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**CASE SUMMARY # 200807**  
November 19, 2008

# MFDA Case Summary

## Enforcement

This case summary was prepared by Staff of the MFDA.

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### **Hearing Panel Approves Settlement With Portfolio Strategies Corporation**

**Nature of Proceeding**

A Hearing Panel of the Prairie Regional Council of the Mutual Fund Dealers Association of Canada (“MFDA”) has approved a Settlement Agreement between the MFDA and Portfolio Strategies Corporation (“PSC”), a Member of the MFDA.

**By-Laws, Rules, Policies Violated**

The Hearing Panel considered the Settlement Agreement at a hearing held on June 19, 2008 in Calgary, Alberta. In the Settlement Agreement, the Respondent, PSC, admitted that:

1. In the Fall of 2004, PSC failed to create and maintain adequate records of a call received from its former client GL concerning the conduct of its former Approved Person, Rodney Jacobson, and the steps that PSC took in response, contrary to MFDA Rule 2.5.4; and
2. Between November 2004 and December 2006, PSC failed to conduct a reasonable supervisory investigation of Jacobson’s conduct in response to GL’s complaint to the MFDA and to take such supervisory and disciplinary measures as would be warranted by the results of its investigation, contrary to MFDA Rules 1.1.5(b), 2.5.1, 2.5.4 and the public interest.

MFDA Rule 2.5.4 states that:

**Maintenance of Supervisory Review Documentation.** The Member must maintain records of all compliance and supervisory activities undertaken by it and its partners, directors, compliance officers and branch managers pursuant to the By-laws and Rules.

MFDA Rule 1.1.5(b) states that:

**Agents.** A Member may conduct its business by Approved Persons retained or contracted by it as agents provided that:

...

(b) the Member shall be responsible for, and shall supervise, the conduct of the agent in respect of the business including compliance with applicable legislation and the By-laws and Rules.

MFA Rule 2.5.1 states that:

**Member Responsibilities.** Each Member is responsible for establishing, implementing and maintaining policies and procedures to ensure the handling of its business is in accordance with the By-laws, Rules and Policies and with applicable securities legislation.

**Penalty** Under the terms of settlement, PSC agreed to accept a reprimand and pay a fine in the amount of \$5,000.

**Summary of Facts** PSC has been a Member of the MFDA since February 8, 2002 and is registered as mutual fund dealer in the provinces of Alberta, British Columbia, Manitoba, Ontario and Saskatchewan.

### **Rodney Jacobson**

Rodney Jacobson was registered as a mutual fund salesperson in Alberta from May 1990 to January 2007 and was an Approved Person with PSC from November 2001 to January 2007 when he was terminated by PSC.

Jacobson was responsible for the accounts of GL and TM, two clients of PSC. Between December 2003 and November 2004, without the knowledge or approval of PSC, Jacobson obtained approximately \$55,000 from GL and TM for investments on their behalf. However, Jacobson deposited the monies in the bank account of his holding company and made personal use of the funds.

Specifically, in December 2003, without the knowledge of PSC, Jacobson offered his client GL, an opportunity to purchase a non-mutual fund investment for \$20,000 which would pay GL \$1,000 per month.

After GL demanded the return of his \$20,000 in July 2004, Jacobson received \$35,000 from TM for the purchase of mutual funds. Jacobson deposited the \$35,000 into the bank account of his holding company. He later applied \$15,000 to the purchase of mutual funds in TM's investment account at PSC using blank signed forms previously obtained from TM. Jacobson used the rest of the money from TM to reimburse GL.

In November 2004, when Jacobson learned that the MFDA was investigating his conduct as a result of a complaint submitted by GL, he borrowed money from his personal line of credit to purchase mutual funds in TM's investment account at PSC to reimburse TM for the remaining misappropriated funds.

By Order dated June 11, 2007, an MFDA Hearing Panel accepted a settlement agreement between Staff and Jacobson.

### **The Call From GL**

PSC admitted that GL called PSC and expressed concerns about missing cheques and claimed that he had not signed for anything. According to PSC, after reviewing GL's file, PSC responded to GL's call and believed that GL's concerns had been addressed. However, PSC did not create or maintain any notes of GL's call or steps taken by PSC to respond to it.

### **GL's Complaint To The MFDA**

In October 2004, GL submitted a complaint to the MFDA because he claimed that he had never received confirmation of his December 2003 investment or the monthly income payments that he expected to receive. The MFDA requested documentation from PSC and a written response to the complaint.

In November 2004, after reimbursing the funds misappropriated from TM, Jacobson wrote a lengthy response to GL's complaint in which he attempted to undermine GL's credibility. At the time, PSC was not aware that Jacobson's letter contained false statements and material omissions.

Later in November 2004, in response to follow-up inquiries from the MFDA, Jacobson admitted that he had deposited \$20,000 obtained from GL in the bank account of his holding company. Jacobson claimed this was done as part of an "off-book investment strategy" carried out for GL's benefit. Jacobson also advised that he had offered a "money management service" to one other client with no adverse consequences. According to PSC, Jacobson was informed that his "money management service" contravened firm policy and agreed to "cease the activity forthwith."

The MFDA investigation determined that there were no other victims of Jacobson's misconduct and he ceased off-book activity after reimbursing TM.

## **Failure To Conduct A Reasonable Supervisory Investigation**

PSC failed to conduct a reasonable supervisory investigation with respect to Jacobson's conduct. In particular, the Member failed to: (a) speak with Jacobson's clients GL and TM; (b) review copies of banking records to verify Jacobson's version of events; (c) verify that Jacobson had not received money from other individuals; (d) seek an explanation from Jacobson to account for the discrepancies between his first and second responses to the MFDA; and (e) review records of trading activity in the accounts of GL and TM to see if it was consistent with Jacobson's story. Had PSC conducted a reasonable supervisory investigation, PSC would have discovered that Jacobson's story was not corroborated by relevant documentation, banking records and the clients. PSC also failed to subject Jacobson to heightened supervision or formal disciplinary action.

## **Subsequent Action Taken By Portfolio Strategies**

In November 2006, during a review of Jacobson's sub-branch, Jacobson falsely informed PSC that he received no financial benefit from his "off-book" dealings with GL and TM. PSC accepted this statement and issued a formal written reprimand to Jacobson with respect to his off-book activity.

In December 2006, the MFDA informed PSC that Jacobson may pose a risk of harm to the public as he had apparently misappropriated client money. On January 11, 2007, Portfolio Strategies terminated Jacobson for cause.

Recently, PSC hired new compliance staff including a new Chief Compliance Officer with regulatory and compliance experience. PSC also substantially revised its policies and procedures manual, particularly with respect to "Complaint Handling, Internal Investigations and Internal Discipline".

## **Penalty**

The Hearing Panel noted that on its face, the penalty was relatively small. In accepting the Settlement Agreement, the Hearing Panel was heavily influenced by the fact that the events occurred in the early days of the MFDA regulatory compliance regime. The Hearing Panel noted that in the intervening period, the MFDA has, through its policies and notices, provided considerable guidance to the dealer community on their supervisory obligations. As a result, MFDA Members should now be fully aware of the importance of issues like complaint handling and diligent review of outside business activity. If the same supervisory failures occurred today, the penalty should and would be considerably higher.

For greater detail, see the Settlement Agreement, accepted on June 19, 2008 and the Decision and Reasons, dated August 6, 2008, posted on the MFDA's website in the "Enforcement" section under "Completed Cases".