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Photo of Izzy Bessner, taken by Ellen Bessner

Getting out of Dodge is not the answer

Advisors who leave the industry to avoid investigations and hearings suffer more severe penalties

By Ellen Bessner and Aaron Gold BABIN BESSNER SPRY LLP

Registered advisors are mistaken if they believe that, after committing a regulatory breach, they can avoid penalties by leaving the securities industry. In fact, the penalties will invariably be worse.

A considerable number of cases brought by the self-regulatory organizations ("SROs") are uncontested because, instead of cooperating with the SRO's investigators and lawyers throughout the investigation and attempting to negotiate a reasonable penalty, advisors choose to be unresponsive and uncooperative. A hearing is then conducted in the advisor's absence, and SRO staff prove the breaches and obtain more severe penalties. Because the registrant didn't appear at the investigatory interview or hearing, additional penalties are imposed for their "failure to cooperate." These uncontested cases result in the most significant monetary penalties and are commonly accompanied by a permanent ban.

These monetary penalties often remained uncollected, until a number of provinces amended their respective securities legislation to permit the SROs to enforce these sanctions in court – a game changer for the SROs, as well as the unassuming advisor.

In March 2017, the Ontario government announced its intention to introduce new measures to assist in the enforcement of sanctions ordered by SROs. Bill 127 came into effect on May 17, 2017, amending section 151 of the *Securities Act*[1] to give the Investment Industry Regulatory Organization of Canada ("IIROC") and the Mutual Fund Dealers Association of Canada ("MFDA") powers to enforce their decisions by entering their orders as judgments of the Superior Court of Justice. If registrants left the securities industry, but had income or assets in the province, their wages could be garnished and their assets seized to satisfy the SRO's order.

It gets worse.

In a decision released last week,[2] the Court held that these legislative powers apply even if the conduct at issue in the hearing panel's decision occurred **before** the effective date of the legislation. So, if you breached the rules in Ontario before May 2017, the SRO could have the penalty entered as a court order, even though the breach occurred before the law was amended. Here are the details of the case.

Background: The Defendant, Hong Lam, was an Approved Person with the MFDA. In January 2016, Lam resigned from his position as a mutual fund representative and branch manager at a registered dealer.

In April 2016, the MFDA launched an investigation into Lam's business and potential breaches of various MFDA Rules. These included allegations that he had referral arrangements with certain companies offering syndicated mortgages, conducted business outside the accounts and facilities of the Member dealer, had other gainful employment that was not previously disclosed to or approved by the Member, and misled the Member during an internal interview.

Lam refused to cooperate with the MFDA investigators, failed to respond to requests for information or make representations to avoid a possible hearing (a "Wells Notice"), and did not appear or otherwise participate in the MFDA hearings. Like many advisors in Lam's position, the reasons for judgment note that he appeared to have chosen this course of conduct on the understanding that the MFDA would be unable to collect any monetary penalty.

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[1] R.S.O. 1990, c. S.5, s. 151.

[2] *Mutual Fund Dealers Association of Canada v. Lam*, 2022 ONSC 2269.

On October 19, 2018, the MFDA hearing panel released their decision and reasons, ordering that Lam be permanently banned from registration with an MFDA Member dealer, a $250,000 fine, and $10,000 in costs (the "SRO Order"). Now you might be thinking, these are serious breaches and therefore, would have attracted a permanent ban and significant penalties. However, we assure you that Lam could have negotiated a less significant monetary penalty had he cooperated.

In the interim, section 151 of the *Securities Act* was amended in May 2017. The SRO Order was entered on May 22, 2019, which the MFDA sought to enforce by filing a writ of seizure and sale, a notice of garnishment, and by conducting an examination to determine the location of his assets so they could be seized.

The Motion: Lam brought a motion to set aside the court order, arguing that it was entered without jurisdiction and was otherwise invalid on the basis that the May 2017 amendments were presumed not to apply retrospectively to conduct pre-dating the effective date of the legislation. He also argued that his contract with the MFDA ended upon his departure from the industry, and therefore he could not be subject to enforcement powers provided to the MFDA subsequent to his resignation.

Krawchenko J. rejected both arguments. On the first point, he noted that the amended section 151 does not apply retrospectively to prior events, as the provision is triggered by the issuance of the hearing panel's decision rather than the conduct that led to the hearing itself. In *obiter*, he commented that, even if section 151 was being applied retrospectively, the presumption against retrospective application did not apply, citing a long-stating exception for statutes that are purely procedural.

Krawchenko J. also rejected the contractual argument, reasoning that Lam had agreed to remain subject to the jurisdiction of the MFDA for five years after ceasing to be an Approved Person and to be subject to the relevant securities legislation as amended from time to time.

The Court accordingly declined to set aside the court order.

Takeaway: The Court's decision in *Lam* confirms the scope of the SROs' powers under section 151 of the *Securities Act*. More broadly, it serves as a cautionary tale for advisors seeking to rely on a restrictive interpretation of securities legislation, and highlights the importance of cooperating with the regulators throughout the disciplinary proceedings.

While registrants might be able to "get out of Dodge" with regard to the SROs, they cannot do so with the courts. It is far better for registrants to negotiate the best deal they can with SRO staff than be stuck defending themselves in court when the judge is asked to enforce a significant penalty imposed in their absence.

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