts. There is also the possibility that cash accounts were opened to be used as collateral for the funds borrowed from the Member firm, to settle trades in margin accounts.
Income and long-term growth made up the majority of the investors’ investment objectives. As shown in Figure 7-5, income represented 41% of investors’ investment objectives, while long-term capital growth represented 30%. The implications of these findings are that investors prefer a return on their investment for immediate use, rather than waiting for long-term capital gains (see Brigham, Ehrhardt, Gessaroli, Nason, 2011: 478). However, this should not detract from the fact that long-term capital gains still represent 30% of investors’ investment objectives. Two possible explanations for a long-term investment strategy are that with capital gains, taxes are deferred until the investor sells the stocks (p. 479). Second, investors who can afford it may want to time the capital gains and wait until they retire and are in a lower income tax bracket before they cash in their stocks (see p. 479). Hence, in the long-term, these investors will effectively pay lower taxes on their capital gains.
Notice also that high risk speculative trading only represented 11% of investors’ investment objectives. This is further evidence that the majority of investors were conservative in their investment approach. That said, as investors lean towards income as their investment objective, they must at the same time be willing to take some risk and reduce the emphasis on safety of their principal amount (see Investopedia, 2011: para. 5). This inverse relationship between income and safety of capital is one possible explanation as to why the latter represented only 6% of investors’ investment objectives in the present study (see para. 5).

Figure 7-5  Investors’ Investment Objectives

**Household Income and Net Worth**

Like the Eron and Typical Canadian Investors studies, the majority of the investors in the IDA study were not wealthy. As Table 7-5 shows, 66% of the investors in the IDA study made less than $50,000 per year, compared to 37% and 40% of investors who were in the same income bracket in the Eron and Typical Canadian Investors studies. One possible reason as to why there are more investors in the IDA study that
earned less than $50,000 per year, is because the study also took into account the average salaries of Canadians in the 1980’s and early 1990’s, which was much lower than the average salaries in the past decade. Note also, that in the IDA study, only 2% of investors made over $200,000 per year, a finding that is no different from the Eron and Typical Canadian studies.

Table 7-5 Annual Household Income of Investors in the Three Studies

<table>
<thead>
<tr>
<th>Annual Income</th>
<th>IDA Study (N=172)</th>
<th>Eron Study</th>
<th>Typical Canadian Investors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under $25,000</td>
<td>31</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>$25,000 to under $50,000</td>
<td>35</td>
<td>27</td>
<td>30</td>
</tr>
<tr>
<td>$50,000 to under $75,000</td>
<td>19</td>
<td>27</td>
<td>25</td>
</tr>
<tr>
<td>$75,000 to under $100,000</td>
<td>4</td>
<td>16</td>
<td>13</td>
</tr>
<tr>
<td>$100,000 to under $150,000</td>
<td>6</td>
<td>8</td>
<td>9</td>
</tr>
<tr>
<td>$150,000 to under $200,000</td>
<td>3</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>$200,000 and over</td>
<td>2</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>DK/NA</td>
<td>*</td>
<td>7</td>
<td>9</td>
</tr>
<tr>
<td>Total Percent</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

As shown in Table 7-6, close to 60% of investors in the IDA study had a household net worth of under $250,000. These findings in the IDA study are no different from the findings in the Eron study, which reported that approximately 60% of investors had a household net worth of under $250,000 (Boyd, 2005:14). A closer look at Table 7-6, also shows that 45% of the investors in the IDA study had a household net worth that was over $250,000, compared to 32% and 10% of Eron and the Typical Canadian Investors in the same category. In interpreting these findings, it is important to keep in mind the proportion of investors in each age group in the three studies. As mentioned

To peruse the historical trend of the average salary increase of Canadians from 1990 to 2005, see Statistics Canada average income after tax by economic family types (Statistics Canada, 2011b).
earlier, approximately 60% of the investors in the IDA study were over 55 years of age, compared to 39% and 30% of the investors who were in the same age group in the Eron and the Typical Canadian Investors’ studies. As such, the investors in the IDA study had more working years to accumulate wealth, than investors in the Eron and Typical Canadian Investors’ studies. It seems natural then that investors in the IDA study would have had more time to pay off their debts and have a higher household net worth than the investors in the Eron and Typical Canadian Investors’ studies (see, Sauvé, 2002: 21-22; Boyd, 2005: 14).

Table 7-6  Household Net Worth (Excluding principal residence) of Investors of the Three Studies

<table>
<thead>
<tr>
<th>Household Net Worth</th>
<th>IDA Study (N=191)</th>
<th>Eron Study</th>
<th>Typical Canadian Investors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under $25,000</td>
<td>5</td>
<td>6</td>
<td>28</td>
</tr>
<tr>
<td>$25,000 to under $50,000</td>
<td>3</td>
<td>10</td>
<td>18</td>
</tr>
<tr>
<td>$50,000 to under $100,000</td>
<td>14</td>
<td>19</td>
<td>15</td>
</tr>
<tr>
<td>$100,000 to under $150,000</td>
<td>15</td>
<td>8</td>
<td>9</td>
</tr>
<tr>
<td>$150,000 to under $250,000</td>
<td>19</td>
<td>17</td>
<td>8</td>
</tr>
<tr>
<td>$250,000 and over</td>
<td>45</td>
<td>32</td>
<td>10</td>
</tr>
<tr>
<td>DK/NA</td>
<td>*</td>
<td>8</td>
<td>12</td>
</tr>
<tr>
<td>Total Percent</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

*Not available

Financial Losses

Figure 7-6 presents the losses incurred by identified investors in the IDA study. For those investors where financial losses were identified, 41% lost under $25,000. This finding point to the possibility that for the majority of investors, once they realized that they were losing money, decided to cut their losses and get out at the earliest opportunity (e.g., see Goldin, 2010: 129). Another 19% of investors lost anywhere between $25,000 to under $50,000, 13% lost between $50,000 to under $75,000, and
5% lost between $75,000 to under $100,000. Also notable, is that 22% of investors lost over $100,000 from their investments. It is highly unlikely that investors will tolerate such huge losses in their accounts, without inquiring about the losses.

Financial advisors utilized a number of techniques from their toolkits to hide these losses. In some cases, the financial advisor took advantage of the investors’ limited financial knowledge and swindled their investments. For example in Silcoff, the Panel noted that

"[f]rom the time the E Account was opened on May 5, 2000 through February 28, 2001 Mr. S effected 75 discretionary transactions in the E Account. When NE and EE became aware of the discretionary transactions in [their] Account, NE called Mr. S to express concern over the trading in [their] account. Mr. S told NE not to be concerned because her bottom line account balance was not affected. When NE expressed concerns to Mr. S regarding the declining balance in [their] Account, he assured her that the …Account was not losing money and that she was simply misreading the account statements. In fact, the discretionary transactions in the …Account resulted in a loss of $18,531.94 (IDA v. Silcoff, 2004: para. 21)."

In other cases, investors were told by their financial advisors to keep their accounts active, and that their investment losses would recover over time. For example, in Youden, the Panel noted that the client

"Mr. M…[gave] evidence that he first complained to Mr. B [his financial advisor] when his portfolio started to drop off in the spring of 2000. He stated that he made several phone calls to Mr. B enquiring about this and what Mr. B intended to do to either recover what he lost or prevent further losses. In response [the client] testified that Mr. B advised him that the market losses were temporary as it was just a dip in the market and things would recover and there was no need for concern…[Mr. M's] main investment account went from a high of $351,000 in March of 2000 to a low of $45,000 when all the accounts were transferred out of RBCDS in May of 2003 (IDA v. Youden, 2003: para. 30 and 94)."
There were also cases where the financial advisors kept the account active in an attempt to recover the losses incurred. In *Migirdic* for example, the client P.A. complained to [Mr. M, his financial advisor] about his losses. In reply, [Mr. M] gave his client a letter on May 14, 2000, in which he stated that he was taking responsibility for the decline of the portfolio and promised to restore the portfolio’s value to its January 20, 2000 level, namely $1,059,954, by the close of the third Friday in January 2001. [Mr. M] also wrote that, if he was unable to restore the value of the portfolio to its January 2000 level, he would reimburse the account holder the difference between the value as at January 2000 and the value as at January 2001...[Mr. M]...was hoping that the markets would recover and that he would not have to reimburse P.A (IDA v. Mirgirdic, 2004: para. 13 and 16).

![Figure 7-6 Investors’ financial losses](image)

**Figure 7-6**  Investors’ financial losses

**Relationship to the Offender**

As indicated in the literature, “a relationship of trust” is a major factor when it comes to handing over your money for investment (CSA, 2007a:1; also see Boyd, 2005: 34-35). The first casualties of investment scams are investors who trusted their financial advisors the most (see CSA, 2007a:2). As can be seen in Figure 7-7, 40% of the
investors were a family member, 37% were an acquaintance, and 23% were a friend of the offender. Like the mortgage brokers in the Eron fraud, investment advisors in the IDA study “operated on the basis of the exploitation of existing trust” (Boyd, 2005: 34). The available data, although limited, indicates that individual registrants were able to earn the trust of the people they were closest to and then betray that trust by swindling them of their retirement funds. It seems prudent to think that investors who are familiar with their financial advisors might have been secure with their investments. However, it may be that being familiar with and blindly trusting an investment advisor may “actually work...against” investors' interests (see Boyd, 2005: 34). Far from giving investors peace of mind, trust without conducting due diligence on the background of the investment advisors, seems to be the cardinal sin investors are committing when selecting a financial expert to manage their money.

98 There were three cases comprising 6, 9 and 16 victims respectively, where the relationship to the offender could not be coded because I was unable to categorize the individual as either a family member or a friend of the offender.
Characteristics of the Offender

Individual Offender

Table 7-7  Crosstabulation of Offenders’ Gender and Disciplinary History

<table>
<thead>
<tr>
<th>Offenders’ Gender</th>
<th>Male</th>
<th>Female</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>464</td>
<td>47</td>
<td>511</td>
</tr>
<tr>
<td>First time offender</td>
<td>92%</td>
<td>96%</td>
<td>92%</td>
</tr>
<tr>
<td>Repeat offender</td>
<td>43</td>
<td>2</td>
<td>45</td>
</tr>
<tr>
<td></td>
<td>8%</td>
<td>4%</td>
<td>8%</td>
</tr>
<tr>
<td>Total offenders</td>
<td>507</td>
<td>49</td>
<td>556</td>
</tr>
<tr>
<td>Total Percent</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
</tr>
</tbody>
</table>

Table 7-7 presents details on the individual offenders and their disciplinary history. In total, there were 556 offenders, out of which 507 (91%) were male and 49 (9%) were female. In terms of repeat offenders, the Hearing Panel specifically looked at whether the individual had “been the subject of any prior disciplinary action by any provincial securities administrator or Canadian self-regulatory organization” (IDA. v. 
Guidoccio, 2001: para. 7). As can be seen in Table 7-7, 464 (92%) of the male registrants were first time offenders and 43 (8%) were repeat offenders. Of the female offenders, 47 (96%) were first time offenders, and only 2 (4%) were repeat offenders.

Offenders Currently Working in the Industry

<table>
<thead>
<tr>
<th>Offenders’ Employment</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>In the Industry</td>
<td>99</td>
<td>26%</td>
</tr>
<tr>
<td>Out of Industry</td>
<td>284</td>
<td>74%</td>
</tr>
<tr>
<td>Total</td>
<td>383</td>
<td>100%</td>
</tr>
</tbody>
</table>

Using IIROC’s AdvisorReport, I conducted a background check to see how many individual offenders are currently employed by an IIROC’s regulated firm. IIROC only maintains data on its individual registrants’ employment history from 1997 to the present. As can be seen in Table 7-8, out of the 383 individual offenders charged and found guilty from 1997 to June of 2008, only 99 (26%) were currently working in the industry, while 284 (74%) were not.99 It is quite possible that the offenders who are not currently working in the industry, did not bother to pay their fines and moved on to work in other sectors of the investment industry. This assertion is corroborated by FAIR Canada. According to FAIR Canada,

[i]t … appears far too common for individuals who have been disciplined by one of the self-regulatory organizations (“SROs”), namely the Investment Industry Regulatory Organization of Canada (“IIROC”) or the Mutual Fund Dealers Association of Canada (“MFDA”), to fail to pay the fine and simply cease to be members or approved persons of the SROs (FAIR Canada, 2011a: para.3).

99 To avoid counting the same offender twice, repeat offenders were eliminated from the final total.
FAIR Canada went on to argue that these individual advisors simply “move platforms to sell in the exempt market (where individuals and firms are not required to register in certain western provinces) or, for example, sell insurance despite having been found to have been dishonest or otherwise not of sufficient integrity to deal with investors” (FAIR Canada, 2011a: para. 1). For instance, in 2007, the Pacific District of the IDA disciplined Mr. DM for

facilitated and solicited participation in the sale of shares of ... a public company, such transactions which were conducted off the books and without the knowledge of his employer; advised[ing] and assist[ing] clients with respect to the purchase of shares when his registration was restricted to the sale of mutual funds; enter[ing] into personal financial dealings with clients; attempt[ing] to conceal information during the course of an investigation by the Association, and misled Association Staff with respect to facts reasonably required for purposes of its investigation and also attempted to frustrate the Association’s investigation; and [for] maintain[ing] an account at another Member firm without the knowledge or consent of his employer (IDA v. Michaels: para. 1).

The Hearing Panel, after taking into consideration the aggravating and mitigating factors of the case, imposed

[a] fine in the amount of $45,000; costs in the amount of $15,000; [t]he amounts ... shall be paid in full prior to any re-approval of the Respondent as an Approved Person; [p]rior to any application by the Respondent for registration as an Approved Person, he shall re-write and successfully complete the CPH examination; [n]o application by the Respondent for registration as an Approved Person shall be made before 2 months from the date of this decision; [i]n the event that the Respondent is again registered as an Approved Person, it will be a condition of such registration that he be subject to a period of close supervision for the first 6 months of his employment as an Approved Person (para. 31).

Yet despite being disciplined, Mr. DM “went on to prey on vulnerable seniors in the exempt market in [British Columbia] where he [was] not required to be registered” (FAIR Canada, 2011a: para. 2).
Of those who stayed in the industry, there were instances where former individual registrants were banned from holding senior positions with an IDA’s regulated Member firm, but returned to the industry a few years later and were hired as investment advisors. For example, take the case of Mr. HC. Mr. HC was at all relevant times the President and a director of Rampart Securities Inc. from approximately September 22, 1997 to April 11, 2001. In 2002, an IDA’s Hearing Panel ruled that Mr. HC failed to

(a) ensure [that] the Member was in compliance with Association Requirements pursuant to Association Regulation 1300.1, 1300.2 and Policy No. 2; and (b) carry out his responsibilities to implement and enforce policies that would ensure that Rampart’s [Ultimate Designated Persons], compliance staff and salespeople would pursue an effective sales compliance program to ensure proper compliance with regulatory requirements, opening of accounts and supervision of account activity (IDA v. Cole, 2002: para. 18).

For these violations, the Panel imposed a fine of $125,000 and banned Mr. HC from holding any senior position with an IDA regulated Member firm for a period of ten years (see IDA v. Cole, 2002: para. 20). In spite of his previous run-in with the IDA, Mr. HC was hired by the investment dealer arm of Canada’s biggest bank—RBC Dominion Securities, as an investment advisor in 2005 and continues to hold a license to sell securities (see Shecter, 2012a: para. 16). According to sources, RBC was aware of his previous brush with regulators, but still hired him “because his earlier sanctions were not related to his conduct with clients and his job did not fall into the categories from which he was banned: supervisory and compliance” (Shecter, 2012b: para.8).

Beginning in 2009, Mr. HC again ran into problems with the IDA.

Between February 2009 and December 2010, [Mr. HC], while a Registered Representative, failed to observe high standards of ethics and conduct in the transaction of his business, and engaged in a business conduct or practice which is unbecoming or detrimental to the public interest (IIROC v. Cole, 2012: 1).
In 2012, he admitted to “(a) misappropriat[ing] client funds in the amount of approximately $5 million; (b) creat[ing] false documents; and (c) misrepresent[ing] payments to investors out of a pool of investor funds as being returns on investment” (p. 2). In the Settlement agreement with IIROC, Mr. HC agreed to “(a) pay a fine of $5,020,022; and (b)... a permanent... ban from registration with IIROC” (p. 2). Mr. HC also agreed “to pay costs to IIROC in the sum of $10,000 to reflect the costs that [IIROC’S] Staff incurred in connection with [the] matter” (p. 2). In a criminal proceeding, Mr. HC “was sentenced to two-and-half years in prison” on January 18, 2012, “after pleading guilty to fraud” (Shecter, 2012a: para. 1).

**Offenders’ Occupation**

**Table 7-9   Occupation of Offenders**

<table>
<thead>
<tr>
<th>Occupation</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Registered Representative</td>
<td>438</td>
<td>79</td>
</tr>
<tr>
<td>Branch Manager</td>
<td>48</td>
<td>9</td>
</tr>
<tr>
<td>Officer</td>
<td>70</td>
<td>13</td>
</tr>
<tr>
<td>Total</td>
<td>556</td>
<td>100</td>
</tr>
</tbody>
</table>

Most of the individuals accused of violating the Association’s rules and regulations were Registered Representatives. According to IIROC’s Approval Category, “[t]he type of customers that a Registered Representative or Investment Representative has been approved by IIROC to deal with,…can be retail customers (that is the general public) and/or institutional customers” (IIROC, 2011a: 1). As can be seen in Table 7-9, 438 (79%) of the offenders were Registered Representatives. Since the victims were predominantly individual retail clients, it is not surprising to see such a high number of Registered Representatives being involved in securities infractions.
However, this should not detract from the fact that Branch Managers and Officers committed 22% of the total offences. Generally, Branch Managers are responsible, inter alia, for the opening of new accounts and the supervision of account activity in the branch and must ‘ensure that the handling of client business is within the bounds of ethical conduct, consistent with just and equitable principles of trade and not detrimental to the interests of the security industry’ (IDA v. Youden, 2005: para. 11).

More specifically, Branch Managers have an obligation to

to review the previous day’s trades to attempt to detect lack of suitability, excessive trading activity, any conflict of interests between financial advisors and their clients trading activity, inappropriate high risk trading strategies, and quality down grading of client’s holdings amongst other things (Goldin, 2010: 84).

Branch Managers who fail to perform these duties are willing participants in the offences. In Dunn for example, Mr. AC who was a registered representative under the supervision of the Branch Manager Mr. D,

was employed at Nesbitt’s Mississauga branch office from May 1993 to August 28, 1997. However, Mr. AC was not approved by the Association to act as a registered representative until January 17, 1998. Between May 1993 and the time that Mr. AC was first approved by the Association (some 8 1/2 months later), Mr. AC opened at least two accounts, prepared the New Account Application Forms, solicited transactions, took client orders and prepared trade tickets for those accounts. Although Mr. D signed the New Account Application Forms for those accounts, Mr. D had little or no involvement in the actual management of the accounts and did not personally meet with the clients to discuss their investment objectives or risk tolerances. In so doing, Mr. D allowed Mr. A.C. to act in furtherance of trades while he was unregistered, contrary to Association By-law 29.1 (IDA v. Dunn, 2004: para. 7).

In Corrigan, Mr. SRJ had been registered as a Registered Representative, but since he failed one of the Association’s educational requirements, his status changed to an
Investment Representative (IDA v. Corrigan, 2005: para. 56). The Panel in Corrigan noted that

the Respondent, as Branch Manager responsible for S.R.J.’s conduct, permitted S.R.J.’s name to appear as [Registered Representative], or Account Representative on the monthly account statements and trade confirmations for the clients’ Accounts.... Further, the Panel argues that they were satisfied that the Respondent either knew, or ought to have known, that S.R.J. sent a letter to the new Account clients, which enclosed the New Client Application Form as well as other information, and that S.R.J. signed those letters as “Investment Advisor” which he was not permitted to do as an IR (para. 59-60).

In other cases, the Branch Managers were guilty for not adequately supervising investment advisors to ensure compliance with the Association’s regulatory requirements. In Bacsalmasi for example,

...the Respondent [a Branch Manager] failed to properly, or at all, supervise S’s trading in the H.B. and C.C. accounts, and inappropriately approved the updates to the H.B. and C.C. NCAFs without any inquiry of S and with the knowledge that the updates were done to bring the NCAF stated investment objectives and risk factors in line with the actual trade activity in the accounts (IDA v. Bacsalmasi, para. 36)

Similarly in Youden, the Panel concluded that

the evidence in its totality demonstrates that Mr. Y failed to reasonably supervise the client accounts of Mr. B as required. Mr. Y did not adequately address the high turn[over] rates in many of Mr. B’s accounts. Mr. Y either did not address these rates with Mr. B at all, or repeatedly accepted Mr. B’s explanations in spite of numerous red flags which cried out for investigation and action. Mr. Y did not adequately review many monthly statements regarding commissions generated as required by Policy 2 and the Manual. Mr. Y did not call Mr. B’s clients to confirm the suitability of the trading activity in the face of repeatedly high turn[over] ratios, high commissions, significant losses, and trading activity that was inconsistent with the client objectives on file as evidenced by the KYCs (IDA v. Youden, 2005: para. 100)
Since “branch managers have a conflict-of-interest in terms of reviewing their own trades,” it is imperative that non-trading Officers and Directors fulfill their duties by ensuring “all orders initiated for clients’ accounts” are reviewed at the earliest opportunity (Goldin, 2010: 84 & 96). Rather than trying to secure compliance with the IDA’s By-laws, it can be argued that Officers and Directors who fail to perform their duties may be more interested in the brokerage house’s bottom line rather than the financial well-being of their clients. It may well be that the brokerage house has a corporate culture that stresses profit maximization, which in turn motivates Officers to negate their compliance duties.

Offenders’ Experience\textsuperscript{100}

![Figure 7-8](image)

**Figure 7-8**  Years of Offenders’ Work Experience in the Securities Industry

Figure 7-8 breaks down the number of years offenders worked in the securities industry. The proportion of offenders shown for each time interval cannot be compared

\textsuperscript{100} The offender’s work experience was coded to take into consideration the number of years that the individual worked in the entire securities industry, and not just when he or she became registered with the IDA.
with the actual number of individual registrants and their corresponding years of industry experience, because this information is not collected. In spite of this shortcoming, data on the investment advisors offending shows that 42% of them violated the Association’s rules and regulations within their first 5 years in the securities industry. If less experienced registrants are overrepresented in discipline cases (and there is no data to confirm or refute this proposition), one viable explanation is that new registrants may not be properly supervised within the first few years in the industry. There is also the possibility that as novice brokers, they may try to circumvent supervision to maximize their commissions in the early stages of their career. Whatever the reason (and even if this group of offenders is not overrepresented compared to all registrants), IIROC should be concerned that more than 40% of the offenders engage in unbecoming conduct at the beginning of their careers.

As can be seen from Figure 7-8, 25% of investment advisors broke the Association’s rules and regulations between 6 to 10 years, 15% between 11 to 15 years, and 11% between 16 to 20 years. Investment advisors with over 20 years of industry experience comprised only 8% of the total offenders. Again, there is no data to determine if these groups are overrepresented or underrepresented in the overall pool of advisors. Some authors suggest that if investment professionals spend more years in the securities industry “covering both good and bad market cycles,” they are likely to “develop better insight and experience that [investors] can benefit from” (Goldin, 2010: 29). Consequently, they become more technically adept at evaluating companies’ financial statements and are in a better position to construct portfolios that will maximize their clients’ return with little or minimal risk. It is unfortunate that data on the experience of advisors is not collected and tracked.
Member Firms

Types of Member Firms

Table 7-10 Types of Member Firms Involved in Enforcement Hearing

<table>
<thead>
<tr>
<th>Type of Firms</th>
<th>Number of Firms</th>
<th>Percent of Firms</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retail</td>
<td>39</td>
<td>67</td>
</tr>
<tr>
<td>Integrated</td>
<td>18</td>
<td>31</td>
</tr>
<tr>
<td>Institutional</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>Total</td>
<td>58</td>
<td>100</td>
</tr>
</tbody>
</table>

Of the 113 Member firms that were involved in disciplinary proceedings from 1984 to June of 2008, data on their business type was available for 58 (51%) of the firms. IIROC’s list of Member firms’ peer group classifications has nine categories (see IIROC, 2010a). However, with the exception of one firm that was involved in proprietary trading all of the other firms that were involved in disciplinary proceedings fall into one of the following three categories: retail, integrated, and institutional. To this end, I will refine my analysis to these three categories. As Table 7-10 shows, 39 (67%) of the Member firms that were involved in disciplinary proceedings were retail firms servicing predominantly individual investors (see IIROC, 2010a: 1). The integrated firms, which comprised 18 (31%) of Member firms sanctioned, were the larger firms that are mostly bank owned and are involved in both retail and institutional trading (see See IIROC, 2010a: 1). Only 1 (2%) of the firms involved in disciplinary proceedings were institutional firms.101 Institutional firms are firms that “provide services exclusively to pension funds,

101 Even though there was only one delinquent proprietary and institutional firm each, I included the institutional firm in the analysis for two reasons. First, institutional firms comprise 51 (25%) of IIROC’s total Dealer Member firms, while firms involved in proprietary trading only comprise 12 (6%) of total Dealer Member firms. Second, institutional firms use the funds of their clients to invest, whereas firms involved in proprietary trading, trade with their own money. As such, since institutional firms make up a higher proportion of the firms on IIROC’s Dealer Member Peer
insurance companies, mutual fund organizations, banks and trust companies”
(Department of Finance, 2005:2-3).

Number of Member Firms

Table 7-11  Number and Percentage of IIROC’s Regulated Integrated, Retail, and Institutional Member Firms

<table>
<thead>
<tr>
<th>Types of Firms</th>
<th>Number of Firms</th>
<th>Percent of Firms</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retail</td>
<td>84</td>
<td>58</td>
</tr>
<tr>
<td>Integrated</td>
<td>11</td>
<td>8</td>
</tr>
<tr>
<td>Institutional</td>
<td>51</td>
<td>35</td>
</tr>
<tr>
<td>Total</td>
<td>146</td>
<td>100</td>
</tr>
</tbody>
</table>

To put these findings into context, I then obtained data on the number of Member firms that were registered with IIROC in these three categories as of March 31, 2011.\(^{102}\) As can be seen, when comparing Tables 7-10 and Table 7-11, retail and integrated firms appear to be over-represented in the IDA data, while institutional firms appear to be under-represented. Retail firms make up 58% of firms registered with IIROC, yet they represent 67% of all firms that were involved in disciplinary proceedings. On the same token, integrated firms represent 8% of all firms registered with IIROC, but make up 31% of the firms involved in disciplinary proceedings. On the other hand, institutional firms make up 35% of firms registered with IIROC, but only represent 2% of firms involved in disciplinary proceedings.

\(^{102}\) Since the time interval I am examining covers a period of 24 years, these figures only provide a rough estimate of the number of firms that were registered with the IDA at any given time. The types and number of the other IIROC’s regulated Member firms are as follows: Managed Accounts (19), Discount Brokers (11), Corporate Finance (10), Alternative Trading Systems (9), and Proprietary (12).
Disciplinary History

Table 7-12  Disciplinary History of Member Firms

<table>
<thead>
<tr>
<th>Valid</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>First time offender</td>
<td>107</td>
<td>95</td>
</tr>
<tr>
<td>Repeat offender</td>
<td>6</td>
<td>5</td>
</tr>
<tr>
<td>Total</td>
<td>113</td>
<td>100</td>
</tr>
</tbody>
</table>

As can be seen in Table 7-12, only 6 (5%) of the IDA's Member firms were repeat offenders. One must however, be cautious when interpreting these results. While Member firms are required to report all complaints from consumers to ComSet, there is still the possibility that some complaints will not be dealt with by the firm’s Designated Complaints Officer (DCO), and may be swept under the carpet. It may be a case where the DCO uses his or her professional judgement and decides that the complaints do not merit further investigation. In other cases, the Member firm may decide to settle the matter internally, without informing the IDA. As such, most regulatory problems against Member firms are probably unearthed by the IDA in its yearly compliance audits. In other cases, complaints may come directly from investors who had accounts at the Member firms. But, as mentioned earlier, even when problems are detected or complaints are filed by the public, there is always the possibility that the IDA’s enforcement staff will use their discretion to “funnel out” complaints by classifying them as minor issues that do not warrant disciplinary actions. Consequently, the number of Member firms that ended up as a part of the final statistic are probably the more egregious cases that the IDA had no other choice but to deal with.
**Enforcement**

**Type of Hearing**

**Table 7-13**  Type of Disciplinary Hearing for Individual Offenders and Member Firms

<table>
<thead>
<tr>
<th></th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Valid Settlement</td>
<td>446</td>
<td>67</td>
</tr>
<tr>
<td>Contested</td>
<td>206</td>
<td>31</td>
</tr>
<tr>
<td>Expedited</td>
<td>14</td>
<td>2</td>
</tr>
<tr>
<td>Total</td>
<td>666</td>
<td>99</td>
</tr>
<tr>
<td>Missing System</td>
<td>3</td>
<td>0.5</td>
</tr>
<tr>
<td>Total Cases</td>
<td>669</td>
<td>100</td>
</tr>
</tbody>
</table>

The majority of cases were disposed of through settlement agreements. As Table 7-13 shows, enforcement staff, individual registrants and Member firms, were able to negotiate a settlement agreement in 446 (67%) of the cases, while there were 206 (31%) contested cases and 14 (2%) expedited hearings. There are a few reasons as to why the number of settlement agreements was so high. In *Milewski*, the Panel noted that “[a] penalty under a settlement agreement is likely to be at the low end of the spectrum in view of the fact that a settlement is negotiated, permits the Association staff to avoid the costs of a contested hearing and guarantees them a favourable result” (*IDA v. Milewski*, 1999: para. 31). Similarly in *Mills*, the Panel noted that there is a distinction between penalties agreed to in a settlement and those imposed in a hearing...A penalty under a settlement agreement is likely to be at the low end of the spectrum. The difference is highlighted by the District Council’s responsibility to determine an appropriate penalty in a [contested] hearing ..., as opposed to accepting a penalty agreed to in a settlement... Settlement process is one of negotiation and compromise. Penalties imposed under settlement agreements thus cannot define the parameters of the penalties available...Within these parameters, the District Council’s responsibility is to determine the penalty that it believes is the correct one, taking into account relevant principles and factors, in the circumstances of the case before it (*IDA v. Mills*, 2001: 12).
The decision of whether to accept or reject a settlement agreement is set out in

Clark and Milewski. In Clark, the District Council noted that

[i]n considering a settlement [agreement]… the panel should not simply substitute its discretion for that of staff who negotiated the settlement. The panel must be cognizant of the importance of the settlement process and should not interfere lightly in a negotiated settlement… The settlement process is one of negotiation and compromise and the penalty imposed following a settlement will often be less onerous than one imposed following a hearing where similar findings are made (IDA v. Clark, 1999: para. 3).

Likewise in Milewski, the Panel argued that

[a]lthough a settlement agreement must be accepted by a District Council before it can become effective, the standards for acceptance are not identical to those applied by a District Council when making a penalty determination after a contested hearing. In a contested hearing, the District Council attempts to determine the correct penalty. A District Council considering a settlement agreement will tend not to alter a penalty that it considers to be within a reasonable range, taking into account the settlement process and the fact that the parties have agreed. It will not reject a settlement unless it views the penalty as clearly falling outside a reasonable range of appropriateness. Put another way, the District Council will reflect the public interest benefits of the settlement process in its consideration of specific settlements (IDA v. Milewski, 1999: para. 32).

These decisions highlight the importance of the settlement process and confirm that a hearing panel should be reticent to interfere with a negotiated settlement by attempting to substitute its discretion for the parties negotiating the settlement agreement. The decisions clearly set out that the obligation of a hearing panel is to reject a settlement agreement only if the hearing panel finds the terms of the settlement agreement to clearly fall outside a reasonable range of appropriateness (IDA v. Wong, 2005: para. 47).

The above cases illustrate that both the IDA and its individual registrants and Member firms have incentives to negotiate settlement agreements. On the one hand, settlement agreements save the IDA the unnecessary costs of a contested hearing and
guarantee them favourable results. On the other hand, individual registrants and Member firms are given lighter penalties for negotiating settlement agreements with the District Council. As for contested hearings, one can only speculate that the registrants either refused to accept responsibility for the act(s) or were not in agreement with the terms of the settlement offer.

**Disciplinary Proceedings and Location of District Council**

![Bar chart showing the number of disciplinary proceedings by District Councils.]

**Figure 7-9 Number of Disciplinary Proceedings by District Councils**

The number of disciplinary proceedings conducted by the IDA’s District Councils against individual registrants and Member firms is shown in Figure 7-9. Of the 669 cases, 283 (42%) were heard in Ontario. The Pacific (British Columbia and Yukon Territory) District Council heard 148 (22%) cases, while the District Council in Alberta and the Northwest Territories heard 89 (13%). Quebec was the only other District

\[^{103}\] There were two cases, both in 1986, with no reference to the location in which the disciplinary proceedings were held.
Council with double digit figures, hearing 71 (11%) cases. Manitoba and Nunavut, and Nova Scotia’s District Councils heard approximately 28 (4%) and 25 (4%) of the cases respectively. Another 12 (2%) were heard by the District Council in Saskatchewan and 8 (1%) by the New Brunswick’s District Council. The Prince Edward Island District Council heard 2 (.30%) cases, while the District Council in Newfoundland heard 1 (.15%) case.

It is expected that the District Councils in provinces with larger populations, will conduct more disciplinary proceedings. To examine whether this pattern exists, I compared the number of disciplinary proceedings heard by the District Councils with the populations in the three larger Canadian provinces (Ontario, Quebec, and British Columbia and Yukon Territory). The latest estimate by Statistics Canada noted that Ontario comprises approximately 39% of Canada’s population, while British Columbia and Yukon Territory combined comprise 13% (see Statistics Canada, 2011a). Yet, the Ontario District Council heard 42% of all cases, while the District Council in British Columbia and Yukon Territory heard 22%. On the other hand, Quebec makes up approximately 23% of Canada’s population; but, only heard 11% of all of the cases. It becomes clear then that Ontario and British Columbia (and Yukon Territory) are disproportionally overrepresented in the data, while Quebec is underrepresented by more than one-half.

\footnote{I added the population of the Yukon Territory to the population of British Columbia, because they both operate under the rubric of the Pacific District Council, for disciplinary hearing purposes. Given the different time frameworks, these figures provide only a rough indication of the distribution of cases.}
### Classification of Offences

#### Table 7-14  Table Showing the IDA’s Offence Categories

| Quasi-Criminal Offences | Conflict of Interest Offences | Improper Sales Practice Offences | Internal Control Offences | Cooperation, Membership, and Misrepresentation

<table>
<thead>
<tr>
<th>Fraud</th>
<th>Unauthorized or Improper Use of Inside Information</th>
<th>Unsuitable Recommendations</th>
<th>Capital deficiencies</th>
<th>Failure to Cooperate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Forgery</td>
<td>Unauthorized or Improper Disclosure and Client Information</td>
<td>Failure to Know Your Client</td>
<td>Failure to Establish Internal Controls</td>
<td>Misrepresenting Credentials</td>
</tr>
<tr>
<td>False Endorsement</td>
<td>Undisclosed/Unauthorized Accounts</td>
<td>Failure to Update NAAF</td>
<td>Failure to Supervise</td>
<td>Allowing an Unregistered Person to Trade</td>
</tr>
<tr>
<td>Misappropriation of Funds</td>
<td>Undisclosed Personal Business</td>
<td>Order not within Bounds of Good Business Practice</td>
<td>Fail to obtain and Maintain Minimum Required Margin</td>
<td>Conducting Business While Suspended</td>
</tr>
<tr>
<td>Securities Act Breach</td>
<td>Undisclosed Personal Business with a Client</td>
<td>Churning</td>
<td>Record Keeping Violations</td>
<td>Misrepresentations</td>
</tr>
<tr>
<td></td>
<td>Attempt to Settle Client Claim for Compensation</td>
<td>Discretionary Trading</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Failure to ensure Client Orders are given Priority</td>
<td>Unauthorized Trading</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Summary Statistics of Number Offences per Case

#### Table 7-15  Number of Offences per Case

<table>
<thead>
<tr>
<th></th>
<th>Individual Offenders</th>
<th>Member Firms</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Cases</td>
<td>556</td>
<td>113</td>
</tr>
<tr>
<td>Mean</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>Median</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Mode</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Maximum</td>
<td>24</td>
<td>10</td>
</tr>
<tr>
<td>Total</td>
<td>1694 (89%)</td>
<td>220 (11%)</td>
</tr>
</tbody>
</table>

Table 7-15 presents summary statistics of the number of offences that were found to have been committed by the hearing panels per case. A total of 1,694 (89%) offences were committed by individual offenders and 220 (11%) were committed by Member firms. Most of the disciplinary proceedings dealt with one offence per case for both individual offenders and member firms. The average number of offences per case was 3 for disciplinary proceedings involving individual offenders and 2 for Member firms. That said, about 2% of the cases involving individual offenders, dealt with more than 15 offences per case. These outlying values may work to push the average offences per case to the higher end. As such, the median which is resistant to the outlying values,

---

105 Table 7-15 does not include offences that were dismissed by the hearing panels.
may be a better indicator of the number of offences per case (e.g., see De Veaux, Velleman, Bock, 2008: 55-57). For both individual offenders and Member firms, the median number of offences dealt with per case was 2.

**Offence Profile for Individual Offenders and Member Firms**

Table 7-16 presents details of the type and number of offences committed by both individual offenders and Member firms. The most frequent type of offence committed by individual offenders was Improper Sales Practices, which made up approximately 47% of all of the offences. Similar to the number of complaints dealt with by the Case Assessment Group in the Annual Reports, discretionary trading (232, 14%) followed by unsuitable recommendations (222, 13%), were the most common offences in this category. Misrepresentation of facts to clients or Member firms was the next most common offence, accounting for 130 (8%) of all of the offences. Misappropriation of funds (or theft) from clients’ accounts rounded off the top four offences, comprising 90 (5%) of all offences committed by individual offenders. With the exception of misrepresentation, one commonality of the other three offences is that they are the ones that result in losses to clients’ accounts and commissions earned for the investment advisors.

Internal Control Offences made up about 60% of all of the offences committed by Member firms. Failure to supervise comprised 58 (26%) of the offences, followed by capital deficiencies, which made up 37 (17%) of all of the offences. To round off the top four offences committed by Member firms, the next most common offences were failure

---

107 Table 7-16 only deals with the number of offences committed, and not allegations.
to establish and/or maintain adequate internal controls and record keeping violations, both of which individually comprised 16 (7%) of all of the offences committed.

The “Other” category consisted of offences that could not be classified in any one of the offence types. Some of the 138 (8%) “Other” offences committed by individual offenders relate to violations concerning carrying broker’s agreements with the Association; failing to report securities held for clients at other institutions; operating branches without having qualified Branch Managers in charge of such branches; opening branch offices without having them approved by the Association; failure to file with the Association a Uniform Termination notice with respect to the termination of Branch Managers; failure to file audited financial statements with the Association; and, failure to have the required qualified officers in accordance with the Association’s By-laws.

Table 7-16  Offence Committed by Individual Offenders and Member Firms

<table>
<thead>
<tr>
<th>Offences</th>
<th>Individuals</th>
<th>Member Firms</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Responses</td>
<td>Responses</td>
<td>N</td>
<td>Percent</td>
</tr>
<tr>
<td>Quasi-Criminal Offences</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fraud</td>
<td>36</td>
<td>2%</td>
<td>N</td>
<td>Percent</td>
</tr>
<tr>
<td>Forgery</td>
<td>53</td>
<td>3%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>False Endorsement</td>
<td>5</td>
<td>.3%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Misappropriation of Funds</td>
<td>90</td>
<td>5%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Securities Act breach&lt;sup&gt;108&lt;/sup&gt;</td>
<td>67</td>
<td>4%</td>
<td>1</td>
<td>.5%</td>
</tr>
<tr>
<td>Total</td>
<td>251</td>
<td>12%</td>
<td>1</td>
<td>.5%</td>
</tr>
<tr>
<td>Conflict of Interest Offences</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unauthorized or Improper use of information</td>
<td>6</td>
<td>.4%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unauthorized or Improper Disclosure and/or Use of Client Information</td>
<td>6</td>
<td>.4%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Undisclosed/Unauthorized Accounts</td>
<td>24</td>
<td>1%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<sup>108</sup> Only breaches of provincial securities acts were coded, and not breaches of any other related provincial or federal legislation.
<table>
<thead>
<tr>
<th>Offences</th>
<th>Individuals</th>
<th>Member Firms</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Responses</td>
<td>Responses</td>
</tr>
<tr>
<td>Undisclosed Personal Business</td>
<td>7</td>
<td>.4%</td>
</tr>
<tr>
<td>Undisclosed Personal Business with Client</td>
<td>84</td>
<td>5%</td>
</tr>
<tr>
<td>Attempt to Settle Client Claim for Compensation</td>
<td>47</td>
<td>3%</td>
</tr>
<tr>
<td>Failure to Ensure Client's Orders are given Priority</td>
<td>6</td>
<td>.4%</td>
</tr>
<tr>
<td>Total</td>
<td>180</td>
<td>11%</td>
</tr>
<tr>
<td>Improper Sales Practices</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unsuitable Recommendations</td>
<td>222</td>
<td>13%</td>
</tr>
<tr>
<td>Failure to Know Your Client</td>
<td>79</td>
<td>5%</td>
</tr>
<tr>
<td>Failure to Update NAAF</td>
<td>22</td>
<td>1%</td>
</tr>
<tr>
<td>Order not within Bounds of Good Business Practice</td>
<td>71</td>
<td>4%</td>
</tr>
<tr>
<td>Churning</td>
<td>8</td>
<td>.5%</td>
</tr>
<tr>
<td>Discretionary Trading</td>
<td>232</td>
<td>14%</td>
</tr>
<tr>
<td>Unauthorized Trading</td>
<td>55</td>
<td>3%</td>
</tr>
<tr>
<td>Unauthorized Distribution of Sales Literature</td>
<td>17</td>
<td>1%</td>
</tr>
<tr>
<td>Unauthorized Third Party Instructions</td>
<td>54</td>
<td>3%</td>
</tr>
<tr>
<td>Outside Business Activities</td>
<td>33</td>
<td>2%</td>
</tr>
<tr>
<td>Total</td>
<td>793</td>
<td>47%</td>
</tr>
<tr>
<td>Internal Control Offences</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital Deficiencies</td>
<td>4</td>
<td>.2%</td>
</tr>
<tr>
<td>Failure to Establish and/or Maintain Adequate Internal Controls</td>
<td>10</td>
<td>.6%</td>
</tr>
<tr>
<td>Failure to Supervise</td>
<td>51</td>
<td>3%</td>
</tr>
<tr>
<td>Fail to Obtain and Maintain Minimum Required Margin</td>
<td>18</td>
<td>1%</td>
</tr>
<tr>
<td>Record Keeping Violations</td>
<td>51</td>
<td>3%</td>
</tr>
<tr>
<td>Total</td>
<td>134</td>
<td>8%</td>
</tr>
<tr>
<td>Cooperation, Membership, and Misrepresentation</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Failure to Cooperate</td>
<td>39</td>
<td>2%</td>
</tr>
<tr>
<td>Misrepresentation Credentials to Association upon Registration/Transfer</td>
<td>7</td>
<td>.4%</td>
</tr>
<tr>
<td>Allowing an Unregistered Person to Trade</td>
<td>19</td>
<td>1%</td>
</tr>
<tr>
<td>Conducting Business While Suspended</td>
<td>3</td>
<td>.2%</td>
</tr>
<tr>
<td>Misrepresentation</td>
<td>130</td>
<td>8%</td>
</tr>
<tr>
<td>Total</td>
<td>198</td>
<td>12%</td>
</tr>
<tr>
<td>Other</td>
<td>138</td>
<td>8%</td>
</tr>
<tr>
<td>Overall Total</td>
<td>1694</td>
<td>100%</td>
</tr>
</tbody>
</table>

159
The Funnel Process: Funnel Away

Continuing on with the funnel metaphor, “the ‘funnel away’ aspect of a disciplinary system is concerned with whether self-regulatory systems deflect” cases away from the criminal justice system in order to protect its members (Brockman & McEwen, 1990: 27). Under this assertion, it is expected that the IDA may not refer cases involving fraud, misappropriation of funds, and forgery to the criminal justice system for investigation. Given that some of the cases with evidence of criminality may be difficult to prove in the criminal justice system, the IDA might be justified in dealing with them internally. That said, the purpose of the “funnel away” aspect of the IDA’s enforcement process is to identify the types of cases with “evidence of criminal activity” that could have justifiably been referred to the criminal justice system (see IIROC, 2008c: 1). This is not to say that these individuals would have been necessarily convicted of a criminal offence if charged, but it may have helped to identify some of the types of misconduct that have “element[s] of criminal” activities attached to them (IDA, 2006b: 12; also see Brockman, 1990: 28-29).

As can be seen from Table 7-16, 251 (12%) of all of the offences committed by individual offenders and 1 (.5%) of all of the offences committed by Member firms, were quasi-criminal offences. Of the quasi-criminal offences committed by individual offenders, with criminal elements attached to them, 36 (2%) were fraud related, 53 (3%) deal with forgery, and 90 (5%) were classified as theft or the misappropriation of funds. False endorsement of regulatory documents made up 5 (.3%), while securities act breaches made up 67 (4%) of all of the quasi-criminal offences committed by individual registrants.
Cases dealing with quasi-criminal offences were mostly disposed of via settlement hearings. As shown in Table 7-17, from 1984 to 2001, there were 59 individual offender’s cases that dealt with quasi-criminal offences. Of these, 38 (64%) were disposed of via negotiated settlement hearings, compared to 21 (36%) of the cases that went through a contested hearing. For the time period (2002-2007) in which the funnel metaphor was applied, there were 57 individual offender’s cases that dealt with quasi-criminal offences. Of these, 28 (49%) were disposed of via settlement agreements and 29 (51%) through contested hearings. The number of quasi-criminal cases “funnelled away” during this 5 year period was only 2 less than the number of quasi-criminal cases “funneled away” from 1984 to 2001.\(^{109}\) Note also that 29 (51%) of the quasi-criminal cases went to a contested hearing from 2002 to 2007, compared to 21 (36%) from 1984 to 2001.

### Table 7-17  Individual offenders Disciplined for Quasi-criminal offences

<table>
<thead>
<tr>
<th>1984-2001</th>
<th>Type of hearing</th>
<th>Settlement</th>
<th>Contested</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quasi-Criminal Offences</td>
<td>Fraud</td>
<td>0</td>
<td>21</td>
<td>21</td>
</tr>
<tr>
<td></td>
<td>Forbery</td>
<td>9</td>
<td>7</td>
<td>16</td>
</tr>
<tr>
<td></td>
<td>False Endorsement</td>
<td>0</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>Misappropriation of Funds</td>
<td>35</td>
<td>29</td>
<td>64</td>
</tr>
<tr>
<td></td>
<td>Securities Act Breach</td>
<td>44</td>
<td>2</td>
<td>46</td>
</tr>
<tr>
<td>Total number of cases</td>
<td></td>
<td>38</td>
<td>21</td>
<td>59</td>
</tr>
<tr>
<td>Total percent of cases</td>
<td></td>
<td>64%</td>
<td>36%</td>
<td>100%</td>
</tr>
</tbody>
</table>

\(^{109}\) It is possible that some of these cases were also dealt with as quasi-criminal offences by the provincial courts, but there was no indication in these cases that quasi-criminal prosecution was pursued.
<table>
<thead>
<tr>
<th>Type of Hearing</th>
<th>Settlement</th>
<th>Contested</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quasi- Criminal Offences</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fraud</td>
<td>3</td>
<td>12</td>
<td>15</td>
</tr>
<tr>
<td>Forgery</td>
<td>15</td>
<td>22</td>
<td>37</td>
</tr>
<tr>
<td>False Endorsement</td>
<td>3</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>Misappropriation of Funds</td>
<td>8</td>
<td>18</td>
<td>26</td>
</tr>
<tr>
<td>Securities Act Breach</td>
<td>13</td>
<td>8</td>
<td>21</td>
</tr>
<tr>
<td>Total number of cases</td>
<td>28</td>
<td>29</td>
<td>57</td>
</tr>
<tr>
<td>Total percent of cases</td>
<td>49%</td>
<td>51%</td>
<td>100%</td>
</tr>
</tbody>
</table>

**Penalties Imposed**

In this section, I will compare the penalties that were imposed on both individual registrants and Member firms before and after the 1993 change in maximum fines, and the addition of the public member to chair hearing panels in 2004. The analysis of penalties will therefore be categorized into three time intervals: 1984 to 1993 ("Period 1"); 1994 to 2003 ("Period 2"); and 2004 to 2008 ("Period 3").
Individual Offenders

**Penalties Imposed**

Table 7-18  Total Fines, Costs, and Disgorgement and other Non-Monetary Penalties Imposed on Individual Offenders\(^{110}\)

<table>
<thead>
<tr>
<th>Year</th>
<th>Fines</th>
<th>Cost</th>
<th>Disgorgement</th>
<th>Dismissal</th>
<th>Bars</th>
<th>Suspension</th>
<th>Supervision</th>
<th>Rewriting License</th>
<th>Reprimand</th>
<th>Terms &amp; Conditions</th>
<th>Total Decisions</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>&quot;Period 1&quot;</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Before the Increase in Fines (1984-1993)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1984</td>
<td>$3,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1985</td>
<td>$3,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1986</td>
<td>$4,000</td>
<td>$1,950</td>
<td></td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1987</td>
<td>$2,000</td>
<td>$1,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1988</td>
<td>$24,000</td>
<td>$4,500</td>
<td></td>
<td>2</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1989</td>
<td>$58,500</td>
<td>$18,700</td>
<td></td>
<td>3</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1990</td>
<td>$138,250</td>
<td>$18,840</td>
<td></td>
<td>2</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1991</td>
<td>$69,000</td>
<td>$18,416</td>
<td></td>
<td>2</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1992</td>
<td>$164,000</td>
<td>$82,480</td>
<td></td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1993</td>
<td>$137,500</td>
<td>$26,920</td>
<td></td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$604,250</td>
<td>$173,306</td>
<td></td>
<td>4</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total % Non-Monetary Penalties</strong></td>
<td>3%</td>
<td>9%</td>
<td>8%</td>
<td>53%</td>
<td>19%</td>
<td>6%</td>
<td>100%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>&quot;Period 2&quot;</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>After the Increase in Fines (1994-2003)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1994</td>
<td>$98,000</td>
<td>$10,515</td>
<td></td>
<td>2</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1995</td>
<td>$108,000</td>
<td>$22,250</td>
<td></td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1996</td>
<td>$232,500</td>
<td>$70,746</td>
<td></td>
<td>2</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1997</td>
<td>$185,000</td>
<td>$58,000</td>
<td></td>
<td>5</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1998</td>
<td>$192,500</td>
<td>$29,000</td>
<td>$1,272</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1999</td>
<td>$369,000</td>
<td>$99,200</td>
<td>$142,659</td>
<td>5</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2000</td>
<td>$1,111,000</td>
<td>$203,640</td>
<td>$162,702</td>
<td>3</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2001</td>
<td>$850,500</td>
<td>$116,817</td>
<td>$34,223</td>
<td>3</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\(^{110}\) There was one appeal to the IDA that was dismissed.
<table>
<thead>
<tr>
<th>Year</th>
<th>Fines</th>
<th>Cost</th>
<th>Disgorgement</th>
<th>Dismissal</th>
<th>Bans</th>
<th>Suspension</th>
<th>Supervision</th>
<th>Rewriting License</th>
<th>Reprimand</th>
<th>Terms &amp; Conditions</th>
<th>Total Decisions</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>$2,154,000</td>
<td>$304,524</td>
<td>$33,616</td>
<td>1</td>
<td>5</td>
<td>10</td>
<td>16</td>
<td>22</td>
<td>21</td>
<td>14</td>
<td>40</td>
</tr>
<tr>
<td>2003</td>
<td>$2,379,250</td>
<td>$471,161</td>
<td>$314,120</td>
<td>2</td>
<td>10</td>
<td>9</td>
<td>9</td>
<td>16</td>
<td>1</td>
<td>14</td>
<td>39</td>
</tr>
<tr>
<td>Total</td>
<td>$7,679,750</td>
<td>$1,385,853</td>
<td>$688,592</td>
<td>40</td>
<td>56</td>
<td>76</td>
<td>174</td>
<td>4</td>
<td>87</td>
<td>276</td>
<td></td>
</tr>
</tbody>
</table>

**Total % Non-Monetary Penalties**

- 9%
- 13%
- 17%
- 40%
- 1%
- 20%
- 100%

**"Period 3"**

Addition of Public Member to Chair Hearings (2004-June 2008)

<table>
<thead>
<tr>
<th>Year</th>
<th>Fines</th>
<th>Cost</th>
<th>Disgorgement</th>
<th>Dismissal</th>
<th>Bans</th>
<th>Suspension</th>
<th>Supervision</th>
<th>Rewriting License</th>
<th>Reprimand</th>
<th>Terms &amp; Conditions</th>
<th>Total Decisions</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>$3,972,000</td>
<td>$743,514</td>
<td>$570,907</td>
<td>1</td>
<td>18</td>
<td>22</td>
<td>19</td>
<td>33</td>
<td>1</td>
<td>30</td>
<td>61</td>
</tr>
<tr>
<td>2005</td>
<td>$2,012,500</td>
<td>$417,298</td>
<td>$652,294</td>
<td>1</td>
<td>12</td>
<td>9</td>
<td>14</td>
<td>20</td>
<td>1</td>
<td>13</td>
<td>38</td>
</tr>
<tr>
<td>2006</td>
<td>$2,852,500</td>
<td>$433,974</td>
<td>$458,298</td>
<td>6</td>
<td>8</td>
<td>8</td>
<td>10</td>
<td></td>
<td>4</td>
<td>21</td>
<td></td>
</tr>
<tr>
<td>2007</td>
<td>$1,747,712</td>
<td>$434,567</td>
<td>$129,653</td>
<td>2</td>
<td>9</td>
<td>12</td>
<td>15</td>
<td>19</td>
<td>10</td>
<td>39</td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td>$80,000</td>
<td>$51,836</td>
<td>$131,836</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td></td>
<td>5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$10,664,712</td>
<td>$2,081,189</td>
<td>$1,942,988</td>
<td>46</td>
<td>51</td>
<td>57</td>
<td>84</td>
<td>2</td>
<td>57</td>
<td>164</td>
<td></td>
</tr>
</tbody>
</table>

**Total % Non-Monetary Penalties**

- 15%
- 17%
- 19%
- 28%
- 1%
- 19%
- 100%

---

**Figure 7-10** Average and Median Fines and Costs Imposed on Individual Offenders

---

111 Note that the decrease in average and median fines in 2008 can be partly attributed to the fact that I only looked at the cases that were dealt with by the IDA hearing panels up to June of that year.
Table 7-18 sets out the penalties imposed on individual offenders by the IDA hearing panels. A first glance at the data shows that the aggregate fines steadily increased from 1984 to 2004. When one examines the total fines imposed for each period, it is evident that the fines imposed in Period 1 were lower than the fines imposed in Periods 2 and 3. Given that the maximum fines that could have been imposed in Period 1 were $100,000 per offence for individual offenders, it is logical that the fines imposed in Period 1 would be lower than the fines imposed in Periods 2 and 3, where the maximum fines that could have been imposed on individual offenders increased to $1,000,000 per offence. That said, a closer look at the data shows that the aggregate fines imposed in Period 3, when a public member was added to chair hearing panels, increased by over $2.9 million from Period 2. This occurred even though data for Period 3 only covered approximately 4.5 years and dealt with 164 cases, as opposed to the 10 years covered and 276 cases heard in Period 2. The inverse relationship between the fines imposed and the number of cases heard from Period 2 to Period 3, indicates that the IDA’s hearing panels across Canada were imposing harsher fines on individual offenders when a public member was added to chair disciplinary hearings. Further evidence that harsher fines were imposed in Period 3 can also be seen in Figure 7-10. The trend in the average and median fines increased significantly in the latter part of Period 2 and continued to increase until the near end of Period 3. Of course, there is also the possibility that individual registrants were committing more serious offences in Period 3 than in Periods 1 and 2, for which higher fines were imposed.

Also evident from Table 7-18, is that the costs that the delinquent registrants were required to pay increased steadily from Period 1 to Period 3. What is noticeable from the data is the magnitude of the increase in aggregate costs over the three Periods. The aggregate costs that were ordered increased by approximately 9 times the amount...
from Period 1 ($173,306) to Period 2 ($1,385,853), and almost doubled from Period 2 to Period 3 ($2,081,189). Further proof of the increase in aggregate costs awarded can also be seen in Figure 7-10. Note that the trend in the mean and median costs started to increase from about the middle of Period 2, and continued to increase right to the end of Period 3. However, what is noticeable is that the number of cases heard in Period 3 (N=164) were much lower than the number of cases heard in Period 2 (N=276), yet the aggregate costs awarded to the IDA for conducting the investigations in Period 3 were higher than the aggregate costs awarded in Period 2. One possible explanation for this outcome is that the IDA’s investigators were spending more time investigating complaints and preparing them for hearings. It could also be that the cost of litigating and prosecuting cases, from initial complaint to final disposition, increased with the complexity and seriousness of the complaints or that the cost structure was adjusted upward.

Disgorgement orders were more pronounced in Period 3 than in Period 2. As can be seen in Table 7-18, the aggregate disgorgement of ill gotten gains was zero in Period 1, but increased to $688,592 in Period 2. One possible explanation for disgorgement being zero in Period 1, was that it may not have been available as an option for hearing panels to consider when imposing sanctions. Disgorgement increased by approximately 2.5 times the amount from Period 2 ($688,592) to Period 3 ($1,942,988). The increase in disgorgement from Period 2 to Period 3 might be reflective of the fact that hearing panels were placing more emphasis on it as a sanction than before.

Of the non-monetary penalties, permanent bans made up 3% (N=4) of penalties in Period 1 and increased to 9% (N=40) in Period 2 and 15% (N=46) in Period 3. Given that permanent bans are reserved for the more egregious cases, one can conclude that
the increases in the number of bans in Periods 2 and 3 were because individual registrants were committing more serious offences in these periods or that the panels started to treat these cases more seriously than in Period 1.

When one looks at other non-monetary penalties, it is clear that rewriting the license and terms and conditions were the sanctions most frequently imposed on individual offenders. Rewriting some form of a conduct and practice exam consistently declined from 53% (N=63) in Period 1, to 40% (N=174) in Period 2 and 28% (N=84) in Period 3. Terms and conditions made up 6% (N=7) of the non-monetary penalties imposed in Period 1, they increased to 20% (N=87) in Period 2, and then decreased slightly to 19% (N=57) in Period 3. Also notable from Table 7-18 is that the percentage of reprimands decreased from 19% (N=23) in Period 1, to 1% in Periods 2 (N=4) and 3 (N=2) respectively. What this trend indicates, is that the hearing panels chaired by a public member were less likely than the hearing panels that were not chaired by a public member, to impose sanctions that required offenders to rewrite a licensing exam. However, with the exception of Period 1, both the hearing panels chaired by a public member and the hearing panels not chaired by a public member, attached terms and conditions as part of the penalties.

The percentage of suspensions and supervisions imposed also increased from Period 1 to Period 3. The number of suspensions made up 9% (N=11) of all of the penalties imposed in Period 1, and increased to 13% (N=56) and 17% (N=51) in Periods 2 and 3. The average number of months per suspension orders was 30. However, there were 10 cases where suspension orders were specified for 10 years and 1 case where the suspension order was for 12 years. When these cases were removed from the data, the average number of months per suspension order was reduced to 21. The
percentage of supervision orders also increased from 8% (N=10) in Period 1, to 17% (N=76) in Period 2, and 19% (N=57) in Period 3. The average number of months per supervision order was 12. The implication of these findings is that the hearing panels chaired by public members were more likely to attach periods of supervision and suspension to individual offenders’ penalties, than the hearing panels that were not chaired by a public member.\textsuperscript{112}

**Member Firms**

*Penalties Imposed*

<table>
<thead>
<tr>
<th>Year</th>
<th>Fines</th>
<th>Fine</th>
<th>Disgorgement</th>
<th>Expulsion/Termination</th>
<th>suspension</th>
<th>Reprimand</th>
<th>T&amp;C</th>
<th>Total decision</th>
</tr>
</thead>
<tbody>
<tr>
<td>1984</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1985</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1986</td>
<td>$1,500</td>
<td>$350</td>
<td>3</td>
<td>3</td>
<td>3</td>
<td>3</td>
<td>3</td>
<td>22</td>
</tr>
<tr>
<td>1987</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>1988</td>
<td>$2,000</td>
<td>$5,000</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>22</td>
</tr>
<tr>
<td>1989</td>
<td>$25,000</td>
<td>$5,000</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>22</td>
</tr>
<tr>
<td>1990</td>
<td>$13,000</td>
<td>$700</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>22</td>
</tr>
<tr>
<td>1991</td>
<td>$10,000</td>
<td>$3,384</td>
<td>2</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>22</td>
</tr>
<tr>
<td>1992</td>
<td>$25,500</td>
<td>$6,500</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>22</td>
</tr>
<tr>
<td>1993</td>
<td>$33,000</td>
<td>$3,000</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>22</td>
</tr>
<tr>
<td>Total</td>
<td>$110,000</td>
<td>$18,934</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>22</td>
</tr>
<tr>
<td>Total % Non-monetary Penalties</td>
<td>25%</td>
<td>25%</td>
<td>50%</td>
<td>100%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

\textsuperscript{112} There may have been other factors involved in this change, for example, government or media demands for harsher penalties, but these factors are beyond the scope of this dissertation.
<table>
<thead>
<tr>
<th>Year</th>
<th>Fines</th>
<th>Cost</th>
<th>Disgorgement</th>
<th>Suspension</th>
<th>Reprimand</th>
<th>T&amp;C</th>
<th>Total decision</th>
</tr>
</thead>
<tbody>
<tr>
<td>1994</td>
<td>$12,000</td>
<td>$3,500</td>
<td></td>
<td></td>
<td></td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>1995</td>
<td>$185,000</td>
<td>$29,100</td>
<td></td>
<td></td>
<td></td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>1996</td>
<td>$322,500</td>
<td>$29,000</td>
<td></td>
<td></td>
<td></td>
<td>4</td>
<td>7</td>
</tr>
<tr>
<td>1997</td>
<td>$130,000</td>
<td>$23,450</td>
<td>1</td>
<td></td>
<td>1</td>
<td>8</td>
<td></td>
</tr>
<tr>
<td>1998</td>
<td>$42,000</td>
<td>$26,500</td>
<td></td>
<td></td>
<td>1</td>
<td>6</td>
<td></td>
</tr>
<tr>
<td>1999</td>
<td>$160,000</td>
<td>$7,000</td>
<td>1</td>
<td></td>
<td></td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>2000</td>
<td>$280,000</td>
<td>$43,360</td>
<td>$11,000</td>
<td>1</td>
<td>1</td>
<td>6</td>
<td>10</td>
</tr>
<tr>
<td>2001</td>
<td>$100,000</td>
<td>$15,500</td>
<td></td>
<td></td>
<td>1</td>
<td>4</td>
<td>6</td>
</tr>
<tr>
<td>2002</td>
<td>$4,110,000</td>
<td>$331,675</td>
<td>3</td>
<td>1</td>
<td></td>
<td>4</td>
<td>7</td>
</tr>
<tr>
<td>2003</td>
<td>$140,000</td>
<td>$42,750</td>
<td>2</td>
<td></td>
<td>2</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$5,481,500</td>
<td>$551,835</td>
<td>$11,000</td>
<td>8</td>
<td>6</td>
<td>21</td>
<td>61</td>
</tr>
<tr>
<td>Total % Non-monetary Penalties</td>
<td>23%</td>
<td>17%</td>
<td>60%</td>
<td>100%</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>Fines</th>
<th>Cost</th>
<th>Disgorgement</th>
<th>Suspension</th>
<th>Reprimand</th>
<th>T&amp;C</th>
<th>Total decision</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>$125,000</td>
<td>$29,000</td>
<td></td>
<td></td>
<td></td>
<td>3</td>
<td>4</td>
</tr>
<tr>
<td>2005</td>
<td>$23,041,579</td>
<td>$238,500</td>
<td>$22,596,579</td>
<td>2</td>
<td>2</td>
<td>5</td>
<td>12</td>
</tr>
<tr>
<td>2006</td>
<td>$1,133,921</td>
<td>$17,000</td>
<td></td>
<td>3</td>
<td></td>
<td>1</td>
<td>7</td>
</tr>
<tr>
<td>2007</td>
<td>$390,000</td>
<td>$45,000</td>
<td></td>
<td></td>
<td>1</td>
<td>2</td>
<td>7</td>
</tr>
<tr>
<td>2008</td>
<td></td>
<td></td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Total</td>
<td>$24,690,500</td>
<td>$329,500</td>
<td>$22,596,579</td>
<td>6</td>
<td>2</td>
<td>0</td>
<td>11</td>
</tr>
<tr>
<td>Total % Non-monetary Penalties</td>
<td>32%</td>
<td>11%</td>
<td>58%</td>
<td>100%</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 7-19 presents details of the penalties imposed on Member firms. A closer look at the monetary penalties shows that the aggregate fines imposed on Member firms increased significantly from Period 1 to Period 3. The aggregate fines imposed in Period 1 were $110,000, compared to $5,481,500 in Period 2 and $24,690,500 in Period 3. Granted that the maximum fines that could have been imposed on Member firms in Period 1 were $100,000 per offence, the aggregate fines are expected to be lower than the aggregate fines in Periods 2 and 3, where the maximum fines increased to
$5,000,000 per offence. However, what is noticeable from Table 7-19, is that when a public member was added to chair hearings, the aggregate fines imposed in Period 3 increased by 4.5 times the amount of the aggregate fines imposed on Member firms in Period 2. Notice also that Period 2 covered 10 years and a total of 61 cases were heard versus Period 3, which covered only 4.5 years and 30 cases were heard by the hearing panels. The implications of these findings for offences committed by Member firms is that the hearing panels chaired by a public member were more likely to dish out harsher fines than the hearing panels not chaired by a public member. As was the case with individual registrants, there is also the possibility the Member firms were committing much more serious offenses in Period 3 than in Periods 1 and 2.

In terms of other monetary penalties, the costs awarded to the IDA to conduct investigations increased significantly from Period 1 to Period 2 and Period 3. The aggregate costs awarded to the IDA to litigate and prosecute cases were $18,934 in Period 1, $551,835 in Period 2, and $329,500 in Period 3. Notice from these numbers that the costs increased from Period 1 to Period 2, and then decreased in Period 3. However, the total number of cases heard in Period 1 and Period 3 was only 22 and 30 respectively, compared to 61 cases heard in Period 2. Thus, the higher number of cases heard in Period 2 may be a reason as to why the aggregate costs awarded were higher in Period 2 than in Periods 1 and 3. Disgorgement of commissions, which was only imposed for two years throughout all three of the periods, is possibly related to the fact that Member firms mostly commit Internal Control Offences, whose infractions do not result in losses to investors.\(^{113}\)

\(^{113}\) Again, it could well be that disgorgement was not an option available for consideration by hearing panels when imposing sanctions in Period 1.
In terms of non-monetary penalties, permanent expulsion/termination from the Association is considered to be the most severe sanction that can be imposed on a Member firm. A closer look at Table 7-19 shows that permanent expulsions/terminations as a percentage of all non-monetary penalties imposed by the Association, fluctuated from 25% (N=1) in Period 1, to 23% (N=8) in Period 2 and 32% (N=6) in Period 3. At the same time, temporary suspensions as a percentage of all non-monetary penalties imposed consistently decreased from 25% (N=1) in Period 1, to 17% (N=6) in Period 2 and 11% (N=2) in Period 3. Reprimands were practically non-existent throughout all three Periods. These findings indicate that the hearing panels, with a public member as Chair, were more severe with the penalties imposed than the hearing panels that did not have a public member to Chair disciplinary hearings. That said, the hearing panels in both Periods 2 and 3 were consistent with the percentage of terms and conditions attached to the penalties imposed. In Period 2, terms and conditions made up 60% (N=21) of all of the penalties imposed, while in Period 3, they were 58% (N=11) - a finding that suggests that the panels were trying to ensure Member firms complied with the penalties imposed.

Summary

This chapter provided a description of the demographic profile of the investors in this study. A significant proportion of the investors were over the age of 65 and retired. They had limited investment knowledge, and an overwhelming majority had to borrow money to fund their investments. Their investment objectives were mostly income, and they were not particularity wealthy. In pursuit of income for basic living expenses, many incurred losses by investing with trusted family members, acquaintances and friends.
An overwhelming majority of the individual offenders were male and employed as registered representatives. Most of them circumvented the IDA’s By-laws within the first 5 years of employment. The majority of the Member firms that were involved in disciplinary proceedings were predominantly serving individual investors. Cases involving individual offenders and Member firms were for the most part, disposed of through settlement agreements with more than three-quarters of them being heard in the District Councils in Ontario, British Columbia (Yukon Territory) and Alberta. Individual offenders mostly committed Improper Sales Practice offences, while Member firms were predominantly involved in Internal Control offences. Even though the IDA continued to “funnel away” complaints with criminal elements from the justice system, harsher penalties were imposed on both individual offenders and Member firms when a public member was added to chair disciplinary proceedings. In the next chapter, I will look at the types of cases reviewed by the securities commissions.
Chapter 8: Data Analysis with Data from the Securities Commissions

In this chapter, I will examine the types of appeals that made their way to the ASC, BCSCn, and the OSC and the results of those appeals. The appeal cases heard by the Commissions came from four sources: Individual registrants, Member firms, the IDA, and the victims themselves.

Individual Registrants and Member Firms Appeals

Table 8-1 Individual Registrants and Member Firms Appeals to the Securities Commissions

<table>
<thead>
<tr>
<th>Year</th>
<th>Type of Issues</th>
<th>Commissions</th>
<th>Appeal Outcome</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>Procedural Fairness</td>
<td>BCSCn</td>
<td>Overturned</td>
</tr>
<tr>
<td>2007</td>
<td>Jurisdictional</td>
<td>BCSCn</td>
<td>Dismissed</td>
</tr>
<tr>
<td>2007</td>
<td>Jurisdictional</td>
<td>OSC</td>
<td>Dismissed</td>
</tr>
<tr>
<td>2008</td>
<td>Jurisdictional</td>
<td>OSC</td>
<td>Dismissed</td>
</tr>
</tbody>
</table>

As shown in Table 8-1, there were seven appeals brought by individual registrants and Member firms to the Commissions. Of these appeals, one was overturned and six were dismissed. One explanation for the majority of appeals being dismissed is highlighted in Dass. In Dass, the BCSCn sets out its standards “for reviewing decisions of a self-regulatory body like the IDA” as follows:

The Commission does not provide parties with a second opinion on a matter decided by an SRO. If the decision under review is reasonable and was made in accordance with the law, the evidence, and the public interest, the Commission is generally reluctant to interfere simply because it might have made a different decision in the circumstances. For this reason, generally, the person requesting the review presents a case for
having the decision revoked or varied and the SRO responds to that case...In these circumstances, the Commission generally confirms the decision of the SRO, unless the SRO has made an error in law; the SRO has overlooked material evidence; new and compelling evidence is presented to the Commission or; the Commission’s view of the public interest is different from the SRO’s (IDA v. Dass, 2007: para. 14)

The appeals to the Commissions all deal with procedural fairness and jurisdictional issues. Of the individual registrants’ appeals that were dismissed, two examined whether the IDA or the IDA’s staff had the legal right to apply for a review of a decision from an IDA’s hearing panel. Two other cases dealt with whether the IDA has jurisdiction to conduct disciplinary hearings against former registrants who were no longer working in the industry. The one case in which the decision of the IDA was overturned, dealt with an “error of law” and “breach of public interest,” in which the Respondent felt that he was prejudiced by the presence of a member on the hearing panel. Both appeals concerning Member firms came from the same firm. One was a motion that examined jurisdictional issues, while the other dealt with a “Refusal to Re-Open Ruling” from an earlier decision.

The IDA and Victims Appeals

Table 8-2  IDA and Victims Appeals to the Securities Commissions

<table>
<thead>
<tr>
<th>Year</th>
<th>Procedural</th>
<th>OSC</th>
<th>Jurisdictional</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td></td>
<td>OSC</td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td></td>
<td>ASC</td>
<td></td>
</tr>
<tr>
<td>2001</td>
<td></td>
<td>BCSCn</td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td></td>
<td>OSC</td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td></td>
<td>ASC</td>
<td></td>
</tr>
</tbody>
</table>

Table 8-2 sets out the details of appeals by the IDA staff and the victims of securities violations. There were two appeals by the IDA staff for a hearing and review of
decisions handed out by the hearing panels of the Alberta and Ontario District Councils. In one case, the Alberta District Council dismissed the charges against the Respondent. The IDA staff in turn, appealed to the ASC which overturned the District Council’s decision and allowed the appeal. In the other case, the OSC overturned the Ontario District Council’s decision, and changed the penalties the Council had imposed.

There were three appeals from victims, all of which were dismissed by the respective provincial Commissions. Two appeals dealt with reviews of the IDA’s decisions. The other appeal was a request for a review of the IDA’s decision in which it was decided that the IDA could not proceed with an investigation of the victim’s complaint regarding the conduct of his investment advisor. In dismissing the appeals, the Commissions noted that the victim were not “directly affected” by the IDA’s decision. In arriving at their decision, the Commissions made specific reference to Section 28(1) of the British Columbia Securities Act, which states that

> [t]he executive director or a person directly affected by a direction, decision, order or ruling made under a bylaw, rule or other regulatory instrument or policy of a self regulatory body or of an exchange may apply by notice to the commission for a hearing and review of the matter under Part 19, and section 165(3) to (5) applies (British Columbia Securities Act, 1996).

In Scott-Mancrieff, the BCSCn observed that

Section 28(1) does not require a person who seeks a hearing and review merely to be “affected” by the decision, but to be “directly affected”. By including the word “directly” the legislature must have intended a narrowing of the word “affected” and indeed the authorities have tended to agree (IDA v. Scott-Mancrieff, 2001: para. 13).

Finally, in Simpson, the ASC noted,
that a person directly affected has to be someone who is affected by the
terms of the order or decision, not just the incidental effects of the
decision. These decisions suggest that this is someone who is a party to
the proceedings that lead to the decision or someone to whom the terms
of the order or decision relate (IDA v. Simpson, 2005: para. 51).

After applying the principles of Section 28 (1) of the Act, the respective Commissions
noted that none of the victims were “directly affected” and therefore could not proceed
with their applications to review the IDA’s decisions.

Summary

It is important to point out that none of the appeals to the Commissions came
from registrants who were appealing their penalties. Rather, it was the victims who
wanted the Commissions to reviews the penalties imposed by the IDA on its individual
registrants. Note also that it was the IDA staff on two occasions who sought a review of
the penalties imposed on individual registrants. These requests for a review of penalties
imposed on individual registrants suggest that the victims as well as the IDA
enforcement staff were of the view that the penalties imposed were not proportionate to
the offence and harm caused by the Respondents’ misconduct(s). In the next section, a
qualitative analysis will be carried out to examine the aggravating and mitigating factors
considered in the imposition of sanctions by IDA hearing panels.
Chapter 9: Qualitative Analysis of the Aggravating and Mitigating Factors used to Determine Penalties

The IDA’s cases also list the aggravating and mitigating factors that were taken into consideration by hearing panels when imposing penalties. The IDA adopted the new Disciplinary Sanction Guidelines in 2003. In order to examine the factors considered in the imposition of sanctions, only cases that were heard between 2003 to June of 2008, were included in the analysis. From 2003 to June of 2008, the IDA hearing panels heard 238 cases. The hearing panels were very inconsistent in their usage of aggravating and mitigating factors when considering sanctions to be imposed on registrants. The factors that were coded were listed in the IDA’s Disciplinary Sanction Guidelines, and they were considered as either aggravating or mitigating factors (see IDA, 2006b: 7-11). As will soon be seen, some of the key considerations in determining sanctions were used as both aggravating and mitigating factors.

There were also cases where I identified aggravating factors, but the factors were not explicitly considered in the imposition of sanctions by the hearing panels. In making these decisions, I coded factors that were considered as aggravating factors in some cases, but not in other cases. For example, there were cases where the hearing panels explicitly made reference to “losses to clients” as an aggravating factor; however, there were also cases where “losses to clients” were present in the material facts of the case, but were not identified as aggravating factors by the hearing panels.

The IDA Disciplinary Sanction Guidelines (2006b: 7-11) lists the factors that the hearing panels must consider when determining sanctions for individual offenders and
Member firms. The list is “illustrative, not exhaustive,” and consists of the following factors:

**Harm to Clients, Employer and/or the Securities Market**

According to the Guidelines,

> [a]ctual harm can...be quantified by considering the type of transactions, the number of transactions, the size of the transactions, the number of clients affected by the misconduct, the length of time over which the misconduct took place, and the size of the loss suffered by the client(s) or the Member firm. Harm can also be measured using less empirical, but more subjective factors, such as the impact of a specific misconduct on a client's life (from an emotional, physical and/or mental perspective), or the impact on the reputation of the Member firm, or the reputation of the Canadian securities industry as a whole (p. 7).

**Blameworthiness**

The Guidelines note that,

> “i)n appropriate cases, distinctions should be drawn between conduct that was unintentional or negligent, and conduct that involves manipulative, fraudulent or deceptive conduct. Distinctions should also be drawn between isolated incidents and repeated, pervasive, or systemic contraventions of the Association’s By-laws, Regulations or other rules. It may also be appropriate to take into account the effect that illness or other extenuating circumstances of a personal nature may have on a registrant’s relative Blameworthiness (p. 7).

**Degree of Participation**

The Guidelines distinguish offenders who are direct participants and those who are not directly involved in the infraction.

As a general rule, there ought to be a distinction between the sanctions imposed on direct perpetrators and those with a lesser level of complicity. A Hearing Panel, when sanctioning multiple respondents, should take an individualized approach by determining, acknowledging, and taking into account the relationship of the particular respondent to the misconduct.
and other participating offenders. This is a large part of what is meant by "degree of responsibility". Any form of diminished or impaired responsibility should also be taken into account to mitigate blameworthiness (Pp. 7-8).

**Extent to which the Respondent was Enriched by the Misconduct**

The Guidelines go on to note that, "[i]n cases where the registrant benefited financially from the misconduct in question, it may be appropriate to require that any profits, commissions, fees, or any other compensation earned be disgorged" (p. 8).

**Prior Disciplinary Record**

In determining the appropriate sanctions, the Guidelines also take into account the prior disciplinary records of the offender. The Guidelines note that,

> [t]he fact that a respondent has no prior disciplinary record should, in the absence of evidence to the contrary, lead a panel to a presumption that the respondent was of good moral character prior to the misconduct. A first conviction may be seen as a measure of punishment in and of itself, given the attendant stigma attached to the process of charging, finding of guilt, and imposition of sanction. A good employment or internal discipline record should be a mitigating factor because it demonstrates responsibility and conformity to professional norms, which are the antithesis of the misconduct (p. 8).

However, in certain cases, "[a] prior disciplinary history may highlight a concern about individual or specific deterrence, an important objective of the disciplinary process, and the need to impose progressively escalating sanctions on repeat offenders [may be more appropriate]"(p. 8). The Guidelines go on to note that,

> it is important for the Hearing Panel to compare past misconduct with the misconduct at issue before determining whether there is any relevance. However, it is also important for the Hearing Panel to consider past misconduct that, while unrelated to the misconduct at issue, nevertheless
offers evidence of prior disregard for regulatory requirements, investor protection or market integrity (p. 8).

Acceptance of Responsibilities, Acknowledgement of Misconduct and Remorse

The Guidelines also have stipulations for offenders who show remorse, accept responsibility, and admit to the offence. According to the Guidelines,

[a]n admission of wrongdoing by a respondent is usually considered to be a mitigating factor because it implies remorse and an acknowledgement of responsibility. The extent of the mitigating value is affected by timing: the earlier, the better. Remorse can be indicated even after a hearing, although its value may be diminished (p. 8).

Credits for Cooperation

The Guidelines also give “credits for cooperation.” The Guidelines note that

[s]ince Member regulation is dependent in large part upon the adherence to internal controls and compliance regimes, full cooperation with Association investigations by registrants is expected. However, respondents or potential respondents should be given credit for cooperation if they act in a reasonable manner during the course of investigation and disciplinary process by self-reporting and self-correcting the misconduct in question (Pp. 8-9).

Examples of conduct that warrant cooperation credits are as follows:

• self-identification of a breach of the Association’s By-laws, Regulations, Rules and Policies;
• the internal investigation and/or report to the Association of all activities that may impact investor confidence or the integrity of the securities industry;
• full and timely cooperation with the Association when asked to provide assistance or information in the course of an investigation, including the voluntary production of all necessary books, reports and records required to assess the matter;
• ensuring that all relevant personnel are available for interviews to allow the Association to fully investigate any and all potential regulatory misconduct (p.9).
Voluntary Rehabilitative Efforts

Consideration is also given to any rehabilitative efforts on behalf of the offender. The Guidelines note that,

[...mediation efforts prior to (or even subsequent to) detection or intervention by the Association should be taken into consideration as mitigating the seriousness of misconduct. There will no doubt be concerns that subsequent rehabilitative efforts are self serving, but they warrant credit because they show both recognition of the misconduct and a commitment to remedy it. The respondent is entitled to mitigating credit for voluntary acts of reparation, including voluntary disgorgement of commissions, profits, other benefits and/or payment of restitution to clients (p. 9).

Further, “other rehabilitative actions that can be taken into consideration include”:

1. Whether a Member firm voluntarily employed subsequent corrective measures, prior to detection or intervention by the Association, to revise general and/or specific procedures in order to avoid recurrence of misconduct.
2. Whether an individual respondent is/was disciplined by their Member firm for the misconduct at issue prior to regulatory detection (p. 9).

Reliance on the Expertise of Others

The offender’s conduct can also be mitigated if it was deemed that he or she relied on the expertise of others. According to the Guidelines,

it is expected that registrants will use proper care and exercise independent professional judgment at all times in the course of their business activities. However, there may be times when an Approved Person’s relative culpability may be tempered by his/her reliance on the expertise of others. Hence, the following may be seen as mitigating factors:

1. whether, at the time of the contravention, the registrant’s Member firm had developed adequate training and educational initiatives; or
2. whether a respondent demonstrated reasonable reliance on supervisory, legal or accounting advice that subsequent to the misconduct in question, was found to have been erroneous (Pp. 9-10).
Planning and Organization

The Guidelines also note that, “evidence of planning and pre-meditation are aggravating factors” (p. 10). As such,

Hearing Panels should consider the degree of organization and planning, associated with the misconduct, along with the number, size and character of the transactions. Evidence of calculated and deliberate acts may foreclose a claim of rash action or temporary lapse of judgment (p. 10).

Other factors stipulated by the Guidelines are as follows:

1. 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; and
2. Whether the respondent engaged in the misconduct at issue notwithstanding prior warnings from the Association, another regulator, or a supervisor (in the case of an individual respondent) that the conduct violated Association rules or applicable federal or provincial statute relating to the trading or advising in respect of securities or commodities or of any regulation or policy made pursuant thereto (p. 10).

Multiple Incidents of Misconduct over an Extended Period of Time

The Guidelines also have considerations for multiple incidents committed by the offender(s) over an extend period of time (p. 10). According to the Guidelines, “generally, blameworthiness is compounded as the number of incidents expand[s]…[t]his rationale applies to all types of misconduct: a series of victims indicates a pattern, which compounds the culpability (p. 10).

Vulnerability of Victim

The Guidelines also seek to protect vulnerable victims. According to the Guidelines,
The disciplinary process must be seen to provide some degree of protection for the investing public, and in particular, the client with a lower level of sophistication. Consequently, the vulnerability of a victim should be taken into account in determining relative culpability, and hence the relative measure of the sanction imposed. However, if there is evidence that the respondent sought out “vulnerable” clients, then this should be seen as an aggravating factor worthy of a greater sanction (p. 10).

Failure to Cooperate with the Association’s Investigation

The Guidelines note that, “[f]ailure to cooperate with the Association’s investigation into a Registrant’s conduct can form the grounds for a separate disciplinary offence, under Association By-law 19.5” (p. 10). However, if the primary misconduct being investigated can be proven without the cooperation of the registrant, a failure to cooperate can be taken into account as an aggravating factor, or as evidence of a registrant’s resistance to governance that may escalate the sanction from a fine to a suspension or permanent ban from membership (p.10).

Significant Economic Loss to the Client and/or Member Firm

Significant loss to a client’s account is also taken into consideration in determining the appropriate penalty. According to the Guidelines,

[a] finding of a significant monetary loss by the respondent’s clients or the Member firm arising out of the respondent’s misconduct can be seen as an aggravating factor to the extent that investing has at its core capital preservation and returns. If that core function is significantly eroded by regulatory misconduct, then it should be taken into account when the appropriate penalty is imposed (p.11).
Aggravating Factors

Figure 9-1 shows the aggravating factors that were identified and considered, as well as the aggravating factors that were identified but not considered in the imposition of the penalties. With the exception of failure to cooperate, what stands out most is that for each factor, the proportion of aggravating factors identified but was not considered, exceeded the proportion of aggravating factors that were identified and considered in the imposition of sanctions by the hearing panels. This finding points to the possibility that the IDA hearing panels were more likely not to see (than to see) aggravating factors where they existed.

Failure to cooperate with the Association’s request for information comprised 24% of the aggravating factors considered in the imposition of penalties. The Association takes a Respondent’s “failure to attend and be questioned” by Enforcement staff as a serious issue because it “compromised the Association’s ability to complete [an] investigation” (IDA v. Bagnell, 2003: para. 17). A failure to cooperate with the
Association's request for information, “even if based upon a matter of principle, strikes at the very integrity of the Association’s duty and ability to police itself” (IDA v. Union Securities Ltd, 2005: 55). More importantly, the impact of non-compliance can “[stop] the investigation completely” (IDA v. Crittall, 2004: para. 8). For example, in Stewart, the Association noted that the “Respondent's failure to provide the information and documentation and failure to attend [a] interview, as requested, resulted in the Association not being able to proceed further in the investigation of the Respondent’s activities” (IDA v. Stewart, 2005: para. 15). In another case,

the Respondent[s]' refusal to cooperate effectively stalled [the investigation] for eight months or more. While, it is impossible to know the extent of the prejudice, which the delay has caused to the investigation, it cannot be doubted that delay is usually prejudicial to an investigation (IDA v. Union Securities Ltd, 2005: para. 50 emphasis added).

Note also, that planning and organization made up 18% of the aggravating factors identified and considered in the imposition of penalties. One of the issues considered by the hearing panels dealt with outright deception by the respondent. For example in Armstrong,

the Alberta District Council took into account the scope of the Respondent's misconduct, in that it involved a large number of clients, hundreds of transactions and it extended over a period of years. In addition to the complaints received by the Association, over 150 complaints were received by Nesbitt itself with respect to Ms. A[s]'...conduct....While the disciplinary panel found it difficult to ‘extend the characterization of [Ms. A’s] activities from a level of gross negligence to that involving deception or fraud, it is difficult to characterize [her] activities with respect to the mispricing of the securities in question on client statements as anything but deliberately deceptive’ (IDA v. Armstrong, 2003: para. 10).

In other cases, the Panel took into consideration the deliberate or intentional conduct of the Respondent. In Shanahan, the Panel argued that
[t]he type of conduct in relation to the trading scheme was intentional and designed to create the scheme which we found to exist in our reasons. This type of trading scheme leads us to conclude that serious sanctions as to registrations must be imposed. A scheme of this nature which involved a high degree of planning and organization and involved a large number of clients also calls for severe sanctions (IDA v. Shanahan: para. 166).

Similarly, in Djordjevic, the Panel noted that “[t]he respondent’s behaviour was egregious…[in that] he deliberately forged the signature of a client on a guarantee of another client’s account… His activity was not negligent, but deliberate and deceptive (IDA v. Djordjevic, 2007: para: 46). In McCaffrey, the Panel reasoned that “[t]he Respondent's violations extended over several months… His conduct was, … serious, wrong, fraudulent, conscious and deliberate” (IDA v. McCaffrey, 2003: para. 18). 

Figure 9-1 also shows that in 19% of the cases where issues regarding planning and organization of the offence existed, the panels did not identify them as such in the imposition of penalties. These issues were no different from the issues that were identified as planning and organization of the offence, and considered in the imposition of penalties in other cases. For example, in IDA v. Tang (2003), the respondent was involved in the planning and organization of the offence, yet the Panel did not identify this as an aggravating factor in the imposition of penalties. More specifically, the respondent

misappropriated approximately $925,000 from the…accounts of family and friends by causing the [Member firm] to engage in transactions involving the exchange of Canadian dollars and US dollars with the holders of the accounts[,] which improperly benefited the holders of the accounts…On at least ten occasions, the exchange rate applied to the transaction was inordinately more favourable to the client than the Bank of Canada rate for the date of the transaction. Further, on at least twenty-one occasions, Ms. T…caused an inappropriate amount to be credited to one of the accounts as part of the exchange rate transaction (IDA v. Tang, 2003: para. 6-7 emphasis added).
Similarly, in another case involving 33 clients and 76 acts of forgery, planning and organization of the offence was present, but was not identify by the Hearing Panel when determining penalties. In the *IDA v. Holowatiuk* (2004), the Hearing Panel appeared to ignore the evidence of the deliberate misconduct and gave more weight to the Respondent’s explanation for his behaviour: The Hearing Panel noted that

> [t]he Respondent has advised the Association that he committed the acts of forgery as a response to his emotions of feeling overwhelmed at times by the number of referrals and the paperwork involved in the transaction of his business and the lack of administrative support. The Respondent has further advised his intent was to expedite transactions in an effort to effectively perform his employment duties within the time constraints and pressures inherent in the occupation (*IDA v. Holowatiuk*, 2004: para. 16).

These examples suggest that even though there was evidence of pre-mediation and planning in the respondents’ conduct, they were ignored by the hearing panels when determining the penalties they imposed.

Multiple incidents of misconduct over an extended period of time made up 15% of the aggravating factors identified and considered, and 22% of aggravating factors identified but not considered in the imposition of penalties. The IDA’s Sanction Guidelines did not define what exactly constitutes “an extended period of time” (See IDA, 2006b: 10). In order to code this variable, I perused the cases in which “multiple incidents of misconduct” were considered and approximately 99% of them referred to acts that occurred over a six-month period. To keep with the trend, I defined and coded “multiple incidents of misconduct” to mean the acts had occurred over at least a six-month period.
In assessing multiple incidents of misconduct over an extended period of time, the hearing panels seemed to put a lot of weight on repeated behaviour that ignored the “red flags,” which led to the misconduct. In Graham, the Hearing Panel noted that Mr. G… had serious supervisory responsibilities, and he failed. The result of this failure was the loss of a significant amount of money. While we agree with Mr. Gross that there was really just one error, our view is that the error was seminal and grave and was repeated over and over. Mr. G… was presented with many “red flags” - as the Guidelines label them - and he chose to ignore them (IDA v. Graham, 2005: para: 28).

In other cases, the hearing panels looked at the scope of the misconduct when considering sanctions. In Armstrong, the Panel noted that

[t]his was not an isolated incident or conduct involving a limited number of transactions over a limited period of time. The Respondent's misconduct involved a large number of clients, hundreds of transactions and extended over a period of four years. While the wrongdoing with respect to the ten complainant clients in the Notice of Hearing involved a loss of those clients of approximately $2 million, the Association's counsel has also put before us further information with respect to similar conduct involving over 100 additional complaints by the Respondent's clients. In excess of 150 additional complaints were received with respect to the Respondent's conduct…(IDA v. Armstrong, 2003: para. 37).

Similarly, in Gareau, the Panel argued that

[t]here were 14 clients affected over several months by Mr. G’s negligent conduct. Also, there was information that came to his attention that should have caused him to alter his conduct and refrain from giving the same investment advice to subsequent clients (IDA v. Gareau, 2005: para. 68).

Culpability is also attached to misconduct that prejudices the Association's investigation. In Michaels, the Panel noted that “[t]he Respondent’s deception of the Association continued over an extended period of time and had the effect of delaying completion of the Association's investigation” (IDA v. Michaels, 2007: para: 26).
While the hearing panels considered multiple incidents of misconduct over an extended period of time in some cases, in others, multiple incidents were present but not addressed by the hearing panels when considering sanctions. For example, in one case, the Respondent “admitted that between January 2000 and May 31, 2002 he acted contrary to [the] Association By-law 29.1, in that he … effected 7 unauthorized transactions in the accounts of 3 separate clients, without prior authorization from those clients” (IDA v. Miller, 2005: para. 2). In another case, the Respondent misappropriated funds from clients and her employer over a two year period (see IDA v. Judt, 2005: para. 4). There are also other examples of cases in which “the Respondent engaged in the conduct of forgery of client signatures to client account documentation,” as well as “[misleading] the Member by providing false information during the course of an internal investigation in respect of the Respondent’s conduct in the forgery of client signatures to client account documentation,” over a nine month period (IDA v. Blaker, 2007: para. 42). These are just a few examples of cases where multiple incidents of misconduct were identified, but appeared not to be taken into consideration in the imposition of the penalties.

When one considers the number of victims that incurred losses on their investments, it is rather surprising that economic loss to the client and/or Member firm only made up 15% of aggravating factors identified and considered in the imposition of sanctions. The identification of losses taken into account by the hearing panels was rather straightforward. In Thompson, the Panel noted that “[t]he Respondent’s clients lost one quarter or more of their investment together with the opportunity costs on the funds recovered” (IDA v. Thompson, 2004: para. 74). Similarly, in Gareau, the Panel took into consideration the fact that “[v]ery significant losses were caused as a result of
the Respondent’s conduct... No fewer than 14 clients lost a total of $724,000 (IDA v. Gareau, 2005: para. 68).

More important however, is that in 20% of the cases, losses to clients’ accounts were identified but not considered in the imposition of sanctions. In one case, a married couple lost $202,000 in unauthorized trades from their joint account (see IDA v. Brazeau, 2005: para. 8). In other cases, the investors lost their entire investment. In Konidis for example, the investors “lost their entire investment …which totaled $26,353.80” (IDA v. Konidis, 2003: para. 19). Similarly, in Grieve, a 63 year-old widow lost $150,000 because of unsuitable investments; another client who was a “50-year-old electrician with less than a complete high school education and very limited investment knowledge…lost his entire investment …a total of approximately $22,400” (IDA v. Grieve, 2003: para. 8, 38, and 40). Yet, none of the losses incurred in these cases were used as an aggravating factor in considering the appropriate penalties.

Harm to clients, employers and/or the securities market were only identified and considered as aggravating factors in 14% of the cases. In the majority of the cases, the amount of financial losses incurred by the clients was the key factor that was taken into consideration in determining what constitutes harm. For example, in Youden, the Panel noted that two of the Respondent’s clients “sustained losses over a two year period” (IDA v. Youden, 2005: para. 116). In Schillaci, the Panel took into consideration that “there [were] two clients who suffered losses through many large transactions...[these losses were] consider[ed]...to be significant relative to their financial circumstances” (IDA v. Schillaci: para. 73).

In other cases, the hearing panels took into consideration the cost of harm to the general investment public, Member firms and the securities market. In Leung, the Panel
noted that the Respondent “fraudulently circumvented regulatory requirements resulting in substantial harm to members of the investing public” (IDA v. Leung, 2005: para. 1). More specifically, the respondent facilitated an RRSP stripping scheme by opening accounts at the Member firm that he worked at, for investors who were recruited by way of newspaper advertisements (IDA v. Leung, 2005: para. 6). In Djordjevic, the Panel stated that “forgeries …cause harm to the employer and harm to the securities markets… They sap the confidence of market participants that the system operates fairly and honestly” (IDA v. Djordjevic, 2007: para. 50).

Approximately 18% of the cases involved harm that was identified, but not considered as an aggravating factor. In keeping with the trend to identify harm based on financial losses, the Panel in Dempsey noted that

[from January 1, 2000 to June 30, 2002 MAP's RIF Account had a rate of return of -70% and the value of the account declined by $38,589.53. From January 1, 2000 to August 31, 2001 the C Margin Account had a rate of return of -48% and the value of the account declined by $97,627.93 and RC's RSP Account had a rate of return of -29% and the value of the account declined by $20,040.39. The C&S Joint Margin Account had a rate of return of -31% and the value of the account declined by $39,060.42… From January 1, 2000 to December 31, 2001 SA's Cash Account had a rate of return of -7% and the value of the account declined by $10,592.69. SA & MB's Joint Account had a rate of return of 4.3% and the value of the account increased by $6,693.50. From January 1, 2000 to May 31, 2001 HJ's Margin Account had a rate of return of -28% and the value of the account declined by $44,114.80 and HJ's RIF Account had a rate of return of -27% and the value of the account declined by $3,643.09 (IDA v. Dempsey, 2005: para. 38-41).

All of the clients' accounts noted above declined substantially in value, but at no point throughout the case were there any references made to the harm caused to the clients. In another case, the Respondent and the Branch Manager were “involved in an illegal distribution of securities by breaching the prospectus exemption available under the Alberta Securities Act” (IDA v. Cubbon, 2006: para. 17). The Respondent "did not
specifically ask,” nor was she informed by the Branch Manager or any other senior employees, that the distribution contravened the Member firm’s policies, the Association’s By-laws and the Alberta securities laws (para. 84). Yet, the Hearing Panel neither identified nor considered such conduct as harmful to the Member and securities market.

The Respondents’ enrichment comprised 7% of the aggravating factors that were identified and considered in the imposition of sanctions. In assessing the “extent to which the respondent was enriched by the misconduct,” particular attention was given to the commissions earned from the misconduct. In Armstrong,

[t]he panel … found it significant that Ms. A benefited considerably from the misconduct in question, in that her commissions earned from the transactions that were the subject of this prosecution involving the ten complainants alone amounted to approximately $241,000.00 (IDA v. Armstrong, 2003: para.10).

Similarly, in Dimitriadis, the Panel highlighted the fact that the “Respondent made a profit, however, with the commissions he was receiving. In fact, the operations of the [R]espondent in the S’s account generated approximately $76,000 in gross commissions” (IDA v. Dimitriadis, 2004: para. 18). In other cases, the hearing panels assessed “enrichment” by taking into consideration the amount that was misappropriated from clients’ accounts. In Hart, the Panel noted that “the Respondent fraudulently misappropriated over $800,000 from two [elderly] widows … for his ‘self-enrichment’ (IDA v. Hart, 2006: 6-7). In Petriello, the Panel made reference to the fact that “[t]he Respondent misappropriated amounts totaling $124,000 belonging to his client over a long period of almost two years during which,…[he]…continue[d] to benefit” from the scheme (IDA v. Petriello, 2007: para. 25).
The Respondents' enrichment comprised 13% of the aggravating factors identified, but were not considered in the imposition of penalties. Note that this is five percentage points more than the number actually considered as aggravating factors by the hearing panels. In one particular case, the commission charged by the Respondent was more than half of the client's original investment (IDA v. Xiao, 2004: para. 35-39).

The client "was single, 42 years old, employed as a hotel housekeeper for an annual salary of $20,000," and "deposited $50,000 in her account; however, the "total purchases amounted to approximately CDN $8,276,047" (para. 18, 36, and 38). The client reportedly "paid approximately CDN $25,258 in commissions" for these purchases (para. 39). In assessing the penalty, the Panel simply noted that the "total commission charges for an eight-month period…was excessive, conducted in willful and/or reckless disregard of [the client's] best interests," without specifically making reference to the Respondent's enrichment from the misconduct (para. 51). Furthermore, the Respondent was only required to disgorge commissions in the amount of $5,051.60 (para. 56).

There were also cases where the Respondent benefitted financially from fees charged, but these fees were not considered as enrichment by the Hearing Panel. For example, in Tobin, the Respondent was involved in discretionary trading in six clients' accounts (IDA v. Tobin, 2006: para. 3). "All of the client accounts…were fee based accounts" (para. 64). During the period (January of 2003 to April of 2003) in which the misconducts took place,

"[t]he Respondent's gross fees…were approximately $60,000. After deductions for his split (50/50) and reasonable branch expenses that the Respondent was required to cover, the agreed upon amount to be repaid for fees was accordingly $28,000" (para, 64).
Yet, in discussing the aggravating factors in this case, no reference was made by the Hearing Panel to the Respondent’s enrichment (see para. 5-9).

The vulnerability of victims was only taken into account as an aggravating factor in 7% of the cases. In some cases, when the vulnerability of victims was considered, the Hearing Panel focused on the level of the clients’ market sophistication. In *Leung*, the Panel considered the fact that the RRSP stripping scheme ... *fraudulently circumvented regulatory requirements resulting in substantial harm* to members of the investing public. In determining penalties, the Panel was influenced by the fact that the defrauded investors had little or no market sophistication and the funds, in large measure, came from retirement savings (*IDA v. Leung*, 2005: para. 1 emphasis added).

Similarly, in determining the Respondent's penalties in *Yanor*, the Panel made reference to the fact that the client’s “sophistication was minimal” (*IDA v. Yanor*, 2005: para. 27). In *Schillaci*, the client's inability to recognize an experienced advisor, made the client vulnerable in the eyes of the Hearing Panel.

The Panel agrees with the submissions of the Respondent that the clients in question chose E.L. as their broker and clearly wanted to participate in risky trading in order to experience significant financial gains. Further, there is no evidence to prove that the clients were unable to sustain the losses that occurred. However, the Panel also agrees that the clients were vulnerable in that they failed to realize the lack of E.L.’s experience as a broker (*IDA v. Schillaci*, 2007: para. 84).

In other cases, the hearing panels took into account the circumstances of the victims in determining sanctions. For example in *Hart*, the Respondent misappropriated funds from two elderly widows’ accounts. In determining the appropriate penalties, the Panel noted that the case “showed a clear plan of forgery and deceit and was an egregious breach of
trust committed against two vulnerable individuals” (*IDA v. Hart*, 2006: para. 10). In *Puccini*, the Panel took into consideration that the facts as proved demonstrated that the investors affected by the Respondent were vulnerable. In particular, the facts set out in the Notice of Hearing disclosed that in the case of one count of unauthorized trading and one count of forgery relating to the opening of a margin account the investor, EA, was a 60 year old retired widow recovering from breast cancer (*IDA v. Puccini*, 2007: Para. 8).

In 8% of the cases, the vulnerability of victims was identified, but was not considered in the imposition of sanctions. In *Wong* for example, the Respondent recommended and purchased Government of Argentina bonds for six elderly and unsophisticated clients "without first using due diligence to ensure that the recommendation was suitable for those clients based on their financial situation, investment knowledge, investment objectives and risk tolerance" (*IDA v. Wong*, 2005: para. 62). These recommendations resulted in significant losses to the clients' accounts. In one particular instance, the clients were an elderly married couple who could not "read English and [even]...went to the Respondent's office on a monthly basis because they had difficulties understanding their monthly account statements" (para. 55). In *Gurion*, the Respondent misappropriated $353,587 from an 89 year old novice female investor, and then left Canada and settled in Russia (*IDA v. Gurion*, 2004: para. 2 and 10). While the Panel acknowledged the “extreme gravity of the Respondent's conduct,” at no point did they allude to the client's vulnerability as an aggravating factor (para. 8). As a matter of fact, the aggravating factors were completely ignored in this case. Given that the Respondent is now living and working in Russia, it would be logical for the Panel to conclude that it would be unlikely that the penalties imposed would have been complied with.
Figure 9-2 Mitigating Factors Considered in the Imposition of Penalties

Figure 9-2 presents the mitigating factors considered by the hearing panels in the imposition of penalties. The Respondents' lack of a “prior disciplinary record” made up 24% of the mitigating factors considered by the hearing panels. The Respondents' prior records were often used to mitigate against harsher penalties. In Chan, the fact that the Respondent had no prior record was one of the factors taken into consideration in reducing her penalty from a fine of $3,000 to a reprimand (IDA v. Chan, 2003: para. 2-3).

Similarly, in Loftus, the Panel "reduced the fine [from $30,000] to $25,000, and the costs [from $10,000] to $7,500, taking into account the cooperation of Mr. L, and the fact that he did not have a prior disciplinary record" (IDA v. Loftus, 2004: para. 16).

In other cases, the length of time that the Respondent spent in the industry with a clean record also mitigated against harsher penalties. In Wright, the Panel's decision was influenced by the fact that, "in a career of some 25 years in the industry[,] Mr. W
ha[d] never been the subject of any disciplinary action" (IDA v. Wright, 2005: 5).

Similarly, in Youden, the Panel noted that the Respondent "ha[d] no disciplinary record during his prior 37 years of involvement in the securities industry" (IDA v. Youden, 2005: para. 120). In Tobin, the Panel considered

that there had been no prior disciplinary proceedings commenced against the Respondent by the Association during his 20 year employment history by Member firms. This fact is considered by the Association sanction guidelines. Section 3.5 provides a good employment record with no prior disciplinary record should lead a panel to conclude a respondent is of good moral character and considered as a mitigating factor (IDA v. Tobin, 2006: para. 10).

The acceptance of responsibilities, acknowledgement of misconduct and remorse, made up 21% of the mitigating factors considered in the imposition of sanctions. When this was considered as one of the mitigating factors against harsher sanctions, the hearing panels made specific reference to the Respondents' acknowledgement of their responsibilities and misconduct. In Gawthrop, the Panel noted that "the Respondent should not be visited with a serious fine because...he admitted [to] his responsibility" for his misconduct (IDA v. Gawthrop, 2003: para. 10). In Saturley, the Panel noted that "[t]he Respondent appear[ed] to have accepted his responsibility in this matter" (IDA v. Saturley, 2004: para. 8). Similarly in Saltsman, the Panel noted that "[t]he Respondent ...admitted to his misconduct ...to both Association Staff and the Member firm" (IDA v. Saltsman, 2003: para. 23).

In other cases, the hearing panel noted that the acceptance of responsibility included or implied remorse. For example in Graham, the Panel reasoned that "there [was] agreement that Graham ha[d] accepted responsibility and [was] remorseful" (IDA v. Graham, 2005: para. 26). Likewise, in Gareau, the Panel took into consideration that the Respondent "has[d] accepted responsibility and [was] remorseful for his conduct"
In *De Long*, the Panel stated that one of the reasons that they accepted the Settlement agreement was because the Respondent "admitted to the inappropriateness of his conduct and ha[d] expressed remorse regarding any negative impact his conduct may have had upon the reputation of [the Member firm] and its business relationship with its trustee (*IDA v. De Long*, 2005: para. 10). One should be cautious when trying to interpret these cases, because it cannot be known for certain whether the Respondents were genuinely showing remorse for their actions or whether they were simply expressing that they felt remorse in order to receive lighter penalties.

Credit for cooperation made up 19% of the mitigating factors considered in the imposition of sanctions. In assessing this factor, the hearing panels paid particular attention to whether or not the Respondent fully cooperated with the Association's investigation. In *Armstrong*, little weight was given to the Respondent's initial cooperation because of her subsequent withdrawal from the investigation (see *IDA v. Armstrong*, 2003). More specifically, the Panel noted that they considered "the Respondent's initial participation and co-operation in the Association's investigation. However, given her subsequent withdrawal from the process, [they] accord her initial participation little weight" (para. 41). On the other hand, in *Boulieris*, the Respondent's participation in the Association's investigation was fully acknowledged. The Panel took into consideration the fact that,

the Association's investigators acknowledged that the Respondent had co-operated with every aspect of the investigation and had provided all requested files and documents. In particular, the last Statement given by the Respondent was given only two weeks before these proceedings, pursuant to an order of this Panel, at the request of the Association, to pose questions that were not previously dealt with (*IDA v. Boulieris*, 2003: 29).

In *Thompson*, the Panel noted that the Respondent
ha[d] cooperated throughout with the Association in its investigation ...[and] most importantly, the Respondent did not walk away from the situation. Using his own resources, he pursued [Mr. D] with the Department of Lawyer Regulation of the Florida State Bar. It is largely due to his efforts that the majority of the money was recovered for the investors in the Debtors Certificates (IDA v. Thompson, 2004: para.87-88).

In another case, the Panel took into consideration Respondents who reported the case(s) on their own initiative and saved the Association from incurring unnecessary costs, as a mitigating factor. In HSBC Securities for example, the Panel reasoned that,

[t]he Respondent cooperated fully with Staff in the investigation in this matter. The Respondent reported promptly and on its own initiative its under-reporting on its response to the January 2004 survey once the error came to its attention. The Respondent, voluntarily and on its own initiative ha[d] established satisfactory arrangements to identify and address emerging issues in the securities industry and ha[d] established appropriate record keeping and data assessing arrangements to address the communication deficiencies that led to the initial under-reporting of the Market Timing activity in this case. As such, the Respondent has demonstrated an understanding and commitment to its gatekeeper role (IDA v. HSBC Securities, 2005: 44-45).

In Doering, the Panel noted that the Respondent's cooperation worked to advance the proceedings by “collaborat[ing] with enforcement counsel to produce the Agreed Statement of Facts” (IDA v. Doering, 2007: para. 20). By doing so, the Respondent saved the Association from incurring unnecessary costs and a great deal of time (para. 20).

Voluntary rehabilitative efforts by the Respondents made up 13% of the mitigating factors taken into consideration by the hearing panels when imposing sanctions. In considering voluntary rehabilitative efforts as a mitigating factor, the hearing panels took into consideration acts of restitution taken on behalf of the Respondents. In determining the appropriate penalties in Chan,
the Association considered a number of unique mitigating factors which included the fact that full restitution had been paid to the clients; the [R]espondent, currently aged 69, had delayed her retirement in order to continue to make restitution payments to her former employers (IDA v. Chan, 2003: para. 2).

In Clarke, the Respondent cooperated with his employer and the Association "to resolve financial problems arising from his conduct" (IDA v. Clarke, 2007: 19). The Panel noted that the Respondent’s employer

ha[d] entered into settlement arrangements with the involved clients. It [was] believed [that] the total losses [were] in the range of $500,000.00. The Respondent ... contributed the sum of $368,000.00 toward those settlements. He substantially liquidated his financial holdings and mortgaged his interest in his matrimonial residence to do so (para. 19).

There were also cases where mitigating credits were given to remedial actions that involved corrective measures to prevent the misconduct from reoccurring. For example in Schillaci,

[t]he Respondent... demonstrated rehabilitation by taking the [Effective Management Seminar], developing procedures for supervision and follow-up, retaining evidence of his supervision efforts, recognizing the need to consult with clients to ensure their accounts are being handled properly and ending relationships with questionable brokers (IDA v. Schillaci, 2007: para. 80).

Other rehabilitative actions considered, have to do with Member firms voluntarily employing corrective measures to address the deficiencies that led to the misconducts in the first place. For instance in Scotia Capital Inc, the Panel “acknowledge[d] that since the period of time in question, the Respondent ha[d] implemented numerous changes to its policies and procedures that ha[d] improved its ability to effectively perform its compliance and supervisory function" (IDA v. Scotia Capital Inc, 2003: para: 22). In assessing the sanction in Brant Securities Ltd, the "Staff specifically considered as a
mitigating factor the fact that the Respondents ha[d] made significant efforts to address the deficiencies [that led to the infractions] and that those deficiencies ha[d] been satisfactorily resolved” (IDA v. Brant Securities Ltd, 2004: para. 98).

Respondents' blameworthiness made up 8% of the mitigating factors considered in the imposition of sanctions. When considering blameworthiness, one of the factors that the hearing panels took into consideration was whether the Respondents' conduct was unintentional or negligent. In Schillaci, the Panel found that

the conduct of the Respondent occurred through negligence and naivety. The Respondent was new to the position of Branch Manager and as [was] clear in the Union decision ... was not supervised. Albeit late, the Respondent did elevate his concerns to responsible persons within [the Member firm] with respect to E.L.'s conduct, without receiving response or direction. In the end [,] the Respondent took it upon himself to put E.L. under strict supervision... (IDA v. Schillaci, 2007: para. 74).

Likewise in Gareau, the Panel considered that "[o]n a scale from innocent conduct to dishonesty, the Respondent's conduct was not on the deceptive end of the scale; however, he clearly was negligent in failing to carry out the necessary due diligence required of him" (IDA v. Gareau, 2005: para. 668). In Youden, the Panel noted that “[t]here is no suggestion that there was any fraudulent or deceptive conduct on the part of Mr. Y. While Mr. Y did take some steps to monitor daily and monthly account statements, his supervision ...was inadequate” (IDA v. Youden, 2005: para. 117).

In other cases, the hearing panels took into consideration “illness or other extenuating circumstances of a personal nature [that] may have [an impact] on a registrant’s relative blameworthiness” (IDA, 2006b: 7). In Brennan, the Panel was advised that “Mr. B had suffered from severe depression and psychological illness” (IDA v. Brennan, 2004: para. 12). In Pryde, the Panel took into consideration that the
Respondent was suffering from severe manic episodes diagnosed as a bi-polar disorder for which he had been under regular treatment. This disorder necessitated him being hospitalized... The Respondent continued to suffer from a state of deteriorated mental health and he controlled his symptoms of bi-polar disorder through medication and counselling (IDA v. Pryde, 2005: para. 13 and 15).

Similarly in Clarke, the Panel made reference to the fact that the Respondent unauthorized trading in the CA and RC accounts was the result of a combination of the extreme personal stress he was under at the time, both at home and at work, and his wanting 'to do very well for CA and RC'. Clarke has been undergoing therapy in order to deal with the underlying conditions that caused his behaviour (IDA v. Clarke, 2007: para. 50).

Even though enrichment, losses and harm to clients were cited as aggravating factors, there were also times when they were considered as mitigating factors by the hearing panels. As can be seen in Figure 8-2, Respondents who were not enriched by their misconduct made up 6% of the mitigating factors considered in the imposition of sanctions, while no losses and harm to clients' accounts made up 4% and 2% respectively. For example, in Dempsey, the Panel noted that the Respondent "did not earn commissions on the mutual fund switches set out" in the material facts of the case, "and therefore was not motivated by personal financial gain when making those recommendations" (IDA v. Dempsey, 2005: 42). Likewise in Graham, the Panel noted that "there was agreement that Mr. G. was not enriched" by his misconduct (IDA v. Graham, para. 26). In Blaker, the Panel "acknowledged...that the Respondent did not receive any financial benefit" from her acts (IDA v. Blaker, 2007: para. 21).

There were also cases when the hearing panels specifically mentioned that none of the clients had suffered any losses from the misconduct. In Cooney, the Panel noted...
that "[n]o client suffered any loss as a result of any of the" misconduct described in the material facts of the case (IDA v. Cooney, 2004: para. 38). In Holowatiuk, specific reference was made to the fact that "[t]here is no evidence of client losses, as a result of the Respondent's acts of forgery. Further, there is no evidence that the [R]espondent received any direct benefit from the forgeries" (IDA v. Holowatiuk, 2004: 15). In Deck, the Panel noted that "[a]part from the complaint from TO ..., there is no evidence of client complaints or of client losses from the activities of the Respondent leading to the agreed contraventions of the Association's [B]y-laws" (IDA v. Deck, 2007: para. 55).

The mitigating credits considered when no harm was inflicted on clients, were relatively straightforward. In Bell, the Panel noted that "[t]here was no malicious intent on the part of the Respondent, [and] no harm to clients resulted from the violations" (IDA v. Bell, 2005: para. 3). In Gordon, the Panel argued that "[they were] satisfied that there was no identified illegal insider trading...Therefore, there was no harm to clients of the Respondents and the integrity of the capital markets was not impaired" (IDA v. Gordon, 2006: para. 23). Similarly, in Furevick, the Panel wrote that "[t]he clients involved suffered no harm...There were no client complaints...[and] the respondent lost small amounts of money because the commission charges outweighed the small profits for the unauthorized trading" (IDA v. Furevick, 2007: para. 3).

A closer look at Figure 9-2 shows that reliance on the expertise of others (2%), and degree of participation (1%), only made up 3% of the mitigating factors considered in the imposition of penalties. In the few cases where the reliance on the expertise of others were considered as a mitigating factor, the Panel put a lot of weight on "whether a respondent demonstrated reasonable reliance on supervisory, legal or accounting advice that subsequent to the misconduct in question[,] was found to have been
erroneous" (IDA, 2006b: 10). For example, in *Gareau*, the Panel noted that "[t]he fact that Mr. G relied on Mr. Graham and was encouraged to do so by his employer [was] definitely a mitigating factor" (IDA v. Gareau, 2005: para. 68). In *Schillaci*, the Panel acknowledged that

> [t]he Respondent's Member firm did not adequately train him and did not provide policy[s] and procedure[s] to effectively supervise the Branch. The Respondent relied on senior people at the Member Firm who ultimately did not support him, which contributed to the misconduct in question. The Respondent was naive in relying upon his Member Firm for direction and not recognizing that the direction was inadequate (IDA v. Schillaci, 2007: para. 81).

In some cases, seeking competent legal advice was seen as a mitigating factor. For example, in *Michaels*, the Panel argued that "[t]here is no evidence that the Respondent sought advice from anyone, with the exception of his then counsel regarding the Association's second interview" (*IDA v. Michaels*, 2007: para. 26).

As mentioned earlier, the Respondents' "degree of participation" in the misconduct was rarely used as a mitigating factor. In cases where it was used however, the Panel considered the Respondent's diminished responsibility in the wrongdoing. In *Gareau*, the Panel noted that, "[a]lthough the Respondent was negligent, his responsibility [was] significantly diminished because of his reliance on his supervisor, SG" (*IDA v. Gareau*, 2005: para. 68). Similarly, in *Youden*, the Panel acknowledged that

> Mr. Y relied on the word and honesty of Mr. B when he should have, among other things, called the clients to confirm that the trading activity in their accounts was in accordance with their investment objectives and instructions. While this Panel found that such reliance was inappropriate in view of the many red flags in existence, it is clear that Mr. Y ha[d] a lesser level of complicity than Mr. B, who was a more direct perpetrator (*IDA v. Youden*, 2005: para. 118).

In *Schillaci*,
[t]he Panel...determined however that the Respondent did not act alone in the misconduct, that his head office had a responsibility to supervise him and not only failed to do so but failed to provide him with policy[ies] and procedure[s] to ensure [that] he [was] supervised effectively as [was] required. Further and through no fault of his own[,] the Respondent was unable to take the EMSI (which would have taught him his supervisory obligations) until much later after the misconduct [had] occurred. He sa[id], and we accept[ed], that he [was presently] much more knowledgeable...about his supervisory responsibilities (IDA v. Schillaci, 2007: para. 75).

Summary

When examining the aggravating factors identified and considered in the imposition of sanctions, failure to cooperate with the Association’s investigation stands out. Of the aggravating factors identified but not considered, multiple incidents of misconduct were more often ignored by the hearing panels in assessing appropriate penalties. When assessing the mitigating factors in penalty imposition, a lack of a prior disciplinary record was cited the most frequently to mitigate against harsher penalties.
Chapter 10: Conclusion and Policy Implications

This dissertation examined the sources and the flow of complaints through the IDA’s disciplinary system between 1984 and June of 2008. Analyses of the types of offences committed, penalties imposed on offenders, and the demographic characteristics of the victims, individual registrants, and Member firms were also carried out. The types and outcomes of appeals brought before the Commissions for review were then highlighted. In this chapter, I will discuss the findings and present recommendations to effectively address investors’ needs and safeguard the public interest in Canada. In order to do this, I will first revisit the misconduct funnel and discuss the corrective measures taken by the IDA to discipline its disobedient members.

The Misconduct Funnel Revisited

The first level of analysis in this dissertation utilized the data from the IDA’s Enforcement and Annual Reports. The Annual Reports’ data allowed me to employ the misconduct funnel developed by Brockman and McEwen (1990), and further refined by Brockman (2004), in order to examine the processing of initial complaints from individual registrants and Member firms to final dispositions. The major finding from the Annual Reports’ data is that while the IDA’s Case Assessment Group was able to process a significant number of complaints, the number shrank considerably as the complaints made their way through to the Investigation and Prosecution stages of the enforcement process.

The argument that SROs “funnel in” more complaints than the state cannot be ascertained because there is no basis upon which to compare this assertion. What is
known, however, is that with the addition of ComSet, the IDA was able to better position itself to scrutinize a wider variety of complaints, than it would have done otherwise. In reviewing these complaints, the IDA achieved greater inspectorial depth because the Case Assessment Group was able to look at more infractions with the existence of ComSet. The fact that the IDA looked at complaints that the state would not be interested in, is likely proof that the IDA does funnel in complaints. ComSet also allowed the IDA to streamline the reporting process and made it easier for Members to report complaints. Even though "the occurrence of attempted investment fraud is relatively common, very few Canadians actually report these attempts to the authorities" (CSA, 2007a: 4). The existence of another avenue for investors to report their complaints is therefore significant. As this study has shown, the top four complaints that the IDA’s Case Assessment Group was able to scrutinize over the six year period were unauthorized and discretionary trading, unsuitable investments, misrepresentation and service related issues.

The “funnelling out” of complaints at the Investigation and Prosecution stages implies that the IDA is “ineffective in controlling wayward” registrants (e.g., see Brockman, 2003: 55-56). The criticism that SROs are too lenient on their members and that they “funnel out” complaints from the system, was evident in the Investigation and Prosecution stages in the IDA’s enforcement process. The number of complaints opened shrunk significantly as they made their way from Case Assessment through to Investigation and Prosecution. The disposition of cases at the Investigation and Prosecution stages only allows for written reprimands - a penalty that is nothing more than a regulatory wrist slap. As such, the claim made by SROs that they set and impose higher standards than state regulators, is not substantiated in the IDA’s case. This sends
the wrong message to investors and investment professionals, and implies that the Association does not take these matters seriously.

Not only did the number of complaints shrink, but the nature of the complaints also changed as they made their way through to Investigation and Prosecution. Unauthorized and discretionary trading, unsuitable investments, along with issues related to supervision, inappropriate personal financial dealings, theft and fraudulent activities, forgery, manipulation and wash trading, conflict of interest, and capital deficiencies, were the most frequent types of complaints sent to Investigation and Prosecution. What is noticeable from this trend is that the top four complaints that made it through to Investigation and Prosecution were more serious in nature than the four top complaints that were initially dealt with by the Case Assessment Group.

There is also support for the claim that SROs’ function to deflect complaints with criminal elements away from the criminal justice system. As shown in this study, the findings from the cases that made their way to a hearing illustrated that the IDA was likely deflecting complaints with criminal elements away from the criminal justice system. Perhaps this is because the IDA was more interested in protecting its members, rather than fulfilling its legislative mandate to serve the public interest. This inherent conflict of interest raises questions on the effectiveness of SROs to be a part of the investors’ safety net in the securities industry. Some scholars even expressed concerns over whether SROs are working for the benefit of their members or serving the public interest as they so often claim to be (see Brockman, 1990: 3; Carson, 2011: 41). By having an SRO that is supposed to be in charge of safeguarding the investing public but, at the same time, deflects investors’ complaints away from the criminal justice system, is
tantamount to putting a fox to guard a henhouse (also see Rosen and Rosen, 2010: 28-35).

The IDA’s reluctance to send complaints with criminal elements to IMET, could very well indicate that they want to protect their members from possible criminal sanctions, and at the same time, “meet the contrasting needs of investors” (Rosen and Rosen, 2010: 197). Considering IMET’s track record, it is possible that the IDA is not confident enough that IMET will investigate and prosecute complaints that are referred to them. IMET’s lax enforcement of *Criminal Code* violations means that the burden to investigate and prosecute these complaints falls on the securities regulators. As such, it could be that the IDA has previous unsatisfactory responses when it referred matters to IMET. There is also the likelihood that the complaints, while containing criminal elements, were not egregious enough to justify sending them to IMET. Another problem may have to do with the beyond -a- reasonable-doubt standard needed to secure criminal convictions. There is no doubt that securities fraud is difficult to prosecute in criminal courts: the burden of proof is more onerous than in the administrative context, the defendants often have substantial legal resources, and it is also extraordinarily costly and time consuming to provide evidence to establish the evil intent – the *mens rea* – of the crime (Boyd, 2005: 35).

While the above constraints are duly noted, harsher sanctions are needed. For self-regulation to be effective, and be a part of the regulatory investors’ safety net in Canada, serious complaints dealing with criminal elements must be referred to the criminal justice system to be further investigated and prosecuted (see Pritchard, 2003: 38). One thing is for certain, the IDA cannot continue to deal with complaints that have criminal elements and then claim that they exist to serve the public interest.
A second level of analysis looks at the enforcement of complaints from the IDA’s cases. The data from the cases allowed for an analysis of the demographic characteristics of the victims, individual registrants, and Member firms involved in violating the IDA’s By-laws. The type of offences committed, penalties imposed on offenders, and the aggravating and mitigating factors considered in the imposition of penalties were also examined.

**Portrait of the Vulnerable Investor**

Even though victims of investment scams can be from all walks of life, the IDA study shows that scam artists target some of the most vulnerable people in society (also see FAIR Canada, 2011b: 21). The vulnerable investor in the IDA study can be described as someone who is interested in securing his or her financial future. Those most vulnerable are investors who are retired and have limited investment knowledge. Older Canadians (50+) are all too often the ones commonly victimized by securities breaches (also see BCSCn, 2012a). Their vulnerability is fueled by promises of high returns and low risks in investment schemes that lure them to invest in products they hardly know anything about. Brenda Leong, the Chair of the BCSCn noted that

> [w]hen you combine the fact that many older Canadians do [not] have a good grasp of what a realistic level of return is in the market with their lack of understanding about the relationship between risk and return, you have the perfect storm for con artists. This group is more vulnerable to promises of unrealistic returns, especially when the offer comes with the additional promise of no risk (BCSCn, 2012b: para. 3).

A considerable number of individuals who invested were those who experienced recent windfalls, dipped into their life savings and borrowed money in order to invest (also see FAIR Canada, 2011b: 21; Boyd, 2005: 36). The fear of not having enough money in their retirement years increases this vulnerability. The victims in this study were not
particularly wealthy, and approximately 66% of them earned less than $50,000 per year at the time of the investment. Roughly 22% of the victims incurred losses of $100,000 or more. Some of these victims include those who lost their entire life savings and in the process, ruined their retirement plans.

One commonality that a number of these investors shared is that they relied on the advice of people they trusted the most to secure their financial well being: family and friends. It does not seem to matter whether the individual is “[y]oung or old, rich or poor, financially literate or not, the power of trust transcends all barriers when it comes to the likelihood of falling victim to investment fraud” (BCSCn, 2012a: 3). Far from giving investors peace of mind, trusting these individuals without conducting due diligence on their backgrounds as investment advisors, seems to be the cardinal sin investors were committing when selecting a financial expert to manage their money. It should also be noted that in some cases, conducting due diligence may not be sufficient to ferret out the deviant advisor who preys on vulnerable investors.

The Most Common Offences

The most common types of offences committed by individual registrants were discretionary trading and unsuitable investments. Together, these two offences made up 27% of all offences committed by individual registrants. Discretionary trading results when registrants trade in their clients’ accounts without proper written authorizations to do so (IDA, 2006b: 32). Discretionary trading in clients’ accounts, “involve elements of deception in that the registrant is not completely open and honest as to the type of trading taking place within the client’s account” (p. 32). It is quite possible that this deception goes unnoticed because of an uninformed investing public who has no idea that their financial advisors are not allowed to trade in their accounts without prior written
approval. Or, it may be that clients did give verbal consent, but, such consent was either abused or misconstrued by their financial advisors to mean that they had full authority to engage in discretionary trading in their clients' accounts. Whatever the reason, “[w]hen taking an order from a client, advisors are prohibited from using their discretion to determine factors such as quantity, security, price or time…These decisions must come from the client” (IIROC, 2012: para. 8).

Financial advisors have a fiduciary duty to make sure that any recommendations that they make are suitable for their clients (IDA, 2006b: 27). These recommendations must be assessed “based on factors that include the client’s financial situation, investment knowledge, investment objectives and risk tolerance” (IIROC, 2012: para. 13). It is the job of the financial advisors to conduct their due diligence to make sure that the recommendations made for clients are in accordance with these stated criteria. The due diligence requirement puts the onus on the financial advisors to be judicious in their selection of investment products. However, the high proportion (13%) of suitability offences cast doubts on whether financial advisors are in fact conducting their background research when selecting suitable investments for their clients (see Goldin, 2010: 40).

Of utmost importance is the financial advisors’ ability to make decisions based on their professional judgment. “The issue with regard to suitability is not whether your financial advisor picked the right stocks, but whether your financial advisor picked the right investments in conformity with your investment objectives, investment horizons and risk tolerance levels” (Goldin, 2010: 227). Other concerns have to do with whether the financial advisors have their clients’ best interest in the investments they are recommending. All too often, financial advisors
who just want to make money for themselves try to acquire control over as much of an investor's portfolio as possible. Beneficiaries of an inheritance, or sellers of a family business, make ideal victims. Intimidated by investing such large sums, investors give authority to the [financial advisor] to make decisions on their behalf, within the limits of the investor's acceptable risk tolerance (Rosen and Rosen: 2010: 169).

In such cases, the advisor's desire to generate commission from the recommendation takes precedence over "product features and structure, ...risk, costs, and the management and financial strength of the issuer" (Goldin, 2010: 228).

**Enforcement of Securities Laws**

As mentioned earlier, financial losses incurred by the investors was the key factor taken into consideration when determining what constitutes harm. In other studies, the harm inflicted from investment fraud goes beyond financial loss. It affects the emotional well-being and physical health of the client (see Boyd, 2005: 28-29; CSA, 2007a: 1-2). Irrespective of the way harm is defined, it is important to pause and query whether the penalties imposed in administrative proceedings adequately reflect the harm caused to investors. More specifically, is a series of fines with conditions attached and permanent bans enough to address the harm caused from the financial advisor's misconduct? For example, a bank robber who holds up a bank and steals $100,000 in cash is appropriately punished by the justice system. A financial advisor, who misappropriates $100,000 from a few elderly clients, will probably enter a settlement agreement with the IDA and agree to a fine and a permanent ban from the Association. The financial advisor will most likely default on the fines imposed and quit the industry without any repercussions. While the bank officials, and those in close vicinity of the bank robbery will experience some initial psychological harm (assuming there is no casualty), the deliberateness of the bank robber's conduct and its "impact on the wider
community is often less significant” than the action of the financial advisor who swindled his elderly clients (see Boyd, 2005: 36).

For SROs to have any teeth and credibility in safeguarding the public interest, they must be able to enforce the penalties imposed on registrants. Fines imposed are quite often not collected. From 2002 to 2007, the IDA collected less than 50% of all of the fines imposed. One possible reason why fines are not paid is that the majority of the individuals (74%) that were found guilty were no longer registered with an IDA’s regulated Member firm. Also disconcerting is that individual registrants and Member firms were encouraged to enter into settlement agreements with the IDA Enforcement staff in exchange for a fine (and other conditions) that is at the low end of the spectrum. As discussed earlier, 67% of the cases were disposed of through settlement agreements. This is so, irrespective of whether the case deals with the more serious quasi-criminal type offences. This appearance of ineffective enforcement [only works] to undermines public confidence in the system...Unfortunately, whether justified or not, inadequate enforcement can create the perception that investor protection is not a top priority for securities regulators (FAIR Canada, 2011b: 24 and 26).

Furthermore, the IDA’s inability to collect fines coupled with “the laxity of sanctions imposed,..., [does] not send a sufficiently strong deterrence message to market participants or the [investing] public” that it can regulate with a big stick, and at the same time, protect investors (p. 26).

A third level of analysis deals with data from appeals to the securities commissions. There were two important findings from the appeals data: first, is that there were appeals from victims; and second, even though there were appeals from
financial advisors, they all dealt with jurisdictional issues and not reviews of the penalties imposed by the IDA. Although limited, the appeals from the victims illustrated their lack of satisfaction in dealing with the IDA. One victim laments his “lack of success in obtaining satisfaction” concerning his complaints from the IDA (*IDA v. Simpson*, 2005: para. 26). Perhaps more formidable is the claim made by another victim that the IDA’s “handling of …securities matter[s] has been far from responsible, appropriate or sufficient to uphold the public’s trust” (*IDA v. Ian Scott-Mancrieff*, 2001: para. 9).

The reason why there was no appeal from financial advisors to review the penalties imposed by the IDA is probably because it was not in their best interest to do so. As mentioned earlier, the IDA’s enforcement of complaints works in favour of its members. Penalties imposed are often seen as inadequate and are not proportionate to the offence. This coupled with the fact that financial advisors were encouraged to enter into settlement agreements in exchange for penalties that were on the lower end of the spectrum, explains why there were no appeals for reviews of the penalties imposed by the IDA.

A fourth level of analysis is more qualitative in nature and looks at the aggravating and mitigating factors identified by the IDA’s hearing panels in the imposition of penalties. What stands out in the qualitative analysis is that the IDA’s hearing panels were more likely to identify mitigating rather than aggravating factors when considering the appropriate penalties to be imposed on registrants. Perhaps this was because the hearing panels were more preoccupied with identifying mitigating factors that would in turn lead to less severe penalties for their members. It is also worth pointing out that the aggravating factors identified and considered were fewer in number than the aggravating factors identified but not considered by the hearing panels when
imposing penalties. One plausible explanation for this outcome was that in cases where aggravating factors were identified and considered, they were more serious and transparent in nature, and as such, the hearing panels had no other options but to consider them when determining penalties. It could also well be that the hearing panels were involved in scapegoating, and only identified and considered aggravating factors against specific players such as advisors from the smaller firms or the smaller firms themselves to justify harsher penalties.¹¹⁴

Overall, the results of the IDA’s enforcement of complaints do not support a claim that the IDA has a vested interest in protecting investors from unscrupulous financial advisors. The findings indicate that when the interest of the public clashes with the interests of the IDA’s members, the IDA puts its members first (e.g., see Rosen and Rosen, 2010: 30). The IDA’s “responsibility to the public gets downplayed, or eliminated, with no safeguard in place to prevent this from happening” (p. 30). The argument that the IDA gets morphed into serving its members may be attributed to the IDA being more interested in protecting the reputation of the securities industry. Another reason is that the IDA’s staff probably has close connections with industry professionals, who put pressure on them to function in the best interest of its members and the industry, rather than the investing public. Industry financing may also be another factor that works to divert the IDA from imposing adequate sanctions. As farfetched as it may sound, there is also the possibility that some IDA staff expect to be employed with the more affluent Member firms after their stint with the IDA. Some staff for example, may not want their careers to be tied to the IDA, while others are probably promised higher salaries and

¹¹⁴ There is anecdotal evidence which posits that the IDA goes after the smaller firms and their players and rarely ever goes after the larger bank owned firms and their financial advisors.
career mobility by some of the IDA’s regulated Member firms. All of the above works to reduce the incentive to impose adequate penalties.

The IDA/IIROC

While the findings from this study are from the enforcement of complaints by the IDA, they also have implications for its replacement, IIROC. The key tasks for IIROC is not only to successfully integrate the regulatory functions of the IDA, but to ensure that it takes the appropriate measures to improve upon the IDA’s enforcement record. The objective is for IIROC to identify specific areas where the IDA (hereinafter IIROC) were lacking and address them with the Enforcement department. This is important because in order to ward off government intervention and the possibility of more-restrictive regulation, IIROC must step up the ante and hold individual registrants and Member firms accountable for their misconduct. Public accountability can only be achieved if IIROC aligns its interests with that of the public. One way to achieve this outcome in the securities industry is through the negotiation and imposition of adequate penalties between IIROC and its registrants.

Recommendations for Effective Self-Regulation in the Securities Industry

Recommendation: Focus on Deterrence

As a starting point, IIROC must seek to ensure that penalties negotiated and imposed on registrants have a deterrent effect. For penalties to have a deterrent effect, their fundamental purpose must be “both a specific, [and]...more importantly a general deterrent” (IDA v. Armstrong, 2003: 36; IDA v. Fee, 2002: para. 5). The intention of the IDA in achieving these outcomes is reflected in the following decisions. In Strocen, “the
District Council has focused on deterrence as one of the major elements in determining an appropriate penalty” (IDA v. Strocen, 2002: para. 62). Similarly in Betnar, the Panel notes that “the amount and type of the penalty assessed should be sufficient in the circumstance to clearly act as a deterrent to other parties who might be tempted to breach Association [B]y-laws” (IDA v. Betnar, 2003: 49).

While the intentions of the IDA are clear, IIROC cannot continue to apply penalties on “a few bad apples” in order to give the impression that the system is working (e.g., see Jackson and Gkantinis, 2007: 1255). These targeted decisions “often fail to reveal weaknesses or prosecute wide-spread practices in the underlying system…” (p. 1255). In Creditfinance Securities Limited, the

Hearing Panel concluded that the purpose of a penalty is to protect the integrity of the self regulatory system and to ensure that its operations are carried out effectively; a penalty must be designed to carry out that purpose by deterring the offender from repetition of the …conduct and by deterring others (IDA v. Creditfinance Securities Limited, 2006: para. 6).

In order to meet these objectives, IIROC must vigorously pursue and prosecute their members so that the penalties imposed are proportionate to their misconduct.

**Recommendation: Focus on Fine Collection**

Policies must be put in place to enable the Association to collect fines imposed on registrants. One way to address the problem of unpaid fines is to empower IIROC with the statutory authority to go after individuals who do not pay their fines. Leading the charge for this policy change is FAIR Canada who

... calls on the rest of the Canadian jurisdictions [to follow Alberta and]... extend the statutory fine collection power to Canada's SROs to increase the efficiency and effectiveness of their enforcement efforts. This would increase the likelihood of the payment of penalties and enhance the
credibility of self-regulation, which would contribute to improved credibility of the overall securities regulatory system (FAIR Canada, 2011a: 7).\textsuperscript{115}

To prevent individual registrants with unpaid fines from working in the insurance industry,

FAIR Canada calls on regulators to enhance the sharing of disciplinary and investigative information between the insurance and securities regulators and promptly act on disciplinary action by other regulators so that individuals who have been found to be dishonest or lacking in integrity cannot simply move from one platform to another or continue to deal with clients under their other license (para. 7).

IIROC must also be accountable to the public and make transparent in their annual financial statements, all of the fines collected from individual registrants and Member firms. Instead of stashing away fines collected in IIROC’s coffers, the money should be used to assist victims who have not been compensated to recover their losses.\textsuperscript{116}

\textit{Recommendation: Focus on Margin Requirements}

As mentioned earlier, margin accounts made up 41% of all the accounts opened by investors in this study. Given that the incentives are there for both investment advisors and Member firms to open margin accounts for their clients, there must be some sort of checks and balances put in place by SROs in charge of securities

\textsuperscript{115} The \textit{Securities Act} in Alberta “provides SROs with the power to enforce their decisions as though they are court judgments” (FAIR Canada, 2011: para. 6).

\textsuperscript{116} The fines collected from members are stored in an “Externally Restricted Fund” account (see IIROC, 2010c: 29). IIROC claims that “the Externally Restricted Fund is the net of revenue from fines and interest and expenses incurred for the following purposes in accordance with the terms and conditions of respective provincial Securities Commissions: (i) [n]on-recurring capital expenditures to address emerging regulatory issues arising from changing market conditions, and are directly related to investor protection and capital markets integrity; (ii) [e]ducation of market participants and the public about or research into investing, financial matters or the operation or regulation of securities markets; (iii) [d]onations to non-profit, tax exempt organizations for investor protection and education; and (iv) [c]osts associated with the administration of IIROC’s Hearing Panels”(p. 29).
regulation to monitor the opening of margin accounts. One way to accomplish this objective is for IIROC to set prescriptive rules that must be met before margin accounts can be opened. Central to these rules is the “presumption that leverage is unsuitable for retail investors, and thus place the onus on salespeople to prove that leverage is in fact suitable and that the client understands the risks” (FAIR Canada, 2011c: 5). These rules should not only be based on investors’ liquid net worth, but must place increased emphasis on investors’ risk tolerance levels, investment objectives, purpose, knowledge, and age to determine if they are suitable candidates for the risks involved in opening and trading in margin accounts. The onus should be on the investment advisor to “make sure that [the client’s] financial position is such that [he or she has] a ready supply of money to meet any margin call, if and when it is made” (Goldin, 2010: 46).

IIROC must make it mandatory for investment advisors to fully disclose all commissions earned from margin trading. This point is endorsed by FAIR Canada which recommends that, at any time the use of leverage is recommended to a client, intermediaries be obligated to disclose the amount of additional commissions and other remuneration that they (and any other related entity) would be paid as a result of the leverage. This requirement should be in addition to the full disclosure of commissions and other remuneration from the investment products recommended (FAIR Canada, 2011c: 5).

To complete the process, there should be a certification requirement, which would oblige Approved Persons to certify, at the time of a leverage recommendation, that they have explained the risks associated with leverage to the client and certify their belief that the client understands the associated risks. The client would acknowledge that the risks have been explained and are understood (p. 1).
More emphasis should be placed on holding Branch Managers and Officers accountable for the opening of margin accounts under their supervision. For a start, Branch Managers who sign off on Margin Agreements without checking to verify the suitability of the client must be held accountable by IIROC. The Chief Compliance Officer of the Member firm should also verify that the requirements set by IIROC are complied with and he/she will be held accountable if he or she fails to do so. For clients who have “sufficient tolerance for risk to take on a particular amount of leverage” in their accounts, there should be a clause, which stipulates that margin calls should only be satisfied once they are “notified and given a reasonable time to meet such margin call from [their] cash resources, before [they] are sold out” (FAIR Canada, 2011c: 5; Goldin, 2010: 46).

**Recommendation: Focus on Suitability Requirements**

To address suitability offences, IIROC must pass rules to deal with the following issues. More responsibility should be placed on Member firms to carefully review the securities offered to investors. At present, the CSA expect[s] brokerage houses to have a process for reviewing and approving new products and existing products whose structure or features have significantly changed. However if a product is on the firm’s “approved list”, it does not mean that it will be suitable for all clients. Individual registrants (i.e. financial advisors and brokerage houses) must still determine suitability of each proposed transaction for each client (Goldin, 2010: 98).

This discretion given to financial advisors and brokerage firms must be more firmly regulated. One approach is to make sure that any orders “recommended by the financial advisor as well as … orders proposed by the client,” go through a formal review process (see Goldin p. 102). The financial advisor should first conduct a suitability analysis of the product. Before determining suitability, the financial advisor should then review the
investor’s profile to make sure that there is no material change in relations to his or her risk tolerance level, investment objective, income, investment knowledge, and needs (also see Goldin, p. 88).

Canadians are increasingly relying on financial advisors who are not fully knowledgeable about the investment industry for investment advice (Branef, 2008: para. 13). These individuals only have to write and pass some industry related courses to be approved as a financial advisor with an IIROC’s regulated firm.117

Regulators register these people as “sales representatives” while the industry provides them with titles of “financial consultant” or “investment advisor.” To the unwary it creates the impression that investors are assured of receiving competent, objective advice rather than just buying a product (para. 13).

These “financial consultants” do not need any “prior educational qualifications before studying for these courses… Anyone who passes [these industry related] examination[s] can become registered as a broker” (Goldin, 2010: 27). Passing industry related exams does not give one the expertise to read and understand complex financial instruments. As such, once the financial advisor has carefully researched the product and reviewed the investor’s profile, the documents should be turned over to an evaluator with the appropriate education and industry expertise employed by the Member firm for further review.

IIROC must ensure that the Member firm has qualified individuals “to perform their own analysis” on securities before offering them to investors (see Goldin, 2010: 98). IIROC must also be very specific about the type of qualifications needed to be employed.

117 These courses included, but, are not limited to the Partners, Directors and Senior Officers Courses, the Canadian Options Course, the Canadian Securities Course, and the Conduct and Practices Handbook Course.
as the Member firm’s designated securities’ evaluator. Individual(s) approving securities for the Member firm, must have either an advance accounting or finance designation and relevant industry expertise to be classified as an expert in evaluating securities. It should be made very clear by IIROC that the expert evaluator, financial advisor, and Member firm will all be held accountable for giving the green light to securities with red flags attached to them.

**Recommendation: Focus on the Authorization to open Discretionary Accounts**

IIROC must focus its attention on the authorization to trade in discretionary accounts. In addition to written authorization, the conventional norm in the industry is for clients to give verbal authority to their financial advisors “to engage in discretionary trading” in their accounts, “without the proper written documentation” (IDA, 2006b: 32). To address this problem, Goldin suggests that IIROC should get rid of verbal consent and implement a rule that will require all accounts classified as discretionary, to be given written approval (2010: 45, 96-97). In other words, registrants should not be allowed to trade in their clients’ account unless the accounts are officially designated as discretionary. For an account to be officially designated as discretionary, the following criteria must be met. First, financial advisors and Branch Managers must make sure that investors understand the risk associated with discretionary accounts. Second, Branch Managers must certify in writing that all matters pertaining to discretionary trading is explained to investors by the financial advisors in plain language. Third, Member firms must “approve, supervise, review, and record all discretionary… accounts to ensure that they are administered properly and in accordance with investors’ instructions” (Goldin, 2010: 80 emphasis added).
At present, all accounts classified as discretionary “must be renewed in writing every year” (Goldin, 2010: 45). This sort of arrangement “can give an unscrupulous broker an easy opportunity to churn [an investor’s] account” (p. 45). To prevent this from happening, Goldin (2010) suggests that IIROC should make sure that Branch Managers “review at least monthly[,] the financial performance of each discretionary account, …including a review to determine whether any person permitted to effect any discretionary trades should continue to do so” (p. 96). The Branch Manager conducting the review must have up-to-date “Know Your Client” information of the investor (see p. 6). It should also be made mandatory that all accounts classified as discretionary be renewed in writing, every three months. Moreover, discretionary accounts should only be handled by experienced and qualified financial advisors with proven track records who have never been implicated in any offences (see pp.96-97).

**Recommendation: Focus on Greater Transparency and Disclosure Requirements**

Other areas that need specific attention relate to the investment advisors themselves. To effectively serve and safeguard the public interest, IIROC “should require advisors to disclose to new and existing clients any proven complaints of unsuitability and other abusive sales practices” (Condon and Puri: 2006: 9). Rules must be implemented that will “require advisors to disclose proven claims of unsuitable investments and other abusive sales practices to new and existing clients (p. 9). To build on these recommendations, IIROC should make it mandatory for financial advisors to disclose any product created by the Member firm, and more importantly, products from business acquaintances that the advisors are closely associated with.
Recommendation: Focus on Investors’ Education

One of the more significant findings of this study is that the majority (62%) of investors had limited investment knowledge. To address this problem, IIROC must focus on investors’ education as part of its gatekeeper’s mandate. Not just random seminars on fraud prevention, but, seminars that target vulnerable groups (also see Boyd, 2005: 35-37). A one size fits all approach will not “account for the significant difference between victim types” (Shadel, 2009: 4). For example, elderly men and women in their late 70s may need seminars on fraud awareness, while men and women in their 40s may need seminars that warn them about the lure of higher returns (also see Shadel, 2009: 4). As such, the focus should be on seminars that are specifically tailored for different subset of people. A special effort should be made to target retired seniors, individuals with funds to invest, and those with “limited financial literacy” (see Heminway, 2009: 307). IIROC should also target individuals who are more prone to be victims of affinity fraud.

Affinity fraud is a type of scam that targets groups such as religious groups, seniors’ groups, ethnic communities or social clubs. The scam artist may be a member of the group or may know someone in the group. These scams are often successful because many people are less likely to question advice that comes from someone they know (CSA, 2011: 4; also see FAIR Canada, 2011b: 21-22)

Investors’ education should be in the form of a major public campaign designed to reach out to and educate these vulnerable groups (see FAIR Canada, 2011b: 34). The goal of the campaign should be to equip vulnerable groups with the necessary tools to detect and avoid financial fraud. The campaign should include advertisements or notices in publications
targeting the elderly, ethnic groups (in various languages), religious
groups, [and] reaching out to organizations representing [other]
vulnerable groups (p. 34).

To gain access to these vulnerable groups, IIROC can join forces with various ethnic
communities, religious organizations, seniors’ groups (such as the Canadian Association
of Retired Persons (CARP), clubs, local governments of small towns, where retirees may
be sitting on large amount of cash, and other governing bodies that represent vulnerable
individuals. Innovative strategies can be developed such as the “God’s Fraud Squad"
initiative taken by the BCSC, who teamed up with “two Fraser Valley pastors, to
prevent and disrupt cases of investor fraud in faith-based communities” (see FAIR
Canada, 2011b: 34). Similar approaches to gain access to other vulnerable groups
can be developed with priests from other faiths, community leaders, and club presidents.

Another key component of IIROC’s education mandate is to inform investors to
keep an eye out for people they trust the most and who work in the investment industry.
These trusted individuals can be a family member or a friend. As mentioned earlier, 40%
of investors were swindled by a family member and 23% by a friend. Part of IIROC’s
mandate should aim to educate prospective investors to be wary of individuals who can
exploit this existing trust and convince them to invest in one of their schemes. This is
particularly important, because in some cultures, reporting a family member to regulatory

118 In 2011, the BCSCn “launched the first phase of a three-year television, radio and print
campaign to educate and warn British Columbians about the dangers of investment fraud”
(BCSC, 2011b: para. 1). The campaign specifically focuses on the Chinese and South Asian
communities and “include television in Mandarin, Cantonese and Punjabi and radio in Punjabi,
Hindi, Urdu, Cantonese and Mandarin, supplemented with full and half page ads” (para. 5).
119 Some of the other BCSCn’s educational programs are InvestRight, Be Fraud Aware, and
Planning 10. InvestRight is a website specifically designed to provide investors with the tools to
research, educate, and protect themselves from fraudulent investments (see BCSC, 2006: para.
1-3). Be Fraud Aware is a three year program designed to raise awareness on the warning signs
of investment fraud in British Columbia (see BCSC, 2011b: para 1). “Planning 10 is a
mandatory Grade 10 course in British Columbia… designed to give young people the financial life
skills they [will] need as adults” (BCSC, 2011c: para. 1).
authorities is frowned upon. It is not uncommon for victims from tight-knit ethnic communities to accept their losses, because they are afraid of the repercussions from family members if they report the perpetrator to the authorities. The same can also be said for individuals from religious organizations and clubs, who may feel ashamed to make public their loss.

The content of investors’ education should focus on the specific issues that investors should ask their financial advisors and brokerage firms before investing. Special consideration should be given to the advisor’s disciplinary record, qualifications, industry experience, personality and attitude towards prospective investors. As a starting point, see Goldin for the “Eleven Key Questions to Ask When Choosing A Broker” (2010: 27-34). IIROC should also “make reference to the dangers of promises of unrealistic returns and guaranteed consistent returns[,] and how they are often a red flag for fraud” (FAIR Canada, 2011b: 34). Increased emphasis should be placed on “educat[ing] investors about market risks and losses and the appropriate bearing of responsibility when an investment has negative returns” (Condon and Puri, 2006: 25). More importantly,

... be given [that requires] financial advisors to specifically disclose the risk[s] associated with entering into a particular transaction before the transaction is entered into, and its effect on the client’s overall portfolio in terms of risk, return and diversification (p. 25).

At the very least, investors should be advised to be extra cautious of investment advisors who try to persuade them to invest in financial products that their business acquaintances are associated with (e.g., see Stromberg, 2002: para.18). The goal should be to educate the individual to become an informed and skeptical investor.
IIROC should start with the assumption that prospective investors have limited financial literacy. Similar to the manner in which English and Mathematics are taught in elementary school, IIROC’s public campaign should start by teaching basic investment and financial literacy skills to investors. Part of IIROC’s investment education mandate should be to encourage investors to invest with financial advisors and Member firms that are registered with IIROC (FAIR Canada, 2011b: 34). Resources should be dedicated to teach investors how to find out the registration status of their financial advisors and Member firms, and more importantly, the process to follow in order to register a complaint (see FAIR Canada, 2011b: 13-14). Anecdotal evidence indicates that there are investors who do not even know that IIROC exists, much less the process of registering a complaint. Some may have heard about the Association in name only, and are oblivious of its purpose. Finally, investors should be encouraged to invest with IIROC’s regulated firms that are backed by a compensation fund (p. 34).

**Recommendation: Focus on Attracting Female Financial Advisors**

Less synonymous with the other recommendations, but worth contemplating, is the need for more women investment advisors to join the industry (see RBC Dominion Securities, 2008: para.1-2). As was mentioned earlier, 9% of the offenders were female. At the same time, women made up 39% of the victims between 1986 and 1997, and 46% of the victims between 1998 and June of 2008. The increasing number of female investors is partly because they are taking control of their own finances, and also have responsibility for household budgeting (e.g., see TD Waterhouse: 2006: para. 5; RBC Dominion Securities, 2008; 6; Heminway, 2009: 310 ). “Yet, the majority of women still

---

120 In British Columbia for example, the “Chinese and South Asian communities…represent 40% and 26%, respectively, of BC’s visible minority population” but “have a low awareness of the BCSC” (BCSCn, 2011b: para.1).
feel under-served and disenfranchised from the financial services industry” (Raymond James, 2011: para.1). To address these concerns, there have been calls for more female investment advisors to join the investment industry (RBC Dominion Securities, 2008: para. 1).

This call can be partly attributed to the fact that females exhibit traits that can make them effective financial planners (see Merrill Lynch Investment Managers, 2005; Heminway, 2009). When it comes to investing, women generally seek more investment advice and conduct more research than men (Merrill Lynch Investment Managers, 2005: 1; Barrett, 2007: para. 9; Heminway, 2009: 311). Women are also “more risk averse in their investment behaviour than men” (Heminway, 2009: 311). There is also the argument that

female investors may be less optimistic and less overconfident than their male counterparts. In addition, female investors typically perceive themselves as lacking in investment competence more than male investors (Heminway, 2009: 313; also see Merrill Lynch Investment Managers, 2005: 5-7).

The perceived lack of confidence and investment competence by female investors, results in them trading “less frequently than men” (Heminway, 2009: 315).

Female financial advisors would likely recommend more conservative portfolio for their clients. In a study done on mutual fund managers, Niessen and Ruenzi found “that female fund managers are more risk averse than male fund managers” (2007: 29). Heminway attributed this variation “in part to sex-based differences in unsystematic risk” (2008: 318). Perhaps because

[f]emale fund managers follow significantly less extreme investment styles as compared to male fund managers. Furthermore, female managers’ investment styles are more stable over time… male managers
trade more, which is reflected in a significantly higher turnover rate of male managed funds as compared to that of female managed funds (Niessen and Ruenzi, 2008: 29).

Greater overconfidence in male investment decisions is blamed for the higher turnover rate of portfolios (Barber and Odean, 2001: 275; Heminway, 2008: 320-321). These traits make “women…well-positioned” as ideal candidates “to capitalize on their expertise in this area” (RBC Dominion Securities, 2008: para. 2). The call for more female financial professionals then is not because they will perform better or will be less likely to swindle their clients’ accounts than their male counterparts; but, maybe there would be less fraud with more women to influence the investment culture.

Some Final Thoughts and Future Directions

This dissertation set out to examine the patterns and trends of the IDA’s enforcement of complaints. The findings indicate that the IDA is ineffective in collecting fines imposed. This coupled with the laxity of accompanying sanctions, is often inadequate to punish wayward registrants.\textsuperscript{121} The lack of adequate enforcement creates a perception that the IDA is not serious about prosecuting securities violations and protecting investors from unscrupulous financial advisors (also see FAIR Canada, 2011b: 26). This problem was echoed by victims like Chris Morgis, who at the starting of this dissertation, noted that he was “disappointed” with the IDA’s handling of his complaint. Morgis expressed concerns about the Association’s reluctance to put its members in a situation where they could face possible criminal charges. In order for IIROC to be efficient in the enforcement of complaints, it must address these concerns. As a starting point, IIROC can use the findings from the present study to inform its policy.

\textsuperscript{121} Also see FAIR Canada (2011b: 26).
making agenda, and effectively fulfill its investors’ protection mandate to serve the public interest.
References


239


243


Cases Cited

Investment Dealers Association of Canada v. Dass, 2007 BCSECCOM 262
Appendix A: The IDA Sanction Guidelines
1. QUASI-CRIMINAL OFFENCES
1.1 Fraud: Association By-law 29.1
1.2 Forgery: Association By-law 29.1
1.3 False Endorsement of Regulatory Documents: Association By-law 29.1
1.4 Misappropriation of Funds: Association By-law 29.1
1.5 Securities Act breach or breach of any related Provincial or Federal Legislation --Association By-law 29.1

2. CONFLICT OF INTEREST
2.1 Unauthorized or Improper Use of Inside Information – By-law 29.1
2.2 Unauthorized or Improper Disclosure and/or Use of Client Information – Bylaw 29.1
2.3 Undisclosed/Unauthorized Accounts – By-law 29.1
2.4 Undisclosed Personal Business – By-law 29.1
2.5 Undisclosed Personal Business with a Client (includes borrowing from a client without firm knowledge or consent) – By-law 29.1
2.6 Attempt to Settle Client Claim for Compensation – By-law 29.1
2.7 Failure to ensure Client Orders are given Priority – Regulation 1300.17, Bylaw 29.1

3. IMPROPER SALES PRACTICE
3.1 Unsuitable Recommendations - Regulation 1300.1(a)
3.2 Failure to Know Your Client - Regulation 1300.1(a) and (b)
3.3 Failure to Update NAAF - Regulation 1300.1(a); By-law 29.1
3.4 Order not within Bounds of Good Business Practice - Regulation 1300.1(o)
3.5 Churning – By-law 29.1 and Regulation 1300.1(o)
3.6 Discretionary Trading – Regulations 1300.4 & 1300.5
3.7 Unauthorized Trading – By-law 29.1
3.8 Unauthorized Distribution of Sales Literature – By-law 29.7
3.9 Unauthorized Third Party Instructions – Regulation 200.1(i) (3)
3.10 Outside Business Activities – By-law 29.1

4. INTERNAL CONTROL OFFENCES
4.1 Capital deficiencies– By-law 17.1
4.2 Failure to Establish and/or Maintain Adequate Internal Controls – By-law 17.2A
4.3 Failure to Supervise – Regulation 1300.2, Policy 2, and By-law 29.27
4.4 Fail to obtain and Maintain Minimum Required Margin –Bylaw 17.13
4.5 Record Keeping Violations – By-law 17.2 Regulation 200

5. Cooperation, Membership and Misrepresentation
5.1 Failure to Cooperate – By-laws 19.5 and 19.6
5.2 Misrepresenting Credentials to Association upon Registration/Transfer
5.3 Allowing an Unregistered Person to Trade
5.4 Conducting Business While Suspended
5.5 Misrepresentations
Appendix B: Codebook
<table>
<thead>
<tr>
<th>Investors' Variables</th>
<th>Value</th>
<th>Label</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable name</td>
<td></td>
<td>Label</td>
</tr>
<tr>
<td>Investors' Gender</td>
<td>1</td>
<td>Male</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Female</td>
</tr>
<tr>
<td>Investors' age</td>
<td>1</td>
<td>0-45</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>46-54</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>55-64</td>
</tr>
<tr>
<td></td>
<td>4</td>
<td>65+</td>
</tr>
<tr>
<td>Investment Purpose</td>
<td>1</td>
<td>Fund future retirement</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Enhance current lifestyle</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>Income for basic needs</td>
</tr>
<tr>
<td></td>
<td>4</td>
<td>For children/grandchildren</td>
</tr>
<tr>
<td></td>
<td>5</td>
<td>Extra income</td>
</tr>
<tr>
<td></td>
<td>6</td>
<td>Diversify investment portfolio</td>
</tr>
<tr>
<td></td>
<td>7</td>
<td>Higher rate of return than other investment</td>
</tr>
<tr>
<td></td>
<td>8</td>
<td>Trust Funds</td>
</tr>
<tr>
<td></td>
<td>9</td>
<td>Purchase Property</td>
</tr>
<tr>
<td></td>
<td>10</td>
<td>Other</td>
</tr>
<tr>
<td>Sources of investment</td>
<td>1</td>
<td>Savings</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Retirement savings (money from RRSP)</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>Cash in other investment</td>
</tr>
<tr>
<td></td>
<td>4</td>
<td>Borrowed funds</td>
</tr>
<tr>
<td></td>
<td>5</td>
<td>Mortgage primary residence</td>
</tr>
<tr>
<td></td>
<td>6</td>
<td>Recent windfall and Inheritance</td>
</tr>
<tr>
<td></td>
<td>7</td>
<td>Sold Property</td>
</tr>
<tr>
<td></td>
<td>8</td>
<td>Mortgage other property</td>
</tr>
<tr>
<td></td>
<td>9</td>
<td>Other</td>
</tr>
<tr>
<td>Investment Objectives</td>
<td>1</td>
<td>Income</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Long-term growth</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>Short-term growth</td>
</tr>
<tr>
<td></td>
<td>4</td>
<td>Speculative</td>
</tr>
</tbody>
</table>

261
<table>
<thead>
<tr>
<th>Investors’ Variables</th>
<th>Value</th>
<th>Label</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable name</td>
<td></td>
<td>Label</td>
</tr>
<tr>
<td>Investors’ occupations</td>
<td>1</td>
<td>Management Occupations</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Business, Finance and Administrative Occupations</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>Natural and Applied Sciences and Related Occupations</td>
</tr>
<tr>
<td></td>
<td>4</td>
<td>Health Occupations</td>
</tr>
<tr>
<td></td>
<td>5</td>
<td>Social Science, Education, Government Service and Religion</td>
</tr>
<tr>
<td></td>
<td>6</td>
<td>Occupations in Art, Culture, Recreation and Sport</td>
</tr>
<tr>
<td></td>
<td>7</td>
<td>Sales and Service Occupations</td>
</tr>
<tr>
<td></td>
<td>8</td>
<td>Trades, Transport and Equipment Operators and Related Occupations</td>
</tr>
<tr>
<td></td>
<td>9</td>
<td>Occupations Unique to Primary Industry</td>
</tr>
<tr>
<td></td>
<td>10</td>
<td>Occupations Unique to Processing, Manufacturing and Utilities</td>
</tr>
<tr>
<td></td>
<td>11</td>
<td>Self-employed</td>
</tr>
<tr>
<td></td>
<td>12</td>
<td>Unemployed</td>
</tr>
<tr>
<td></td>
<td>13</td>
<td>Retired</td>
</tr>
<tr>
<td>Relations to client</td>
<td>1</td>
<td>Family member</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Friend</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>Acquaintance</td>
</tr>
<tr>
<td>Investor investment knowledge</td>
<td>1</td>
<td>Limited</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Average</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>Sophisticated</td>
</tr>
<tr>
<td>Investors’ account type</td>
<td>1</td>
<td>Cash</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Margin</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>RRSP</td>
</tr>
<tr>
<td></td>
<td>4</td>
<td>RRIF</td>
</tr>
<tr>
<td>Investors’ annual income</td>
<td>1</td>
<td>Under $25,000</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>$25,000 to under $50,000</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>$50,000 to under $75,000</td>
</tr>
<tr>
<td>Investors’ Variables</td>
<td>Value</td>
<td>Label</td>
</tr>
<tr>
<td>----------------------</td>
<td>-------</td>
<td>------------------------------------</td>
</tr>
<tr>
<td>Variable name</td>
<td>4</td>
<td>$75,000 to under $100,000</td>
</tr>
<tr>
<td></td>
<td>5</td>
<td>$100,000 to under $150,000</td>
</tr>
<tr>
<td></td>
<td>6</td>
<td>$150,000 to under $200,000</td>
</tr>
<tr>
<td></td>
<td>7</td>
<td>$200,000 and over</td>
</tr>
<tr>
<td></td>
<td>8</td>
<td>DK/NA</td>
</tr>
</tbody>
</table>

| Investor' net worth  | 1     | Under $25,000                     |
|                      | 2     | $25,000 to under $50,000          |
|                      | 3     | $50,000 to under $100,000         |
|                      | 4     | $100,000 to under $150,000        |
|                      | 5     | $150,000 to under $250,000        |
|                      | 6     | $250,000 and over                 |
|                      | 7     | DK/NA                             |

| Investors' losses    | 1     | Under $25,000                     |
|                      | 2     | $25,000 to under $50,000          |
|                      | 3     | $50,000 to under $75,000          |
|                      | 4     | $75,000 to under $100,000         |
|                      | 5     | $100,000 to under $150,000        |
|                      | 6     | $150,000 to under $200,000        |
|                      | 7     | $200,000 and over                 |
|                      | 8     | DK/NA                             |

| Individual Offender and Member Firm’s Variables | Firm type | 1 | Integrated |
|                                               | 2 | Retail |
|                                               | 3 | Retail type 1 and 2 introducers |
|                                               | 4 | Managed accounts |
|                                               | 5 | Discount brokers |
|                                               | 6 | Institutional |
|                                               | 7 | Corporate finance |
|                                               | 8 | Alternative trading system |

<p>| District council | 1 | Alberta Northwest Territories |
|                 | 2 | Manitoba and Nunavut |
|                 | 3 | New Brunswick |
|                 | 4 | Newfoundland |
|                 | 5 | Nova Scotia |</p>
<table>
<thead>
<tr>
<th>Variable name</th>
<th>Value</th>
<th>Label</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ontario</td>
<td>6</td>
<td>Ontario</td>
</tr>
<tr>
<td>Pacific</td>
<td>7</td>
<td>Pacific</td>
</tr>
<tr>
<td>Prince Edward Island</td>
<td>8</td>
<td>Prince Edward Island</td>
</tr>
<tr>
<td>Quebec</td>
<td>9</td>
<td>Quebec</td>
</tr>
<tr>
<td>Saskatchewan</td>
<td>10</td>
<td>Saskatchewan</td>
</tr>
<tr>
<td>Offender experience</td>
<td>1</td>
<td>0-5 years</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>6-10 years</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>11-15 years</td>
</tr>
<tr>
<td></td>
<td>4</td>
<td>16-20 years</td>
</tr>
<tr>
<td></td>
<td>5</td>
<td>21-25 years</td>
</tr>
<tr>
<td></td>
<td>6</td>
<td>26-30 years</td>
</tr>
<tr>
<td></td>
<td>7</td>
<td>31-35 years</td>
</tr>
<tr>
<td></td>
<td>8</td>
<td>36-40 years</td>
</tr>
<tr>
<td>Offender offending status</td>
<td>1</td>
<td>First time offender</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Repeat offender</td>
</tr>
<tr>
<td>Type of offender</td>
<td>1</td>
<td>Individual member</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Member firm</td>
</tr>
<tr>
<td>Type of hearing</td>
<td>1</td>
<td>Settlement</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Contested</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>Expedited</td>
</tr>
<tr>
<td>Offender occupation</td>
<td>1</td>
<td>Registered representatives</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Branch managers</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>Officers</td>
</tr>
<tr>
<td>Offender gender</td>
<td>0</td>
<td>Female</td>
</tr>
<tr>
<td></td>
<td>1</td>
<td>Male</td>
</tr>
<tr>
<td>Number of Cases by Year</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Period 1</td>
<td>1</td>
<td>1984-1993</td>
</tr>
<tr>
<td>Period 2</td>
<td>2</td>
<td>1994-2003</td>
</tr>
<tr>
<td>Period 3</td>
<td>3</td>
<td>2003-2008</td>
</tr>
<tr>
<td>Variable name</td>
<td>Value</td>
<td>Label</td>
</tr>
<tr>
<td>-------------------------------------</td>
<td>-------</td>
<td>----------------</td>
</tr>
<tr>
<td>Disciplinary history member firm</td>
<td>0</td>
<td>First time offender</td>
</tr>
<tr>
<td></td>
<td>1</td>
<td>Repeat offender</td>
</tr>
<tr>
<td>Disciplinary history individual offender</td>
<td>0</td>
<td>First time offender</td>
</tr>
<tr>
<td></td>
<td>1</td>
<td>Repeat offender</td>
</tr>
<tr>
<td>Appeals</td>
<td>1</td>
<td>Allowed</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>Dismissed</td>
</tr>
<tr>
<td>Penalties Individual offender</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Terms and conditions</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Reprimand</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Rewriting license</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Supervision</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Suspension</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Permanent bans</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Fines</td>
<td>Dollar Amount</td>
<td></td>
</tr>
<tr>
<td>Costs</td>
<td>Dollar Amount</td>
<td></td>
</tr>
<tr>
<td>Disgorgement</td>
<td>Dollar Amount</td>
<td></td>
</tr>
<tr>
<td>Penalties Member Firms</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Terms and conditions</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Reprimand</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Suspension</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Termination</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Expulsion</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Fines</td>
<td>Dollar Amount</td>
<td></td>
</tr>
<tr>
<td>Costs</td>
<td>Dollar Amount</td>
<td></td>
</tr>
<tr>
<td>Disgorgement</td>
<td>Dollar Amount</td>
<td></td>
</tr>
<tr>
<td>Offences</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Variable name</td>
<td>Quasi-Criminal offences</td>
<td>Value</td>
</tr>
<tr>
<td>---------------</td>
<td>-------------------------</td>
<td>-------</td>
</tr>
<tr>
<td>Fraud</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Forgery</td>
<td></td>
<td>2</td>
</tr>
<tr>
<td>False Endorsement</td>
<td></td>
<td>3</td>
</tr>
<tr>
<td>Misappropriation of funds</td>
<td></td>
<td>4</td>
</tr>
<tr>
<td>Securities Act breach</td>
<td></td>
<td>5</td>
</tr>
<tr>
<td><strong>Conflict of Interest Offences</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unauthorized of inside information</td>
<td></td>
<td>6</td>
</tr>
<tr>
<td>Improper use/disclosure of client information</td>
<td></td>
<td>7</td>
</tr>
<tr>
<td>Undisclosed/unauthorized accounts</td>
<td></td>
<td>8</td>
</tr>
<tr>
<td>Undisclosed personal business</td>
<td></td>
<td>9</td>
</tr>
<tr>
<td>Undisclosed personal business with client</td>
<td></td>
<td>10</td>
</tr>
<tr>
<td>Attempt to settle client claim from compensation</td>
<td></td>
<td>11</td>
</tr>
<tr>
<td>Failure to ensure client orders are given priority</td>
<td></td>
<td>12</td>
</tr>
<tr>
<td><strong>Improper Sales Practices</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unsuitable recommendation</td>
<td></td>
<td>13</td>
</tr>
<tr>
<td>Failure to know your client</td>
<td></td>
<td>14</td>
</tr>
<tr>
<td>Failure to update NAAF</td>
<td></td>
<td>15</td>
</tr>
<tr>
<td>Order not within bounds of good business practice (free riding)</td>
<td></td>
<td>16</td>
</tr>
<tr>
<td>Churning</td>
<td></td>
<td>17</td>
</tr>
<tr>
<td>Discretionary trading</td>
<td></td>
<td>18</td>
</tr>
<tr>
<td>Unauthorized trading</td>
<td></td>
<td>19</td>
</tr>
<tr>
<td>Unauthorized distribution of sales literature</td>
<td></td>
<td>20</td>
</tr>
<tr>
<td>Unauthorized third party instruction</td>
<td></td>
<td>21</td>
</tr>
<tr>
<td>Outside business activities</td>
<td></td>
<td>22</td>
</tr>
<tr>
<td><strong>Internal Control Offences</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital deficiencies</td>
<td></td>
<td>23</td>
</tr>
<tr>
<td>Failure to establish and maintain adequate internal controls</td>
<td></td>
<td>24</td>
</tr>
<tr>
<td>Failure to supervise</td>
<td></td>
<td>25</td>
</tr>
<tr>
<td>Failure to obtain and maintain minimum required margin</td>
<td></td>
<td>26</td>
</tr>
<tr>
<td>Investors’ Variables</td>
<td></td>
<td></td>
</tr>
<tr>
<td>----------------------</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Variable name</strong></td>
<td><strong>Value</strong></td>
<td><strong>Label</strong></td>
</tr>
<tr>
<td>Record keeping violation</td>
<td>27</td>
<td></td>
</tr>
<tr>
<td><strong>Cooperation, Membership and Misrepresentation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Failure to cooperate</td>
<td>28</td>
<td></td>
</tr>
<tr>
<td>Misrepresenting credentials</td>
<td>29</td>
<td></td>
</tr>
<tr>
<td>Allowing an unregistered person to trade</td>
<td>30</td>
<td></td>
</tr>
<tr>
<td>Conducting business while suspended</td>
<td>31</td>
<td></td>
</tr>
<tr>
<td>Misrepresentations</td>
<td>32</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>33</td>
<td></td>
</tr>
<tr>
<td><strong>Aggravating and Mitigating Factors</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aggravating Factors Identified and Considered</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Aggravating Factors Identified, but not Considered</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Mitigating Factors</td>
<td>3</td>
<td></td>
</tr>
</tbody>
</table>