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MFDA Bulletin

Enforcement

For Distribution to Relevant Parties Within your Firm

MFDA imposes lifetime ban and \$3.5 million fine on Earl Crackower

Nature of Proceeding A Hearing Panel of the Mutual Fund Dealers Association (“MFDA”) Ontario Regional Council has imposed disciplinary penalties on Earl Crackower (“Crackower”), a former Approved Person of the MFDA.

By-Laws, Rules, Policies Violated Following a hearing on July 20, 2005, the Hearing Panel found that Crackower:

1. had, and continued in, another gainful occupation that was not approved by the Member, contrary to MFDA Rule 1.2.1(d);
2. solicited and accepted monies from clients in the total amount of \$3.4 million, more or less, which he failed to return or otherwise account for, contrary to MFDA Rule 2.1.1;
3. misled the MFDA by stating in response to an inquiry from the MFDA that he had only borrowed or solicited monies from one client when he knew that to be an incorrect response, contrary to s. 22.2 of MFDA By-law No. 1 and MFDA Rule 2.1.1(b).
4. failed to attend at the offices of the MFDA and give information for the purpose of allowing the MFDA to investigate a complaint made against him, contrary to s. 22.1(c) of MFDA By-Law No. 1.

MFDA Rule 1.2.1(d) states:

An Approved Person may have, and continue in, another gainful

occupation, provided that:

(iii) *Member approval*. The Member for which the Approved Person carries on business either as an employee or agent is aware and approves of the Approved Person engaging in such other gainful occupation;

MFDA Rule 2.1.1 states:

Each Member and each Approved Person of a Member shall:

- (a) deal fairly, honestly and in good faith with its clients;
- (b) observe high standards of ethics and conduct in the transaction of business;
- (c) not engage in any business conduct or practice which is unbecoming or detrimental to the public interest; and
- (d) be of such character and business repute and have such experience and training as is consistent with the standards described in this Rule 2.1.1 or as may be prescribed by the Corporation.

Section 22.2 of MFDA By-Law No. 1 states:

For the purpose of any examination or investigation pursuant to this By-law, the Corporation shall be entitled to free access to, and to make and retain copies of, all books of account, securities, cash, documents, bank accounts, vouchers, correspondence and records of every description of the Member or person concerned, and no such Member or person shall withhold, destroy or conceal any information, documents or thing reasonably required for the purpose of such examination or investigation.

Section 22.1(c) of MFDA By-Law No. 1 states:

For the purpose of any examination or investigation pursuant to this By-law, a Member, Approved Person of a Member or other person under the jurisdiction of the Corporation pursuant to the By-laws or the Rules may be required by the Corporation:

- (b) to attend and give information respecting any such matters;

Penalty

The Hearing Panel imposed the following penalties on Crackower:

1. Permanent prohibition of the authority of Crackower to conduct securities related business in any capacity;
2. A fine of \$3.4 million for engaging in another gainful

- occupation and for soliciting and accepting \$3.4 million from his clients and failing to return or otherwise account for these funds;
3. A fine of \$50,000 for misleading the MFDA;
 4. A fine of \$50,000 for failing to attend and give information; and
 5. Costs of the investigation and hearing in the amount of \$7,500.00.

Summary of Facts

From March 1993 to November 2003, Crackower was registered in Ontario as a mutual fund salesperson for Worldsource Financial Management Inc. ("Worldsource").

Between January 1994 and October 2003, Crackower solicited and accepted monies from certain of his mutual fund clients whom he led to believe would be participating in non-mutual fund investment opportunities. The clients were, for the most part, elderly individuals with limited investment knowledge and low investment risk tolerance.

Crackower led these clients to believe that he would invest their monies by either providing bridge financing to small businesses that were unable to obtain loans from conventional lenders or by placing their monies in some other form of non-mutual fund investment. Crackower led these clients to believe that their investments would be secure and would yield a higher rate of return than the clients would earn from the mutual funds or fixed income investments in which they would otherwise invest.

Crackower provided each client with a promissory note as evidence of the monies that had been given to Crackower to invest on the client's behalf. The promissory note set out the terms on which the initial investments and the returns thereon would be repaid to the client. There is no evidence that Crackower ever used any of the monies given to him by the clients to provide bridge financing to third parties or that he invested the monies in any other type of investment.

In April 2004, Crackower filed an assignment in bankruptcy in which he acknowledged that 33 of his mutual fund clients were unsecured creditors to whom he owed, cumulatively, \$3,390,475.00. Crackower has not returned or otherwise accounted for any of these monies.

In October 2003, the MFDA commenced an investigation. Crackower provided a false and misleading response to an MFDA request. Crackower also failed to attend and give information when requested to do so by the MFDA.

The Hearing Panel noted that Crackower's private business deals, which he had not disclosed to Worldsource, were not only to the extreme detriment of

his clients, but also in conflict with the work for which he was employed. In cases involving misappropriation of funds and borrowing money from clients, the Hearing Panel noted that the fine should roughly equal the amounts misappropriated or borrowed.

The Hearing Panel also found that the penalty for misleading an MFDA investigation should be at least equal to the penalties imposed for failing to cooperate with an MFDA investigation. Otherwise, it would imply that it is better to lie during an investigation (which may misdirect the MFDA investigators and result in unnecessary expense and delay) than to refuse to cooperate.

For greater detail, see the Decision and Reasons, dated August 22, 2005 and the Order, dated August 29, 2005, posted on the MFDA website under "Enforcement".

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