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Citation: Sutton (Re), 2018 ONSEC 42
Date: 2018-08-14
File No. 2017-37 and 2018-10

IN THE MATTER OF
BRIAN MICHAEL SUTTON

and

IN THE MATTER OF THE INVESTMENT
INDUSTRY REGULATORY ORGANIZATION OF CANADA

REASONS AND DECISION
(Subsection 8(3) and section 21.7 of the *Securities Act*, RSO 1990, c S.5)

Hearing:	June 28, 2018	
Decision:	August 14, 2018	
Panel:	Timothy Moseley	Vice-Chair and Chair of the Panel
	Deborah Leckman	Commissioner
	Lawrence Haber	Commissioner
Appearances:	Kenneth A. Dekker Daphne Hooper	For Brian Michael Sutton
	Linda Fuerst Rob DelFrate Ted Brook	For Staff of the Investment Industry Regulatory Organization of Canada
	Yvonne Chisholm	For Staff of the Ontario Securities Commission

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REASONS AND DECISION

I. OVERVIEW

[1] Brian Sutton was the Chief Financial Officer (**CFO**) of First Leaside Securities Inc. (**FLSI**), a dealer member firm of the Investment Industry Regulatory Organization of Canada (**IIROC**). One of Mr. Sutton's responsibilities at FLSI involved the pricing of certain unlisted securities issued by three limited partnerships (the **Funds**) related to FLSI. Specifically, Mr. Sutton was responsible for ascribing a price for the units of the Funds (the **Fund Units**), to be shown on statements issued to every unitholder, most if not all of whom were clients of FLSI.

[2] IIROC Staff alleged that from September 2009 to October 2011 (the **Material Time**), Mr. Sutton failed to discharge that responsibility properly, contrary to IIROC Dealer Member Rule 38.6(c), which requires a CFO to "monitor adherence to the Dealer Member's policies and procedures as necessary to provide reasonable assurance that the Dealer Member complies with [IIROC's] financial rules."

[3] At a hearing before an IIROC tribunal panel, Mr. Sutton claimed that he had relied on an active market in the Fund Units in order to ascribe an appropriate price. In the IIROC panel's decision of July 5, 2017 (the **Liability Decision**)[1], the panel concluded that there had been no active market that could properly form the basis for pricing decisions, and that the price of the Fund Units as communicated to the unitholders did not reflect the value of those securities. The IIROC panel found that Mr. Sutton had indeed breached Rule 38.6(c).

[4] In a subsequent decision dated January 31, 2018 (the **Sanctions and Costs Decision**)[2], the IIROC panel described Mr. Sutton's error as an "honest mistake".[3] The panel imposed a fine of $25,000 and reprimanded Mr. Sutton. It declined IIROC Staff's request for a $100,000 fine, a permanent prohibition against Mr. Sutton's registration as a CFO with an IIROC Dealer Member, and costs.

[5] Mr. Sutton applies to the Commission for a review of the Liability Decision. He asserts that the IIROC panel erred in a number of ways, including by:

a. reviewing material that was not properly before it;

b. making findings of fact that were unsupported by the evidence;

c. unjustifiably concluding that there was no active market in one of the Funds at issue;

d. reaching conclusions, without the benefit of expert evidence, about Mr. Sutton's conduct; and

[1] *Sutton (Re)*, 2017 IIROC 35.
[2] *Sutton (Re)*, 2018 IIROC 03.
[3] Sanctions and Costs Decision at paras 1, 12.

e. effectively holding Mr. Sutton to a strict liability standard, by finding a breach despite what the panel described as an absence of "*mens rea* or intent to do wrong".[4]

[6] IIROC Staff applies to the Commission for a review of the Sanctions and Costs Decision. IIROC Staff asserts that the sanctions ought to be more severe, and that Mr. Sutton ought to be ordered to pay costs. IIROC Staff submits that the IIROC panel erred by, among other things:

a. failing to consider Mr. Sutton's role as a gatekeeper;

b. disregarding the importance of accurate information to investors;

c. concluding that Mr. Sutton's breach did not harm investors;

d. improperly treating Mr. Sutton's history and seniority in the securities industry as a mitigating factor; and

e. concluding that because Mr. Sutton's error was "an honest mistake", it would not be appropriate to impose a prohibition on his approval.

[7] Our decision and these reasons relate to both applications, which were heard together.

[8] For the reasons that follow, we conclude that in reaching the Liability Decision, the IIROC panel made errors that, when taken together, constitute an error of law that leads us to set aside the Liability Decision and substitute our own decision. Having said that, once we complete our own analysis, we reach the same result that the IIROC panel did; that is, that Mr. Sutton contravened Rule 38.6(c).

[9] Any sanctions decision has as its foundation a preceding liability or merits decision. In this case, therefore, because we are setting aside the Liability Decision, we consider the questions of sanctions and costs afresh, and substitute our own decision for the Sanctions and Costs Decision. We conclude that the sanctions imposed by the IIROC panel did not adequately address the seriousness of this matter, and that the circumstances warrant a fine of $50,000, a three-year prohibition against Mr. Sutton being approved as a CFO of an IIROC dealer member, and a reprimand. We also conclude that Mr. Sutton should be required to pay costs to IIROC in the amount of $50,000.

II. REGULATORY FRAMEWORK

[10] In carrying out its responsibility to oversee recognized self-regulatory organizations such as IIROC, including the review of decisions of those organizations, the Commission must be guided by the purposes of the *Securities Act* (the **Act**)[5], as set out in section 1.1 of the Act. In this matter, most relevant among those purposes are the protection of investors from unfair or improper practices, and the fostering of confidence in capital markets.

[11] In an enforcement proceeding that originates before a self-regulatory organization, that organization, like the Commission, must discharge its function

[4] Liability Decision at para 2.
[5] RSO 1990, c S.5.

in a manner that "restrain[s] future conduct that is likely to be prejudicial to the public interest in fair and efficient capital markets".[6]

[12] These principles apply both to the liability phase and to the sanctions and costs phase (if any) of an enforcement proceeding. In our analysis below regarding sanctions, we also refer to the *IIROC Sanction Guidelines*[7], a document that assists IIROC panels in determining appropriate sanctions, and helps set expectations among those participants in the capital markets who are regulated by IIROC.

III. BACKGROUND

A. Introduction

[13] Before setting out the background facts, or engaging in our analysis, some clarification is in order with respect to one key issue that arises in this case. We address the issue in more detail below, but a reading of our reasons will be assisted by some preliminary comments regarding terminology.

[14] The issue relates to the price of the Fund Units, and to the roles played by Mr. Sutton and others in that regard. The price of a Fund Unit manifests itself at two different stages in the process: first, when a trade is executed, and second, when information is communicated to unitholders by way of periodic statements.

[15] As we explain below, the price at which every trade in Fund Units was executed during the Material Time was fixed by Mr. Phillips, the President and Ultimate Designated Person (**UDP**) of FLSI. In this sense, Mr. Phillips "determined" the price of every trade.

[16] It was then Mr. Sutton's responsibility to assess the price at which the trade had already been executed and decide whether it was appropriate to show that price on unitholder statements. An internal FLSI document that Mr. Sutton created to describe the pricing methodology (see paragraph [88] below) notes that it is the CFO's responsibility to "determine" and to "establish" the price of a Fund Unit.

[17] The word "determine", in this context, is ambiguous as between the different roles played by Mr. Phillips and Mr. Sutton. Accordingly, we have adopted "fix" to describe Mr. Phillips's role, and "ascribe" to describe Mr. Sutton's role. These terms reflect our findings as set out below.

B. Facts

[18] The Fund Units were sold through FLSI, a dealer that was a member of a group of affiliated entities (referred to together as the **FL Group**). The three Funds, which were themselves members of the FL Group, were:

a. the First Leaside Fund, units of which were issued as an exempt product to accredited investors starting in 2005, and the sole material assets of which were unsecured promissory notes given by FL Master Texas Ltd. (**Master Texas**), a member of the FL Group;

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[6] *Committee for Equal Treatment of Asbestos Minority Shareholders v Ontario (Securities Commission)*, 2001 SCC 37, [2001] 2 SCR 132 at para 43.

[7] *IIROC Sanction Guidelines*, Investment Industry Regulatory Organization of Canada, online: http://www.iiroc.ca/industry/enforcement/Documents/IIROCSanctionGuidelines_en.pdf (***IIROC Sanction Guidelines***)

b. the First Leaside Properties Fund (**Properties Fund**), units of which were issued pursuant to a prospectus beginning in 2009, and the sole material assets of which were unsecured promissory notes given by FL Master Sherman Ltd. (**Master Sherman**), a member of the FL Group; and

c. the Wimberly Fund, units of which were issued pursuant to offering memoranda under two offerings in May and November of 2010, and the sole material assets of which were unsecured promissory notes given by Master Texas.

[19] The debtors Master Texas and Master Sherman were based in Texas, and invested in real estate, primarily in that state. Interest on the promissory notes was paid first by the debtor to the Fund, and then paid out to unitholders of the Fund. The unitholders also expected to receive a return of their principal at the end of the ten-year maturity period.

[20] All trades of all units of all three Funds, including initial distributions and secondary market trades, were executed at $1.00 per unit throughout the Material Time. Until the fall of 2011, FLSI issued statements to its client unitholders, showing $1.00 as the current price of the Fund Units. Beginning in the fall of 2011, FLSI began to show the price as "not available".

[21] Mr. Sutton is 68 years old and has had a long and unblemished career in various capital markets-related positions, including consulting work and senior roles with IIROC member firms. He is not currently registered. During the Material Time, he was CFO of FLSI but had no other role at FLSI or with other members of the FL Group.

IV. ISSUES

[22] These applications present the following issues:

a. What is the standard of review when the Commission reviews the decision of a self-regulatory organization, including with respect to alleged procedural errors?

b. What should be the consequences, if any, of the IIROC panel's having reviewed material that was not properly in evidence before it, as the parties have agreed that the panel did?

c. Apart from the IIROC panel's review of extraneous material, did the panel reach conclusions unsupported by the evidence, and if so, what should be the consequences of its having done so?

d. Was Mr. Sutton's methodology for ascribing a price for Fund Units appropriate? In particular, did the trading history of Fund Units constitute an "active market" sufficient for this purpose?

e. Did Mr. Sutton adequately monitor adherence to FLSI's policies and procedures as necessary to provide reasonable assurance that FLSI complied with IIROC's financial rules, and if not, did he thereby contravene IIROC Dealer Member Rule 38.6(c)?

f. Was the Commission required to hear expert evidence in order to reach a conclusion on the preceding issue?

g. If Mr. Sutton contravened IIROC Dealer Member Rule 38.6(c), what are the appropriate sanctions, and should Mr. Sutton be required to pay costs?

V. ANALYSIS

A. Standard of review

[23] Subsections 8(3) and 21.7(2) of the Act govern an application to the Commission, by a person or company directly affected by a decision of a self-regulatory organization (**SRO**), for a review of that decision. Together, those subsections authorize the Commission to confirm the decision of the SRO, or to "make such other decision as the Commission considers proper."

[24] The Commission's review of an SRO decision is a hearing *de novo*, rather than an appeal. In other words, the Commission exercises original jurisdiction rather than a more limited appellate jurisdiction. Further, no deference need be accorded by the Commission to the SRO panel's decision.[8]

[25] Despite the fact that such deference is not required, the Commission has chosen as a matter of practice to limit the circumstances under which it will substitute its own decision for that of an SRO panel.[9] This choice is consistent with the requirement in the Act that the Commission have regard to the fundamental principle that the Commission should "use the enforcement capability and regulatory expertise of recognized self-regulatory organizations."[10]

[26] The Commission has often stated[11] that it will interfere with an SRO decision only if:

a. the hearing panel proceeded on an incorrect principle;

b. the hearing panel erred in law;

c. the hearing panel overlooked some material evidence;

d. new and compelling evidence is presented to the Commission that was not presented to the hearing panel; or

e. the hearing panel's perception of the public interest conflicts with that of the Commission.

[27] Mr. Sutton submitted that "there is no deference shown [to the SRO panel] on issues of law or issues of procedural fairness – in which case the standard of review is always correctness."[12] In support of this proposition, Mr. Sutton cited authority that addresses the standard of review applicable to a court reviewing a decision of the Commission, as opposed to the Commission reviewing an SRO decision.

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[8] *Johal v Funeral Services*, 2012 ONCA 785 at para 4; *HudBay Minerals Inc. (Re)*, 2009 ONSEC 15, (2009), 32 OSCB 3733 at para 106.

[9] *Pariak-Lukic v Investment Industry Regulatory Organization of Canada*, 2016 ONSC 2564 (Div Ct) (***Pariak-Lukic* DivCt**) at para 14.

[10] Paragraph 4 of section 2.1 of the Act.

[11] See, *e.g.*, *Canada Malting Co. (Re)* (1986), 9 OSCB 3565 at para 24; *Marek (Re)* 2017 ONSEC 41, (2017), 40 OSCB 9167 at para 24.

[12] Sutton's written submissions (liability) at para 152.

[28] We do not accept that submission. While courts may impose a standard of correctness on issues of procedural fairness, there is no statutory or judicial authority that requires a similar approach by the Commission. We see no reason to disturb the long-standing test set out above in paragraph [26].

B. Problems relating to evidence at the IIROC hearing

1. Introduction

[29] We will now consider Mr. Sutton's submission that the IIROC panel made a number of errors regarding evidence, and that these errors are serious enough to warrant our setting aside the Liability Decision.

[30] Underlying this submission is the important principle that respondents must know the case they have to meet, and that they must have the opportunity to meet it.

[31] The errors fall into two categories: review by the panel of material not properly before it, and findings of fact not supported by the evidence that was properly before it.

2. Review of material not in evidence

[32] We begin with Mr. Sutton's submission that the panel reviewed material that was not in evidence.

[33] At the beginning of the liability hearing before the IIROC panel, IIROC Staff filed a 13-volume compendium of documents. The parties had reached an agreement, which the panel accepted, that admissibility of the compendium's contents would be dealt with on a document-by-document basis, as documents were referred to by counsel or by witnesses. The panel members were not to review material that was not brought to their attention during the hearing.

[34] It is common ground that despite this clear understanding, the IIROC panel made three references in the Liability Decision to material that had not been referred to during the hearing, and which, it would appear, the panel reviewed after the hearing, or possibly before the hearing but without adverting to the material during the hearing. In this application before the Commission, IIROC Staff properly conceded that the panel ought not to have done so. IIROC Staff submits, however, that these errors by the IIROC panel were inconsequential. IIROC Staff disagrees with Mr. Sutton's submission that the errors resulted in an unfairness to him.

[35] We consider each of the three errors in turn. We then consider Mr. Sutton's concern that the panel may have reviewed other extraneous material not cited in the Liability Decision.

(a) Internal IIROC emails

[36] Paragraph 35 of the Liability Decision reproduces a series of internal IIROC emails from September 2010. In that paragraph, the IIROC panel introduced the emails as follows:

> While there was no direct evidence in the record before the Hearing Panel of a concern on the part of FinOps [IIROC's Financial Operational Compliance section] about FLSI's pricing of the Fund Units until the latter part of 2010, in an

> email dated September 17, 2010 from Mr. Dines [IIROC's Manager, Financial and Operational Compliance] to his FinOps superiors, there is an indication that FinOps had had concerns earlier.

[37] It is common ground that the emails were not introduced into evidence during the hearing. The panel ought not to have reviewed them and ought not to have incorporated them into the Liability Decision.

[38] The Liability Decision contains no subsequent explicit reference to the emails, and it is not clear whether or not the emails formed a part of the panel's analysis. It is possible, although not certain, that the panel had the emails in mind in writing paragraph 60 of the decision, which concludes that at least by 2010, "the FL Group faced financial difficulties", a finding for which there was no evidence before the panel. The panel goes on to imply, without stating explicitly, that the financial difficulties resulted in pressure to maintain the price of $1.00 per Fund Unit.

[39] Nowhere in the Liability Decision does the panel make a connection between IIROC Staff's view of the situation (as reflected in the emails) and any of the factual findings that underlie the panel's ultimate conclusions as to liability. In our view, no such connection exists.

[40] IIROC Staff submits that while the IIROC panel's reference to the emails was an error, it was an inconsequential one. We agree that by itself, this error would not justify our interfering with the decision.

(b) Grant Thornton report

[41] Paragraphs 46 and 47 of the Liability Decision refer to the contents of an August 2011 report produced by Grant Thornton LLP, an accounting and consulting firm that had been retained to review and make recommendations regarding the affairs of the FL Group (the **Grant Thornton Report**).

[42] The Grant Thornton Report was presented to one witness, who was asked only to review an organizational chart that was included in the report. The report's authors were not called as witnesses at the IIROC hearing, and the report was never referred to again.

[43] Despite the limited use made during the hearing of the Grant Thornton Report, the IIROC panel quoted in the Liability Decision a number of the report's findings regarding the process associated with the purchase of certain unspecified limited partnership units. The panel did not go on to rely on those findings, however. In fact, the panel noted that there are errors in the findings with respect to the pricing process. The panel also noted that Mr. Sutton is not mentioned in the report, that it appeared that Mr. Sutton had not been interviewed for the report, and that Mr. Sutton did not even see the report until after the IIROC proceeding was commenced.

[44] Further, the panel did not advert to whether the quoted findings actually referred to the three Funds involved in this case. It is not clear that they do.

[45] Given all those limitations, we do not know why the Grant Thornton Report was mentioned in the Liability Decision. In any event, it is common ground that the panel ought not to have reviewed the report (other than the organizational chart) and ought not to have referred to the report's findings. Having said that,

and especially in light of the panel's conclusion that the report's findings were incorrect, we are satisfied that the panel did not rely on the report. We agree with IIROC Staff's contention that this error by the panel was inconsequential.

(c) IIROC Staff's interview of FLSI's former Chief Compliance Officer

[46] In paragraph 58 of the Liability Decision, the panel addresses what it calls the "precarious nature of the promise" by Mr. Phillips, the founder of the FL Group and the President and UDP of FLSI, that any investor who wanted to recover their investment could do so. To illustrate that point, the panel quotes from the transcript of an interview by IIROC Staff of FLSI's former Chief Compliance Officer (**CCO**). In the quoted portion, the former CCO testifies about what might happen "should investors sense problems", *i.e.*, if holders of the Fund Units were to become aware that their expected interest payments were in jeopardy:

> So that they then turn to their clients and say, You know what? We just figured out these properties can't afford your 9 percent interest." And then everyone says, "Give me back my money". And, boom, we would be where we are today. At least we stopped selling it.

[47] It is common ground that the interview transcript was not in evidence at the hearing. It ought not to have been reviewed by the panel and it ought not to have been referred to in the Liability Decision. Once again, IIROC Staff concedes the error but maintains that it is of no consequence, for two primary reasons.

[48] First, IIROC Staff submits that it is "only common sense"[13] that a sell-off might have occurred if the value of a Fund Unit could not be determined or was less than $1.00. IIROC Staff acknowledges that this possibility may have been a motivation for FLSI to continue to show the price as $1.00.

[49] While there is some truth to that submission, one must ask why, if the proposition were "only common sense", the panel nonetheless felt that the CCO's perspective added anything and was therefore worth mentioning. We cannot be sure of the answer, but in our view, there is at least a reasonable likelihood that the CCO's statement contributed to the panel's view of the nature of the commitment by Mr. Phillips or FLSI to redeem Fund Units for $1.00. Indeed, as noted above, the panel's opening words in paragraph 58 of the Liability Decision connect the quoted statement with the panel's conclusion about the commitment. We are therefore unable to conclude that the quoted text had no influence on the panel's thinking.

[50] IIROC Staff's second submission on this point is that the excerpted portion does not directly relate to the question of whether Mr. Sutton adhered to the FLSI Pricing Policy. It is true that the panel's reasons do not explicitly connect the CCO's comment to the ultimate conclusion. However, we are left with some discomfort, given that the $1.00 price, and the process that led to every trade being conducted at that price, were central to the panel's analysis.

[51] Specifically, the extent to which FLSI or Mr. Phillips could be counted on to deliver a trade at $1.00, no matter what the circumstances, may have played a

[13] IIROC's written submissions (liability) at para 62.

part in the panel's ultimate determination that it was inappropriate to show the $1.00 price to other investors as being the actual value of a Fund Unit.

[52] The panel's reasons do not disclose what emphasis, if any, the panel placed on the quoted text. In such circumstances, we are of the view that within a range of reasonable possibilities, the uncertainty should accrue to the benefit of Mr. Sutton, against whom the adverse finding was made.

(d) The possibility of other extraneous material

[53] Mr. Sutton expresses the concern that the above three items are the known instances of the panel going beyond the permissible boundaries, but that the panel may have reviewed other extraneous material. IIROC Staff submits that there is no basis for that concern, and that it is mere speculation.

[54] In response, Mr. Sutton cites the example of the excerpt from the transcript of the CCO's examination. He points out that the transcript numbered more than 250 pages. At no time during the IIROC hearing did either party direct the panel's attention to the quoted portion. Mr. Sutton asserts, and we agree, that it defies logic to assume that the panel did not read any portion of the transcript other than the several sentences quoted above.

[55] Similarly, neither party directed the IIROC panel's attention to the emails referred to in paragraph 35 of the Liability Decision. The panel selected the emails and the quoted text from among the 13 volumes, and cited them along with the findings from the Grant Thornton Report. We can conceive of no reasonable explanation other than that the panel reviewed various extraneous materials from the compendium, either before or after the hearing, and in either case without notice to the parties. In our view, this scenario is a likely one and is well beyond mere speculation.

(e) Conclusion as to extraneous material

[56] The IIROC panel's review of extraneous material, the extent of which is unclear, is of particular concern to us. Mr. Sutton was denied the opportunity to confront this material, whether by challenging its admissibility, or by seeking to minimize its impact by leading evidence to the contrary or through cross-examination.

[57] We cannot be sure how influential the extraneous material was on the panel's thinking, in particular because we are not in a position to know how much extraneous material the panel reviewed in addition to the three items referred to in paragraphs [36] to [52] above. Given the uncertainty, it would be unfair to Mr. Sutton for us to assume that there was no further prejudice to him beyond that associated with those three items.

3. Unsupported findings of fact

[58] We now consider Mr. Sutton's other complaint regarding evidentiary matters, *i.e.*, his submission that the panel reached factual conclusions unsupported by the evidence that was properly before the panel. They are as follows.

(a) Alleged promise by Mr. Dines to Mr. Sutton

[59] In paragraphs 52 through 55 of the Liability Decision, the IIROC panel refers to a meeting that took place in June of 2011. Attendees included Mr. Dines of IIROC and Mr. Sutton, as well as a number of other individuals. Immediately following that group meeting, Mr. Dines and Mr. Sutton met separately. The only evidence

before the IIROC panel about what happened at that second meeting came from Mr. Sutton at the IIROC hearing.

[60] In his evidence, Mr. Sutton referred to a Review Engagement Report prepared by accounting firm Sloan Partners LLP (the **Sloan Report**), which had been prepared at the request of Properties Fund, and which commented on the book value of the Fund's promissory notes receivable. According to Mr. Sutton, Mr. Dines said to Mr. Sutton in the second meeting that if Penson Financial Services (**Penson**), FLSI's carrying broker, would accept the Sloan Report, then "my [Mr. Dines's] file is closed."[14] Mr. Sutton "said okay", and the meeting ended. The IIROC panel had no further evidence about that discussion.

[61] In the Liability Decision, the IIROC panel mischaracterized Mr. Sutton's evidence. In paragraph 55, the panel wrote:

> …even assuming the promise was made as Mr. Sutton asserts it was, it was far beyond Mr. Dines' authority to terminate proceedings, which at that stage involved both IIROC Enforcement and the Ontario Securities Commission on his own initiative. In that regard, it is worthy of note that there is no written reference in the written record before us of such a promise. If it was made, the promise was unenforceable and Mr. Sutton would have been well aware of that fact.

[62] Contrary to the panel's description, Mr. Sutton's evidence did not refer to any "proceedings". According to Mr. Sutton, Mr. Dines referred only to Mr. Dines's own file. There was no basis for the panel to conclude that Mr. Sutton was claiming that Mr. Dines had made a promise beyond Mr. Dines's authority; indeed, there was no evidence about what limits there were on that authority.

[63] More importantly, the panel's reference to the absence of a written record, and the somewhat dismissive "Mr. Sutton would have been well aware of that fact", both imply that the panel questioned the reliability of his evidence on this point.

[64] It is true that the unfavourable impression that this mischaracterization created would have been mitigated at least somewhat by the favourable comments that the panel made about Mr. Sutton throughout the Liability Decision. Nonetheless, the unfavourable impression ought not to have existed at all.

(b) Conclusion regarding the setting of the price

[65] Paragraph 57 of the Liability Decision says: "While it is not entirely clear on the record, it seems highly likely that the selection of $1.00 was made by Mr. Phillips."

[66] Mr. Sutton submits that there was no evidence upon which the panel could have concluded that Mr. Phillips set the price. We disagree. At the IIROC liability hearing, IIROC Staff read into the record various excerpts from the transcript of the interview of Mr. Sutton during the investigation. Mr. Sutton testified that

[14] Exhibit 1, Tab 32, Transcript of the testimony of Brian Sutton, January 20, 2017, at p 65, lines 8-9.

Mr. Phillips described the process as follows: "We maintain the market. We maintain the price. We support it."[15]

[67] Mr. Phillips's role did not end at fixing the price that was to be applied. According to Mr. Sutton, Mr. Phillips also said: "…I'm in charge here… I approve every single trade",[16] and that Mr. Phillips justified that role by saying, "It's my firm."[17]

[68] That evidence amply supports the IIROC panel's conclusion.

[69] In paragraph 57 of the Liability Decision, the panel goes on to say:

> By offering the original purchase price to investors who 'wished to liquidate' their investments as one witness put it, Mr. Phillips offered them the security of believing they would be able to recover their investment should they choose to do so…

[70] Mr. Sutton notes that the mentioned witness is unidentified, and he submits that there was no evidence to support the panel's conclusion about investors' beliefs. In our view, the identity of the witness is inconsequential; the panel merely adopted the phrasing of that witness. The conclusion the panel reached is a sensible and natural inference that could easily be drawn from the evidence in the record.

(c) FL Group's financial difficulties

[71] In paragraph 60 of the Liability Decision, the panel states:

> In 2010 and perhaps earlier, it was apparent that the FL Group faced financial difficulties which would become overwhelming if it couldn't maintain the confidence of its investors. Mr. Sutton must have known that was the case…

[72] Mr. Sutton submits that there was no evidence to support the conclusion about the FL Group's financial situation or about Mr. Sutton's knowledge of that situation. In response, IIROC Staff does not cite any supporting evidence, but maintains that the conclusions are of no consequence to the ultimate issue.

[73] We are unable to accept IIROC Staff's categorical submission. The panel goes on to say that "Mr. Sutton stuck bravely, if somewhat irrationally, to the idea that $1.00 was a market derived price." The panel included both the text quoted above regarding the FL Group's financial situation, and this latter comment about Mr. Sutton's "irrational" behaviour, in the same paragraph. At the very least, this suggests that the panel thought there was a connection, and likely a causal one. If the panel reached that conclusion, as would appear to be the case, it ought not to have done so.

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[15] Exhibit 2, Tab 5, Transcript of the testimony of Edward Varela, January 17, 2017, at p 154, line 3835.

[16] Exhibit 2, Tab 5, Transcript of the testimony of Edward Varela, January 17, 2017, at p 150, line 3739.

[17] Exhibit 2, Tab 5, Transcript of the testimony of Edward Varela, January 17, 2017, at p 160, line 3999.

(d) Trades in the Properties Fund

[74] Finally, Mr. Sutton points to paragraph 42 of the Liability Decision, in which the IIROC panel refers to a report from accounting firm Parker Simone LLP, issued in August 2011, regarding trading in the Properties Fund (the **Parker Simone Report**). Mr. Sutton submits that the panel was incorrect in stating that "there were relatively few trades and the trades were all through FLSI or a related company at a fixed price."

[75] We do not accept Mr. Sutton's assertion. The term "relatively few" is not unreasonable, because it is vague, and we do not know "relative to what?". As for the trades being "through FLSI or a related company", the evidence was clear that all trades had some connection to FLSI or other members of the FL Group. Even those trades that were crosses between third parties involved no independent dealers. Further, as noted above, Mr. Phillips approved every trade. It is therefore fair to say that all trades were "through FLSI or a related company."

4. Conclusion as to evidentiary issues

[76] Disciplinary proceedings before an SRO panel, or similar proceedings before this Commission, can have serious consequences for market participants generally, and particularly for those whose career may be affected by an adverse decision. We bear that important point in mind as we assess the gravity of the IIROC panel's errors in this case.

[77] To summarize our findings regarding Mr. Sutton's concerns about the IIROC panel's treatment of evidence, we conclude that his concerns are well-founded in respect of the following:

a. the panel's review of numerous extraneous materials, *i.e.*, the 2010 internal IIROC emails, the Grant Thornton Report, and the transcript of the interview of the former CCO;

b. the likelihood that the panel reviewed other documents not in evidence before it, including other portions of the transcript of the interview of the former CCO;

c. the panel's mischaracterization of the evidence regarding the meeting between Mr. Dines and Mr. Sutton; and

d. the panel's statement, unsupported by the evidence, regarding the FL Group's financial difficulties in 2010, and Mr. Sutton's knowledge of those difficulties.

[78] None of these, by itself, appears to have determined the outcome of either the Liability Decision or the Sanctions and Costs Decision. However, these errors have a cumulative effect. Together they constitute a significant unfairness to Mr. Sutton, and an error of law that is substantial enough to warrant our setting aside the Liability Decision and the Sanctions and Costs Decision, and substituting our own decisions.

[79] Therefore, we now turn to conduct our own analysis of the issues raised by IIROC Staff's allegation against Mr. Sutton, that he breached Dealer Member Rule 38.6(c).

C. IIROC Staff's allegation that Mr. Sutton breached Dealer Member Rule 38.6(c)

1. Introduction

[80] The rule that Mr. Sutton was alleged to have breached requires that a CFO "monitor adherence to" firm policies and procedures "as necessary to provide reasonable assurance" that the firm is in compliance with applicable financial rules.

[81] In this case, the relevant firm policies and procedures governed the task of ascribing an appropriate price to the Fund Units, to be communicated to client unitholders (among other purposes). At many firms, someone other than the CFO would carry out that task, and the CFO would monitor that activity. In contrast, at FLSI the policies and procedures expressly contemplated that the CFO herself/himself would be carrying out the task of ascribing an appropriate price. Such a practice is not unusual, especially for a smaller firm.

[82] Mr. Sutton points to the fact that the Dealer Member Rule that he is alleged to have contravened addresses the obligation imposed on a CFO, not the obligations of a person who prices securities. Mr. Sutton therefore urges us to focus on the appropriate conduct of a CFO who is in a monitoring role, and he emphasizes the Rule's reference to "reasonable assurance" in that context.

[83] We will return below to review that submission, and to consider the implications of Mr. Sutton having been both the CFO and the person who carried out the task of ascribing a price to the Fund Units. Before doing so, however, we look at the pricing methodology and how Mr. Sutton applied it, without considering any different or additional obligations he had as CFO.

2. Pricing of the Fund Units

(a) Regulatory and policy requirements

[84] IIROC's Dealer Member Rule 17.2A requires that "every Dealer Member shall establish and maintain adequate internal controls in accordance with", among other things, IIROC's Internal Control Policy Statement 7 (**ICPS 7**), which addresses the pricing of securities.[18]

[85] ICPS 7 sets out a number of control objectives, including "independent and timely verification of security prices", and "accuracy and completeness of the pricing of securities and… the reliability of prices." This latter objective contemplates the existence of a range of possible approaches to determining an appropriate price. It also requires the application of a sound methodology designed to produce a sufficiently "reliable" price.

[86] FLSI's Policies and Procedures Manual (**PPM**), which Mr. Sutton was involved in drafting, described the firm's procedures and methodologies aimed at ensuring compliance with ICPS 7. Section 3.8.3 of the PPM, which dealt with the pricing of unlisted securities, listed various bases on which a price could be determined, with the first basis being the price at which previous trades were executed. However, the section provided that if the CFO were to obtain prices from traders

[18] Internal Control Policy Statement 7 is made part of IIROC's rules by virtue of Rule 2600.

or from Penson (its carrying broker), the prices must be accompanied by a record showing an independent source for the pricing.

[87] The PPM's alternative bases for pricing unlisted securities included the determination, where possible, of an issuer's net asset value or shareholders' equity. In situations where audited financial statements alone did not provide an accurate basis for valuation, *e.g.* where real estate assets were involved, the CFO was entitled to rely on valuations or appraisals performed by qualified third parties, and current financial statements. If the CFO could not obtain sufficient information to support a price, then the price was to be shown as "Price not available" on client monthly statements.

[88] IIROC Staff became concerned with how the Funds were being priced, and communicated those concerns to FLSI. In response, Mr. Sutton created the PPM Pricing Supplement (**Supplement**). He testified at the IIROC hearing that he wanted to "make a couple of things very clear to IIROC and Mr. Warden [the author of the report referred to in paragraph [133] below] …what exactly I had to do in my role and who I consulted with."[19]

[89] The Supplement described, in greater detail than the PPM, the processes and methodologies employed by FLSI in pricing the Fund Units, although it referred specifically only to the Properties Fund. It stated that the CFO, in consultation with Senior Management, would first determine if an "active market" existed for the Fund Units. If so, then the CFO, "in consultation with Senior Management, shall ascribe a price per Trust Unit accordingly".[20] Mr. Sutton emphasized that while the Supplement described a hierarchy of other criteria he would look to if no active market existed, "If I satisfy '1' [*i.e.*, the active market criterion], we're done."[21]

[90] The meaning of the term "active market", found in the Supplement, is therefore a central issue in this proceeding. The term is not defined in Ontario securities law, or in IIROC's rules, or in FLSI policies. We must therefore determine its meaning for the purposes of this case.

(b) What is meant by an "active market"?

[91] In the absence of a prescribed definition of "active market", we should be guided by the purpose for which that criterion forms a central element of the pricing methodology. A true active secondary market in a security can be the most reliable indicator of the fair market value of that security, and can equip existing or prospective unitholders to make fully informed investment decisions. As Mr. Sutton agreed at the hearing before us, he was responsible for assessing the price at which trades were executed, and for determining whether that price was an appropriate one to ascribe to the Fund Units and to show clients on their statements.

[92] Various factors can contribute to making a secondary market more reliable for the purpose of ascribing an appropriate price. It would be beyond the scope of this proceeding for us to attempt to prescribe an exhaustive list of factors that

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[19] Exhibit 1, Tab 31 and Exhibit 2, Tab 8, Transcript of the testimony of Brian Sutton, January 19, 2017, at p 119, lines 5-7.

[20] Exhibit 2, Tab 18, PPM Pricing Supplement at p 420.

[21] Exhibit 1, Tab 31 and Exhibit 2, Tab 8, Transcript of the testimony of Brian Sutton, January 19, 2017, at p 119, line 1.

could be applied in all cases in order to determine whether a particular market is sufficiently reliable. In the context of this case, however, three factors are particularly relevant:

a. *Independence* – Are the trades that purport to constitute the active market independent of any artificial constraint? In other words, did the trades occur at prices that reflect a true auction market, and/or freely negotiated arm's-length transactions between a willing seller and a willing buyer?

b. *Recency* – Are the trades sufficiently recent to justify reliance on them? In other words, are those trades now stale, giving rise to an appreciable risk that intervening events undermine the reliability of the prices?

c. *Frequency* – Even if there are trades that are sufficiently recent, did the relied-upon trades occur frequently enough to provide an adequate basis for concluding that the recent price is a fair market price?

[93] With those specific factors in mind, we now consider whether, throughout the Material Time, there was an active market as Mr. Sutton asserts there was.

(c) Did the trading in the Fund Units constitute an active market?

i. Introduction

[94] Before conducting our own analysis as to whether the trading in the Fund Units constituted an active market, we pause to note that Mr. Sutton's third basis of complaint regarding the Liability Decision is that the IIROC panel unjustifiably concluded that there was no such active market. He submits that the IIROC panel overlooked material evidence and misapprehended other evidence in reaching its conclusion. Because we have decided that we are substituting our own decision for that of the IIROC panel, and because we are therefore conducting our own analysis of the core question, there is no need for us to scrutinize the process by which the IIROC panel arrived at its conclusion. We decline to do so.

[95] We begin our own analysis by recalling Mr. Sutton's description of how he determined if there was an active market in the trading of the Properties Fund:

> …I looked at trading, trading summaries and the blotters that were produced from Penson. That tells me whether there's an active market… It was absolutely an active market… because of the volume of the trades...

[96] Mr. Sutton submitted that his reliance on Penson fulfilled the obligation, set out in the PPM and referred to in paragraph [86] above, that there be an independent source for the pricing. In one limited sense, Mr. Sutton is correct in this assertion. Penson was independent of FLSI, and it reported pricing information. However, Penson had a limited role. It was FLSI's carrying broker and performed administrative functions for FLSI. Penson's report detailed the trades that took place each month and the price at which each trade was executed. The prices on Penson's report were based directly on the trade tickets that were submitted by FLSI.

[97] While Penson had an obligation to give accurate reports that reflected the information it received, it was not Penson's role to assess or to opine on the appropriateness of trade prices, or on the communication of price information to FLSI clients. Indeed, as was expressly confirmed in the Parker Simone Report, "Penson is not involved in the pricing process."[22] Further, as Mr. Sutton himself confirmed, pricing was "[his] job. Not the others."[23]

[98] We agree with the IIROC panel's observation that "Penson's pricing of units was simply mirroring what FLSI said, and therefore cannot be seen as independent."[24] In other words, while Penson was independent for the limited purpose of summarizing and reporting objective facts (the prices at which trades took place), Penson's presence contributed nothing to the question of whether those prices were arrived at in a manner independent of artificial constraints. We reject Mr. Sutton's position that Penson's independence as a reporting entity means that its presence helps to establish the independence of the prices themselves, or that Penson was giving an independent opinion about the appropriateness of the prices (as opposed to the fact that those were the trade prices).

[99] Accordingly, Penson's presence is of no consequence to any of the three criteria we identified above, *i.e.*, independence, recency and frequency. We will now consider those criteria in the context of the other relevant facts of this case.

ii. Independence from artificial constraints

[100] Beginning at paragraph [66] above, we reviewed the evidence that demonstrates that Mr. Phillips fixed the price at which each trade took place. He maintained one consistent and constant price for units of all three Funds, throughout the Material Time, despite the different yields and maturity terms of the Funds, and despite the variability of market conditions (including prevailing interest rates) and of the values of the underlying assets. As we explain below, we find that Mr. Phillips's role precludes the conclusion that a true active market existed.

[101] Mr. Phillips's role in fixing the trade price leads to an inconsistency in Mr. Sutton's position. On one hand, Mr. Sutton maintains that there was an "active market" sufficient to serve the main purpose described above, *i.e.*, to equip existing and potential unitholders to make fully informed decisions about investing in Fund Units. On the other hand, Mr. Sutton relies on the very fact of Mr. Phillips's role, when Mr. Sutton maintains that the $1.00 price is reliable, in the sense that a unitholder wishing to sell could expect to be able to do so at that price.

[102] We find these two submissions to be inherently contradictory, in that the one thing on which potential sellers could supposedly rely is an external constraint that is inconsistent with the existence of a true active market.

[103] Having stated our finding in that regard, we nonetheless explore both submissions, beginning with Mr. Sutton's position regarding the existence of an active market. Our conclusion that no such active market existed is reinforced by the fact that, as noted above, there was no evidence that any bid or offer

[22] Exhibit 1, Tab 6, Parker Simone Report, at p 4.
[23] Exhibit 1, Tab 32 and Exhibit 2, Tab 8, Transcript of the testimony of Brian Sutton, January 19, 2017, at p 114, line 21.
[24] Liability Decision at para 61, footnote 2.

involved a dealer other than FLSI. In other words, there was no independent check against the arbitrary price that Mr. Phillips had set.

[104] Mr. Sutton could not reasonably have assumed that the constant price also happened to be a true market price. There is no inherent reason that fixed income instruments such as the Fund Units should trade at par. Factors such as interest rates, credit quality considerations and term to maturity would normally affect the pricing of any fixed income instrument.

[105] Even in times of low volatility, it would be highly improbable that the Fund Units from all three Funds would freely trade at the same price as each other, let alone all at a constant price, without any fluctuation, even over a few months, let alone over the longer period at issue here.[25] Such a pattern, especially given the higher-than-normal volatility in the wake of the global financial crisis, ought to have been an extreme red flag conveying the clear message that there was an external and artificial constraint on the trading price, and that an alternative approach was required in order to ascribe an appropriate price to the Fund Units, to disclose to unitholders.

[106] Having said that, and as noted above, Mr. Sutton also relies on this artificial constraint. Rather than seeing the unwavering price as a red flag, he viewed the history as evidence that unitholders who wanted to sell would continue to be able to do so at that price. His perspective might be somewhat defensible, but for two reasons:

a. The "guarantee" was illusory. The trading history was evidence that clients had, in the past, sold their Fund Units at $1.00, but there was no evidence that FLSI had committed to all or any unitholders to ensure a similar result in the future. If anything, the past history may have provided existing unitholders with a false sense of security.

b. The fixed price of $1.00 acted not only as a floor, but also as a ceiling. A selling unitholder was able to sell Fund Units at $1.00, but for no more than $1.00. It may well have been the case that at some point during the Material Time, if Fund Units had freely traded, their price would have exceeded $1.00. In those circumstances, some unitholders who sold at $1.00 would have been deprived of the opportunity to realize a higher market price.

[107] Any inherent contradictions aside, the fatal flaw in Mr. Sutton's position is, in our view, the incompatibility between the notion of a truly independent active market and Mr. Phillips's role in fixing prices.

iii. Recency and frequency

[108] Even if the trading history reflected prices that were independent, in that they were determined solely by market forces, it would be necessary to consider

[25] Mr. Sutton did submit that all primary market distributions had to be at the offering price. However, this fact is of little assistance to him, particularly given that most of the subject trading was in units of the Properties Fund, and that all of that trading came after the conclusion of the primary distribution. Further, IIROC Staff takes the position that trades from a fund to an FL Group entity may have been primary market distributions, but the subsequent sale of those units to a client would have been a secondary market trade. It is unnecessary for us to resolve that question, given our conclusion that much of the subject trading came after the initial distribution period.

whether that trading had been sufficiently recent and frequent so as to provide reliable information to existing or prospective unitholders.

[109] Our review of the records discloses that trading was sporadic at best for some periods during the Material Time.

[110] In the Properties Fund, three of the 24 months featured no trading at all, and one six-week period passed without any trades. Eleven of the remaining months featured only one day on which any trades took place, and no month had more than three such days. For the full year from October 2010 to October 2011 inclusive, trading occurred on only 14 days.

[111] The First Leaside Fund saw no trading at all in five of the 24 months, and only one day of trading in each of seven of the other months. From October 2010 to October 2011, trading occurred on only 12 days. Almost every month from June 2010 to October 2011 featured no more than 10 trades in the month.

[112] Trading in units of the Wimberly Fund was somewhat more active while it was in primary distribution from March 2010 to March 2011, although for the remaining months of 2011 (during which the Fund may still have been in primary distribution; the evidence is unclear) it followed a pattern similar to that of the other two Funds. Three of the seven months in 2011 featured no trading at all (including the two-month period of June and July), and four of the months had trading on only one day.

[113] Despite these patterns, FLSI showed $1.00 as the price on client statements, without interruption.

[114] It would not be appropriate for us to prescribe specific numeric measures against which, in all cases relating to all securities, the recency and frequency of trading can be assessed in order to determine whether that trading constitutes an "active market". Having said that, we have no hesitation in concluding that in this case, for at least some periods during the Material Time, there was insufficient trading to support the pricing information that FLSI communicated to its clients. This is particularly so for the Properties Fund throughout the two-year period, and for the First Leaside Fund for the last eighteen months, given the infrequent and sporadic trading.

iv. Conclusion as to active market

[115] We therefore cannot accept Mr. Sutton's position that there was an "active market" throughout the Material Time.

[116] At a minimum, Mr. Sutton should have been on alert not to rely solely on the trading history. By itself, the lack of independent trading ought to have set off alarm bells. The lack of sufficiently recent and frequent trading ought to have done the same, at least during the latter half of the Material Time, if not sooner.

[117] It was not reasonable for Mr. Sutton to conclude, especially as categorically as he did and on the basis that he did, that the trading history provided a sufficient basis for price disclosure to FLSI's clients.

(d) Other potential sources of information relevant to determining the price of the Fund Units

i. Introduction

[118] Mr. Sutton was adamant that there was an active market, and that he did not need to resort to other factors in his "hierarchy" (described in paragraph [89] above) to ascribe an appropriate price. Indeed, when asked whether yield would be one possible consideration, he stated that yield would be "key… if you have to go that far in the hierarchy, but as I said, if you satisfy number 1, trading activity, then you don't have to look at the other items."[26]

[119] However, he also testified that he did consider yield and other factors "from a comfort point of view",[27] although it is not clear how often or how consistently he did so.

ii. Yield

[120] With respect to yield, Mr. Sutton stated that he relied upon the consistent high yields paid by each of the Funds to support the price of $1.00. All of the Fund Units yielded between 7% and 9%, which rates were substantially higher than the prevailing interest rates. During his interview with IIROC, Mr. Sutton asserted that the $1.00 price was supported by the fact that interest rates for the Fund Units were higher than rates for comparable products in the market. However, when asked if the rates supported a price of more than $1.00, Mr. Sutton responded categorically that it "isn't for me to say."[28]

[121] We are unable to reconcile that disavowal with Mr. Sutton's acceptance of responsibility for ascribing an appropriate price. To our knowledge, Mr. Sutton offered no basis for being in a position to conclude from the yield that $1.00 was an appropriate price but not being in a position to reach a conclusion about any price greater than $1.00.

iii. Value of underlying real estate

[122] In September 2009, Mr. Sutton obtained a report regarding the value of the real estate underlying the promissory notes held by the three Funds. The report indicated that the value of the assets exceeded the Funds' liabilities. However, contrary to Mr. Sutton's assertion that this four-page report constituted an "appraisal", it is a "Broker Opinion of Value" from a "national mortgage banking firm".

[123] Mr. Sutton ought not to have derived any comfort from the report, for a number of reasons. Significantly, the report assumed future redevelopment of the subject properties. It provided a stabilized, *pro forma* value assuming completion of a capital improvement program and reflected "post-rehab" rental rates, a fully recovered U.S. economy and a fully stabilized real estate market. The report's author described this as "essentially a best case scenario." Further, the report omits any assumptions about future rental rates and the cost of the necessary

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[26] Exhibit 1, Tab 31 and Exhibit 2, Tab 8, Transcript of the testimony of Brian Sutton, January 19, 2017, at p 144, lines 20-25.

[27] Exhibit 1, Tab 31 and Exhibit 2, Tab 8, Transcript of the testimony of Brian Sutton, January 19, 2017, at p 143, lines 18-19.

[28] Exhibit 1, Tab 16, Transcript of the testimony of Edward Varela, January 17, 2017, at p 184, lines 20-21.

capital improvements. The report did not even purport to provide a fair market, present day value of the underlying real estate.

iv. Financial statements

[124] Mr. Sutton highlights the fact that he reviewed some financial statements. In order to determine how much comfort (if any) he ought to have derived from this review, we must examine the extent to which he reviewed financial statements of three categories of entities:

a. the Funds themselves;

b. Master Sherman and Master Texas, whose debts to the Funds constituted the Funds' only material assets; and

c. WALP, which by December 31, 2009, was the parent partnership of Master Sherman and Master Texas.

[125] With respect to the Funds themselves, Mr. Sutton had no financial statements available to him for the First Leaside Fund or the Wimberly Fund. He did review the Properties Fund's 2009 and 2010 audited financial statements, although these statements were not available until May 2011, almost at the end of the Material Time.

[126] While the audit opinion in those financial statements was "clean", notes to the statements warned that the fair value of the Master Sherman promissory notes held by the Fund (*i.e.*, the Fund's only material assets) "could not be reasonably calculated as no comparable commercial terms are available", and that:

> …the promissory notes receivable and virtually all of the interest income are from Master Sherman. The loss of interest income or the inability of Master Sherman to repay the promissory notes receivable could have a material adverse effect on the Fund's results of operations and financial position.

[127] Notwithstanding these notes in the Properties Fund's financial statements, Mr. Sutton did not review the underlying financial statements for Master Sherman (which, similarly, were not even available until May 2011). Those statements disclosed operating losses, cash flow deficiencies and a partners' deficiency of $8.7 million in 2010. Master Sherman could not service its debt obligations from its cash flows, and it used capital injections from the Fund itself to enable the Fund to make interest payments to unitholders. Mr. Sutton testified that he took comfort from the fact that payments to unitholders were made consistently. However, the Master Sherman financial statements showed that these payments were not sustainable.

[128] We were not directed to any evidence that Mr. Sutton ever reviewed financial statements for Master Texas, if indeed those financial statements even existed.

[129] Finally, Mr. Sutton did not, during the Material Time, review any financial statements of WALP. Statements for the years ended December 31, 2009 and 2010 were not issued until September 2011, and were therefore not available to Mr. Sutton during the Material Time, except for approximately one month at the end of that period. However, WALP's financial statements as at December 31, 2008, which included results from Master Texas (but not Master Sherman), were

issued in September 2009. Mr. Sutton did not review those financial statements during the Material Time. Had he done so, he would have seen a partners' deficiency of more than $41 million, and the following note:

> There is significant doubt about the appropriateness of the use of the going concern assumption because the Partnership does not have sufficient cash on hand to meet its obligations…
>
> There is no certainty that management will raise sufficient capital to permit the Partnership to continue its operations and discharge its liabilities when due.[29]

[130] Given the timing of the issuance of the various financial statements, Mr. Sutton could not have derived any comfort from them for most of the Material Time. Further, given the limitations of the Properties Fund's financial statements, he ought not have derived any comfort from them even following their release.

v. Sloan Report

[131] Following 2011 discussions with IIROC about the pricing of the Fund Units, FLSI hired Sloan Partners LLP, an independent accounting firm, to prepare the Sloan Report referred to in paragraph [60] above. The Sloan Report stated:

> Based on our review, nothing has come to our attention that causes us to believe that the promissory notes receivable is not, in all material respects, less than the book value disclosed in the audited financial statements (of First Leaside Properties Fund as at December 31, 2010).

[132] The Sloan Report was a review, not an audit. There is no detail as to what information was supplied and what analysis was undertaken. The report was delivered in June 2011, very near the end of the Material Time. It could not have provided any comfort to Mr. Sutton throughout virtually the entire period, and ought not to have provided meaningful comfort even after its issuance.

vi. Parker Simone Report

[133] The Parker Simone Report, referred to in paragraph [74] above, concluded that the valuation methodologies of FLSI appeared in all material respects to be in compliance with IIROC Internal Policy 7. It went on to state that the methodologies appeared appropriate for pricing the fair value estimate of the Fund and management had complied with its policy under Section 3.8.3. Specifically, the report stated that there appeared to be sufficient evidence of an active secondary market during 2009-2011 and that "it would not appear unreasonable to accept that the Dealer Member is in compliance with the pricing methodologies underlying the policy provided by management".[30]

[134] The report relied on a one-page trading summary provided by Mr. Sutton. The summary presented only three-year averages and did not break down trading by month, nor did it identify which trades involved FLSI or any other affiliate of the FL Group. We find it to be of limited support for Mr. Sutton's view.

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[29] Exhibit 2, Tab 38, WALP financial statements as at December 31, 2008, at p 710-711.
[30] Exhibit 1, Tab 6 and Exhibit 2, Tab 11, Parker Simone Report, at p 23.

(e) Conclusion as to pricing

[135] Mr. Sutton maintains that he priced the three Funds appropriately, and as set out in the PPM he drafted.

[136] We disagree. We find that there was no "active market" for the Fund Units. Such market as existed was wholly insufficient to provide reliable information for investors to make fully informed decisions. The trade prices were not determined through market forces, and the recency and frequency of the trades were insufficient.

[137] By Mr. Sutton's own evidence, he went no further than the "active market" question in assessing whether $1.00 was an appropriate price. However, to the extent he claims to have derived "comfort" from other sources, the sources he cites ought not to have given him any such comfort.

[138] We therefore find that the pricing approach adopted by Mr. Sutton did not fall within a reasonable range of possible approaches.

3. Role played by Mr. Sutton

[139] Our conclusion that the way in which Mr. Sutton applied the pricing methodology was unreasonable does not end the matter. As we discussed above in paragraphs [80] to [83], the rule that Mr. Sutton is alleged to have contravened relates to the obligation of a CFO to monitor adherence to the firm's policies and procedures so as to provide reasonable assurance that the firm is complying with IIROC's financial rules. We therefore return now to Mr. Sutton's submission that this obligation, which is to ensure "reasonable compliance", somehow modifies the standard by which Mr. Sutton's conduct should be measured.

[140] We reject that submission.

[141] If Mr. Sutton had truly been in an oversight role with respect to this task, and in an oversight role alone, then our analysis would align more closely with his submissions. Sensibly, an individual in an oversight role is typically afforded some latitude, because that person is not expected to be a guarantor of perfect compliance by the person whom she or he oversees. Put another way, the person in the oversight role may not be expected to review each and every transaction. The imposition of such an expectation could cause a significant and unnecessary burden and duplication of effort. It is for this reason that many regulatory requirements contemplate the development of systems designed to provide **reasonable assurance** of compliance by those carrying out the original tasks.

[142] An example of the contemplated latitude may be found in Member Regulation Notice MR0435, issued by Staff of the Investment Dealers Association of Canada (IIROC's predecessor organization) and other regulators in late 2006. The Notice, titled *The Role of Compliance and Supervision*, describes its purpose as being to provide "SRO expectations of the compliance function at Members".[31] The Notice explicitly distinguishes between the compliance function on the one hand (independent oversight, but without decision-making authority over the activity in question) and the supervisory function on the other (authority for day-to-day management). This distinction is even more pronounced when contrasting the

[31] *The Role of Compliance and Supervision,* IDA MR0435 (30 November 2006) at p 1.

compliance function with the individual who is actually carrying out the task and therefore subject to supervision, as opposed to the person doing the supervising.

[143] Mr. Sutton's reliance on the Notice, and on the principles set out in it, is misguided. No one was overseeing Mr. Sutton's work of ascribing a price to be communicated to unitholders. Mr. Sutton was under an obligation to do that work appropriately, as would anyone else charged with that task. His obligation was neither more nor less onerous than the obligation that would have been imposed on a hypothetical individual carrying out the same task, with respect to whom Mr. Sutton would have had oversight responsibility. Whatever range of reasonable pricing approaches would have been available to such an individual was equally available to Mr. Sutton. The boundaries of the range of reasonable pricing approaches are independent of the identity or title of the person who carries out the pricing task.

[144] It is illogical, and contrary to the important objective of investor protection, to further broaden the range of reasonable pricing approaches simply because the person who is assessing the propriety of the price also happens to be the CFO. Mr. Sutton highlights the words "reasonable assurance" in Dealer Member Rule 38.6(c), but the determination of how much assurance is "reasonable" must be made in context. In this context, given that Mr. Sutton was both actor and overseer, it is unreasonable for him to benefit as CFO from an incremental degree of latitude beyond that afforded the person who ascribes an appropriate price. It is reasonable to expect that he would be no less diligent in overseeing his own pricing (an illusory conceptual separation of responsibilities) than he would be in doing the pricing in the first place.

[145] Accordingly, in the circumstances of this case, we conclude that Mr. Sutton's obligation to monitor, as imposed by Dealer Member Rule 38.6(c), required him to apply the same level of scrutiny as he was required to apply to his task of ascribing an appropriate price. A choice of pricing approach outside the range of reasonable approaches was therefore, by definition, a failure to provide reasonable assurance that FLSI was complying with IIROC's financial rules.

[146] It follows that we reject Mr. Sutton's fifth basis of complaint about the Liability Decision, *i.e.*, that the IIROC panel effectively held him to a strict liability standard, by finding a breach despite the absence of an "intent to do wrong". As explained above, the obligation to provide accurate price information to unitholders allows for a reasonable range of pricing approaches. A particular approach is either reasonable or it is not; the provision of unreasonable price information by an individual to unitholders can support a breach even absent unfavourable conclusions about the individual's mental state in selecting the unreasonable approach.

D. Expert evidence

[147] Mr. Sutton submits that the IIROC panel erred in reaching its ultimate conclusions in the absence of expert evidence "on the standard of care that was required to be met by a reasonable CFO for an IIROC dealer in the circumstances."[32] He further submits that the panel erred "in reversing the onus

[32] Sutton's written submissions (liability) at para 149(b).

of proof and requiring that Mr. Sutton adduce expert evidence of the standard he was required to meet as CFO".[33]

[148] Our earlier finding, that the IIROC panel's evidence-related errors warrant our substituting our own decision, obviates the need to consider whether that panel also erred with respect to the need for expert evidence. However, Mr. Sutton makes the same argument to us about our own ability to reach certain conclusions without the benefit of expert evidence led by IIROC Staff. We must therefore consider that submission in the context of this application.

[149] We begin our analysis by noting that Mr. Sutton submits that expert evidence was required about the standard of care of "a reasonable CFO". We do not accept that framing of the issue.

[150] As explained above in paragraphs [141] to [144], we find that on the facts of this case, any discussion about the standard of care of a CFO is inapplicable. Mr. Sutton himself was the person who was carrying out the task of determining the price to be shown on client statements. He was not supervising such a person, nor was he monitoring such a person.

[151] We therefore reject the notion that there is a need for expert evidence about the standard of care of a CFO. On the facts of this case, that issue simply does not arise.

[152] Given that conclusion, we need not, for the purposes of this decision, address Mr. Sutton's submission that neither the IIROC panel nor this panel is qualified to decide for itself whether his conduct met a standard of care for CFOs. However, the point was fully argued and the general question arises from time to time before SRO panels and before the Commission. For those reasons, and because during the hearing before us Mr. Sutton's counsel provided a Court of Appeal for Ontario decision on the point, we consider it important to address the issue.

[153] Specialized administrative tribunals may draw upon their own expertise. They may assess evidence and draw inferences within the boundaries of that expertise, without the assistance of an expert. It is for a tribunal to determine whether it needs that assistance.[34]

[154] While Dealer Member Rule 38.6(c), the rule that Mr. Sutton is alleged to have contravened, imposes an obligation on Chief Financial Officers specifically, the obligation relates to the member firm's compliance with IIROC's financial rules. The core task at issue in this case is the pricing of securities. It is not an esoteric accounting question such as the determination of the appropriate accounting treatment of complex corporate actions. The assessment of alternative methods of valuing securities, and in particular determining whether there is an active market sufficient for that purpose, are questions that are squarely within the expertise of this Commission. We do not require the assistance of an outside expert.

[155] Moreover, even if we had accepted the fiction that Mr. Sutton as CFO (*i.e.*, with oversight responsibility) was one step removed from Mr. Sutton as the person who determined the appropriate price in the first place, no expert evidence is

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[33] Sutton's written submissions (liability) at para 149(b).

[34] *Sammy (Re)*, 2017 ONSEC 21, (2017), 40 OSCB 4877 at paras 36-37; *R v Abbey*, [1982] 2 SCR 24 at p 42, cited in *Northern Securities (Re)*, 2012 IIROC 35 at para 6.

necessary about the standard for someone in that kind of oversight role. The nature of the CFO role in the context of IIROC's financial rules is substantially similar to that of a CCO in the context of IIROC's trading rules, for example. In both cases, the central question is what constitutes reasonable assurance as to the propriety of another's activity. Again, that question is one that is squarely within the expertise of a securities regulator, and the sufficiency of that expertise is unaffected in this case by the fact that the individual involved is a CFO and not a CCO.

[156] Finally on this point, during the hearing before us, counsel for Mr. Sutton produced the 1983 decision of the Court of Appeal for Ontario in *Reddall and College of Nurses of Ontario (Re)*,[35] in which the court allowed in part an appeal from the decision of a disciplinary tribunal. Mr. Sutton submits that this decision, applied to the present case, requires the conclusion that without the benefit of expert evidence, we cannot reach the conclusions sought by IIROC Staff.

[157] The decision was provided to IIROC Staff only the day before the hearing. After hearing submissions during the hearing, we are not of the view that the parties had the opportunity to fully argue the implications of the decision, including the effect of any subsequent decisions that considered it. Having said that, it appears that the decision should be distinguished from the present case, given a central finding by the court that the tribunal in question was subject to a specific statutory limitation regarding evidence and findings, which limitation would not apply to this Commission. Further, we observe that the conclusion sought by Mr. Sutton on this point would, in our view, run counter to the cases cited above and to the well-established authority that the admission of expert evidence depends on, among other things, necessity in assisting the trier of fact.[36]

[158] We therefore conclude that there were no issues before the IIROC panel, and there are no issues in this proceeding before us, with respect to which expert evidence was or is required.

E. Sanctions

1. Introduction

[159] In the Sanctions and Costs Decision, the IIROC panel:

a. ordered a reprimand as requested by IIROC Staff;

b. imposed a $25,000 fine instead of the $100,000 fine requested by IIROC Staff; and

c. rejected IIROC Staff's request for a permanent prohibition on Mr. Sutton's approval for registration as a CFO with an IIROC dealer member, instead ordering no prohibition at all.

[160] IIROC Staff applies to the Commission for a review of that decision. IIROC Staff asks for the sanctions originally requested, except that it now seeks a prohibition of between three and five years as opposed to a permanent prohibition. Further, while IIROC Staff originally requested that the prohibition be against Mr. Sutton's

[35] 1983 CanLII 1947.
[36] *R v Mohan*, 1994 CanLII 80, [1994] 2 SCR 9.

approval for registration as a CFO with an IIROC Dealer Member,[37] its request before us is not limited to registration in a particular capacity.[38]

2. Analysis

[161] We begin our analysis regarding sanctions with a review of the various principles and factors that we consider to be relevant in determining an appropriate result. The principles and factors reflected in the *IIROC Sanction Guidelines* are substantially similar to the sanctioning factors considered by the Commission in its decisions.[39]

(a) Importance of timely and accurate disclosure

[162] As we have explained above, an important principle at the centre of this matter is the need for "timely, accurate and efficient disclosure of information", as prescribed by subparagraph 2(i) of section 2.1 of the Act. Disclosure is a cornerstone of securities regulation,[40] and a failure of disclosure undermines confidence in our capital markets.[41] In the context of this case, proper disclosure would have enabled existing and potential investors to have adequate and reliable information.

[163] This principle is reflected in section 3.8.3 of FLSI's PPM, which in turn reflected the requirements of IC Policy 7. We agree with the IIROC panel's description that "the position Mr. Sutton espoused that it was an active market undercuts the very purpose underlying the regulatory objective of making sure that the investors had the information necessary to make informed investment decisions."[42]

[164] Pricing unlisted securities is not an exact science. However, as we have discussed, Mr. Sutton's approach in this case falls outside a reasonable range of approaches. His failure to follow a reasonable methodology denied existing and potential unitholders the information that they required and to which they were entitled. We consider this to have been a serious breach of the requirement to make timely and accurate disclosure.

(b) Mr. Sutton's seniority and experience

[165] This Commission has often stated that registrants are held to a higher standard of conduct than are non-registrants, given the level of trust that is placed in registrants by investors.[43] This is particularly so for registrants who are in senior positions and/or who have lengthy experience. Investor confidence in the capital markets depends in part on senior registrants diligently exercising their gatekeeper role.

[166] We agree with the following comments of the IIROC panel in *Trenholm (Re)*:

> Gatekeeper obligations have been imposed by courts because registrants are in a unique position, and even better

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[37] Sanctions and Costs Decision at para 3(i).
[38] IIROC's written submissions (sanctions) at paras 4(a)(ii), 72(c).
[39] *Northern Securities Inc. (Re)*, 2014 ONSEC 27, (2014), 37 OSCB 8535 at para 140.
[40] *Coventree Inc. (Re)*, 2011 ONSEC 38, (2011), 35 OSCB 119 at para 48.
[41] *Home Capital Group Inc. (Re)*, 2017 ONSEC 32, (2017), 40 OSCB 7136 at para 3.
[42] Liability Decision at para 62.
[43] See, *e.g.*, *Pro-Financial Asset Management (Re)*, 2018 ONSEC 18, (2018), 41 OSCB 3512 at para 100.

than regulators, to effectively monitor market activities and to apply their knowledge to spot any potential impropriety.[44]

[167] Mr. Sutton has had a 37-year career in the capital markets, including numerous positions at senior levels. His position as CFO at FLSI was among the very highest positions one could occupy at a dealer. His experience and his seniority impose a greater burden on him than would apply to a non-registrant or to a new entrant. The capital markets, the investing public, FLSI clients, and securities regulators are entitled to expect Mr. Sutton to meet that high standard.

(c) Mr. Sutton's unblemished record

[168] While Mr. Sutton's long career in senior positions imposes a greater obligation on him, it is also noteworthy that this is the first time throughout his lengthy career that he has been subject to disciplinary action. We consider this to be a mitigating factor in Mr. Sutton's favour, especially since a primary objective of sanctions is to protect the investing public. In determining what sanctions are necessary to achieve sufficient protection, we have regard to Mr. Sutton's previously unblemished record as an indicator of the likelihood of future breaches.

[169] That record cannot be determinative, however. In this case, we struggle to understand how an individual of Mr. Sutton's seniority and experience could have regarded the available trading history as a sufficient and reliable indicator of an active market. His failure to see the red flags, and to take meaningful additional steps to ascribe an appropriate price to the Fund Units, undermines any confidence we have that there is little risk of a future lapse.

(d) Significance of Mr. Sutton's role as the sole gatekeeper

[170] Mr. Sutton's failure is particularly concerning to us, because of the fact that Mr. Sutton was effectively FLSI's only independent control with respect to communicating appropriate pricing information. As discussed above, he was responsible for ascribing an appropriate price. He was not overseeing the work of another, and his work was not supervised by a more senior person.

[171] There was no true compensating control. Mr. Sutton was the sole gatekeeper. With his experience, he ought to have had a sound appreciation for the associated risk. If he did have a sound appreciation, then he failed to respond accordingly.

[172] We consider this failure to have been an aggravating factor.

(e) Harm

[173] Mr. Sutton submits, correctly, that there was no specific evidence of actual detrimental reliance or pecuniary loss incurred by any investors. However, we do not accept the conclusion that he says follow from that, *i.e.*, that there was no

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[44] [2009] IIROC No. 40 at para 28. Mr. Sutton noted that the decision goes on to find that for disciplinary cases, the "conduct at issue must amount to something more than mere inadvertence or negligence" (para 29) and that "[n]egligence is not likely to be a basis for discipline unless it is gross or habitual, or both" (para 30). We do not believe those statements are an accurate reflection of the law, and we decline to adopt that standard.

harm. As noted above, existing and potential investors were deprived of the opportunity to make a fully informed decision. It follows that at a minimum, investor funds were subject to a risk that the investors did not knowingly assume. It also follows that at least some investors likely suffered a financial loss, and it would be no answer to that to say that some other investors might have realized a gain, even if that aggregate gain were equal to or greater than the aggregate loss.

[174] In addition, his failure caused a more general harm to the capital markets, by undermining confidence in those markets.

[175] As a result, we categorically reject the IIROC panel's finding that it heard "no evidence in the liability phase that would support a conclusion that Mr. Sutton's breach caused some measure of harm to investors."[45] Evidence of specific and quantifiable harm would be admissible and relevant, but the absence of such evidence does not support a conclusion that there was no such harm. The harm we have described above is a reasonable inference to be drawn from the circumstances, and is a conclusion we have no difficulty reaching on the balance of probabilities.

(f) Absence of dishonest or intentional misconduct

[176] The IIROC panel emphasized its finding that Mr. Sutton's breach was an "honest mistake". Mr. Sutton urges that characterization upon us, and submits that an honest mistake cannot justify a prohibition against approval with IIROC.

[177] The term "honest mistake" may be accurate in a literal sense, because there is no evidence that Mr. Sutton was dishonest, and as we have found, his chosen pricing methodology was indeed a mistake, in that it was unreasonable and unacceptable. However, we do not adopt the term, especially to the extent it implies an innocent mistake or mere inadvertence.

[178] In our view, there is no evidence in the record that would lead us to conclude that Mr. Sutton's mental state should be either an aggravating or a mitigating factor. We recognize the absence of any deliberate misconduct, but we consider his conduct to fall well short of the necessary standard. In our view, Mr. Sutton's pricing approach was a serious mistake.

[179] An absence of deliberate misconduct does not lead to the conclusion that no prohibition against registration is warranted. This Commission has previously rejected the notion that "only matters of integrity merit periods of suspension".[46]

(g) Repetition over time

[180] Repetition of improper behaviour typically acts as an aggravating factor. In such cases, however, the *IIROC Sanction Guidelines* caution against imposing a cumulative sanction that is excessive; rather, a global approach may be appropriate.[47] Ultimately, the total sanction must be proportionate to the overall misconduct.

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[45] Sanctions and Costs Decision at para 23.

[46] *Pariak-Lukic (Re)*, 2015 ONSEC 18, (2015), 38 OSCB 5755 at paras 98-102, aff'd *Pariak-Lukic* DivCt; *Sterling Grace & Co. Ltd. (Re)*, 2014 ONSEC 24, (2014), 37 OSCB 8298.

[47] *IIROC Sanction Guidelines* at s 3.

[181] In one sense, Mr. Sutton's misconduct in this case was repeated monthly over a two-year period. On the other hand, it could be argued that the contravention has one single root, *i.e.*, one inappropriate exercise of judgment about pricing methodology, that manifested itself a number of times.

[182] In our view, this case lies somewhere between the two. Mr. Sutton's breach was not confined to a single incident. As time passed, and especially as the trading became less frequent, the validity of Mr. Sutton's decision about an active market diminished. He had an ongoing responsibility to judge whether the chosen basis for pricing was appropriate, and that judgment had to be renewed monthly and independently in light of changing circumstances.

[183] We consider this repetition to be an aggravating factor, although we place less weight on it than we would in a case of repeated deliberate misconduct.

(h) General deterrence

[184] Deterrent sanctions are prospective and preventive. They are aimed at potential wrongdoers.[48] Ensuring that sanctions are proportionate to misconduct, and ensuring that the sanctions are sufficient to deter others from engaging in misconduct, serves to protect investors and other market participants against future harm.

[185] While we must be cautious never to place too much weight on the need for general deterrence, it is an important principle that is particularly relevant in this case. Persons in positions similar to Mr. Sutton's must clearly understand the responsibility that they have accepted, and that a failure to discharge that responsibility diligently can lead to serious consequences.

(i) Specific deterrence

[186] Mr. Sutton submits that this process, including a finding that he contravened the rules about which he claims to be an expert, is "devastating".[49] We understand that he believes that his reputation is at stake, and we consider that belief to be a reasonable one.

[187] In our view, the mere existence of this decision and these reasons will have some effect as a specific deterrent. However, to impose token sanctions would be to send a message to Mr. Sutton that a significant failure need not attract a meaningful response. We are of the view that there is a need for sanctions proportionate to the failure.

[188] We do not accept the IIROC panel's finding that "a reprimand is at least as significant as a suspension and in fact may carry more opprobrium with it."[50] IIROC Staff's request for sanctions did not characterize a reprimand and a prohibition as alternatives. The two sanctions may be ordered together and it cannot be doubted that a reprimand accompanied by a suspension would be viewed by Mr. Sutton (and others) as being more severe than a reprimand alone.

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[48] *Cartaway Resources Corp. (Re)*, [2001] 1 SCR 672 at paras 52 and 60.
[49] Hearing transcript, at p 156, lines 9-10.
[50] Sanctions and Costs Decision at para 28.

(j) Conclusion as to sanctions

[189] As we have explained, we consider Mr. Sutton's lengthy unblemished record to be a mitigating factor. We consider the following to be aggravating factors:

a. the seriousness of the contravention, given the particular importance of timely and accurate disclosure;

b. Mr. Sutton's seniority and experience;

c. the significance of Mr. Sutton's role as the only true control at FLSI with respect to assessing the appropriateness of reported prices; and

d. the repetition over two years of the failure to conduct a proper assessment of the reported prices.

[190] It is rare that substantially similar precedents can be found to assist in determining appropriate sanctions. That is particularly true here, given the unusual facts of this case. Having said that, we note that the present circumstances are, in part, somewhat comparable to those in *Stevenson (Re)*,[51] in which an IIROC panel approved a settlement agreement relating to the individual respondent's failure to exercise his gatekeeper function (by failing to adequately supervise the opening of about twenty accounts), among other contraventions. The agreed-upon sanctions included a twelve-month suspension from approval, along with an obligation to complete various courses and examinations, a fine of $50,000, and a requirement of on-site close supervision. In approving the settlement, the IIROC panel noted that "no harm was done", and that the respondent had a 40-year "spotless disciplinary record".[52]

[191] The range of contraventions in *Stevenson* is broader than the single (but repeated) contravention in this case. However, the range of sanctions in that case is correspondingly broad, and some of the aggravating factors present in this case and cited above were not present in *Stevenson*. Given the distinguishing factors, given that *Stevenson* was a settlement as opposed to a contested hearing, and given that ten years have passed, we think it appropriate and in the public interest to impose a similar fine, and a somewhat longer prohibition.

[192] We also refer to the Commission's decision approving a settlement in *Mark Bonham (Re)*,[53] in which the individual respondent admitted to having carried out manual pricing of securities held in a mutual fund, without proper documentation or a consistent and proper methodology. The Commission noted that this conduct posed a risk to the investing public,[54] and approved the agreed-upon sanctions, which included a three-year suspension of registration, a three-year ban on the individual respondent acting as an officer or director of a registrant, and a three-year cease-trade order against the individual respondent, except for trading in his personal accounts. The settlement also called for a voluntary payment of $50,000, plus costs of $150,000.

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[51] 2008 IIROC 24 (***Stevenson***).
[52] *Stevenson* at para 12.
[53] (2002), 25 OSCB 5741 (***Mark Bonham***).
[54] *Mark Bonham* at para 6.

i. Prohibition against approval as an IIROC registrant

[193] In our view, taking into account all the circumstances and in particular the aggravating and mitigating factors listed above, a prohibition against Mr. Sutton's approval for some period is warranted. That result is consistent with the authorities we have cited above and is proportionate to the conduct at issue. It is also consistent with the *IIROC Sanction Guidelines*, which advise that a suspension should be considered where, as in this case, there has been one or more serious contraventions, or where, as in this case, the misconduct in question has caused some measure of harm to investors or the securities industry as a whole.[55]

[194] We must determine the appropriate scope and length of that prohibition.

[195] As noted above, IIROC Staff's requested prohibition against approval as a registrant changed from the IIROC hearing to the hearing before us. IIROC Staff explicitly advised us that while it had sought a permanent prohibition before the IIROC panel, it now seeks a three- to five-year prohibition, which on further reflection it considers to be a sufficient sanction.

[196] On the other hand, despite this request for a shorter prohibition, the scope of the requested prohibition appears to have expanded, from one relating only to Mr. Sutton being a CFO, to one not confined to a particular role. While this broader scope is apparent from IIROC Staff's written submissions, it was not explicitly addressed during the hearing, and we received no written or oral submissions as to why this broader scope would be appropriate.

[197] Under the circumstances, we are not prepared to accede to IIROC Staff's request in this regard. In fairness to Mr. Sutton, he might have addressed this point had IIROC Staff argued it before us. Further, we are satisfied that a three-year prohibition against Mr. Sutton being a CFO with an IIROC Dealer Member serves the appropriate protective purposes, including both general and specific deterrence.

ii. Fine

[198] IIROC Staff requests a fine of $100,000. We conclude that a meaningful fine is warranted, but we consider $100,000 to be excessive, especially in light of the three-year prohibition we have decided to impose.

[199] We observe that in enforcement cases before the Commission, administrative penalties of approximately $100,000 are sometimes imposed where a respondent has engaged in deliberate misconduct, including fraud. While the conduct here is serious, it lacks that character. In our view, a $50,000 fine is appropriate and is proportionate to the conduct at issue.

iii. Reprimand

[200] We grant IIROC Staff's request for a reprimand. We consider these reasons for decision as adequately expressing that reprimand.

F. Costs

[201] At the IIROC hearing, IIROC Staff requested a costs order in the amount of $50,000. In the Sanctions and Costs Decision, the IIROC panel declined to order

[55] *IIROC Sanction Guidelines* at s 5.

any costs payable by Mr. Sutton, but gave no reasons for that conclusion. As part of IIROC Staff's application for a review of the Sanctions and Costs Decision, IIROC Staff asks us to order the costs originally requested. IIROC Staff advised that its recorded costs were $223,714, and Mr. Sutton does not take issue with that amount. He does submit that we ought not to order costs.

[202] Like the Commission, IIROC is a self-funded body. The Commission has regularly affirmed the principle that the cost of enforcement proceedings ought not to be borne in their entirety by the industry as a whole, and that it is appropriate for an unsuccessful respondent to bear a portion of the costs incurred.[56]

[203] The portion of costs that IIROC Staff requests in this case is consistent with costs orders typically made by the Commission in its own enforcement proceedings. IIROC Staff was entirely successful in the eight-day hearing before the IIROC panel and in the one-day hearing before us. We conclude that it is appropriate to order Mr. Sutton to pay costs in the amount of $50,000.

VI. CONCLUSION

[204] For the reasons set out above, we find that the IIROC panel erred in its conduct of the liability hearing before it, and that these flaws constituted an error of law that warrants our substituting our own decision for that of the IIROC panel.

[205] We conclude that Mr. Sutton breached IIROC Dealer Member Rule 38.6(c), and we will issue an order:

a. prohibiting, for a period of three years, Mr. Sutton's approval as a CFO with an IIROC dealer member firm;

b. requiring Mr. Sutton to pay a $50,000 fine to IIROC; and

c. requiring Mr. Sutton to pay costs in the amount of $50,000 to IIROC.

Dated at Toronto this 14th day of August, 2018.

"Timothy Moseley"
Timothy Moseley

"Deborah Leckman"
Deborah Leckman

"Lawrence Haber"
Lawrence Haber

[56] See, *e.g.*, *2241153 Ontario Inc. (Re)* 2016 ONSEC 10, (2016), 39 OSCB 2733 at para 16.