Ontario Securities Commission
Commission des valeurs mobilières de l'Ontario
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**IN THE MATTER OF THE *SECURITIES ACT*,
R.S.O. 1990, c. S.5, AS AMENDED**

AND

**IN THE MATTER OF
JOHN DAUBNEY AND CHERYL LITTLER**

**REASONS AND DECISION: SANCTIONS AND COSTS
(Section 127 and 127.1 of the *Securities Act*)**

Hearing:	Written hearing by submissions completed July 18, 2008.	
Decision:	August 14, 2008	
Panel:	Carol S. Perry Margot C. Howard	- Commissioner - Commissioner
Counsel:	Alexandra Clark	- For the Ontario Securities Commission
Agent:	James C. Morton	- For John Daubney

REASONS AND DECISION

A. OVERVIEW

[1] This was a bifurcated hearing before the Ontario Securities Commission (the "Commission") pursuant to sections 127 and 127.1 of the *Securities Act,* R.S.O. 1990, c. S.5, as amended (the "Act"), to consider whether it is in the public interest to make an order with respect to sanctions and costs against John Daubney ("Daubney").

[2] On July 14, 2006, Staff of the Commission ("Staff") filed a Statement of Allegations and Notice of Hearing with respect to Daubney and Cheryl Littler ("Littler"). Staff alleged that Daubney and Littler indiscriminately recommended an aggressive and risky investment strategy to their clients, without taking proper account of their clients' risk tolerance, investment objectives, investment knowledge, age, income or net worth, and thereby provided investment advice that was unsuitable for their clients, contrary to their obligations under section 1.5(1)(b) of OSC Rule 31-505 – *Conditions of Registration* (1999), 22 O.S.C.B. 731, amended (2003), 26 O.S.C.B. 7170 ("OSC Rule 31-505"). Staff also alleged that Daubney and Littler failed to deal with their clients fairly, honestly and in good faith, contrary to section 2.1(2) of OSC Rule 31-505. Further, Staff alleged that Daubney and Littler made misleading and inaccurate undertakings about the investment returns that their clients should expect from following their advice, in contravention of section 38(2) of the Act.

[3] Staff and Littler entered into a settlement agreement on October 3, 2007, which was approved by the Commission on October 4, 2007, leaving Daubney as the only remaining respondent in this proceeding.

[4] The hearing on the merits was held on October 9, 10, 11, 12, 15 and 17, 2007, and closing written submissions were completed on November 23, 2007. A decision on the merits was rendered on April 30, 2008.

[5] Following the release of the decision on the merits, counsel for Staff and the agent for Daubney agreed that the hearing on sanctions and costs should be held in writing pursuant to section 5.1 of the *Statutory Powers Procedure Act*, R.S.O. 1990, c. S.22, as amended, and Rule 5 of the Commission's *Rules of Practice*.

[6] On May 28, 2008, Staff filed joint sanctions submissions in which Staff and Daubney (the "Parties") requested an order:

- terminating Daubney's registration (which was suspended in January 2003);
- permanently prohibiting him from becoming or acting as an officer or director of a registrant; and
- reprimanding him.

[7] Daubney filed a response on June 3, 2008 confirming that Staff's submissions were joint submissions and adding brief additional submissions regarding his health and financial status.

[8] Upon reviewing these submissions, the Commission invited submissions in writing with respect to whether costs and additional sanctions should be considered. The Parties' written responses were received on June 30, 2008 (Daubney) and July 11, 2008 (Staff).

[9] For the following reasons, we find that it is in the public interest to order sanctions in accordance with the joint submissions of the Parties.

B. THE DECISION ON THE MERITS

[10] The Commission found that Daubney failed to fulfill his obligations as a registrant pursuant to s. 1.5(1)(b) of OSC Rule 31-505 in respect of the advice given to the six investors who testified for Staff (the "Six Investors"). OSC Rule 31-505 (the "know your client" rule) requires a registrant to "make such enquiries about each client" as "are appropriate, in view of the nature of the client's investments and of the type of transaction being effected for the client's account, to ascertain the general investment needs and objectives of the client and the suitability of a proposed purchase or sale of a security for the client." The Commission also found that Daubney failed to deal fairly, honestly and in good faith with the Six Investors. However, the Commission was not persuaded that Daubney gave undertakings to his clients relating to the future value of the investments he recommended, contrary to s. 38(2) of the Act.

[11] The Commission made the following specific findings:

- "Daubney's knowledge of investment products and approaches was seriously deficient." For example, "his plan for nearly all the investors was to achieve maximum exposure to equity mutual funds through leveraging any leverageable asset. There was never a discussion of appropriate asset allocation and return objectives taking into account each investor's time horizon and risk tolerance." (*Re Daubney* (2008), 31 O.S.C.B. 4817 ("*Re Daubney*"), para. 198)
- "Daubney failed to make appropriate enquiries to assess his clients' investment needs and failed to assess their needs in any reasonable way." For example, he "did not understand the importance of time horizons in assessing an investor's tolerance for risk" and "placed his clients in a position where they owned insufficient unencumbered liquid assets to meet any margin calls." (*Re Daubney*, para. 199)
- The Six Investors "were relatively vulnerable because of their lack of investment knowledge. We accept their evidence that they relied on Daubney's advice. We also find that this was or should have been evident to Daubney." (*Re Daubney*, para. 201)
- "Daubney failed to recommend suitable investments for the Six Investors. Indeed, the investment approach he recommended was highly risky and fundamentally unsuitable for these investors, by any reasonable standard." (*Re Daubney*, para. 203)

- The Commission did not believe Daubney's testimony that he clearly explained the risks, as well as the benefits, of the investments he recommended. The Commission found that "he focused on high rates of return, and virtually disregarded the potential for disaster in the combination of leveraged investing in high-risk investment products. . . . he disregarded or gave scant regard to relative risks." (*Re Daubney*, para. 206)
- "While investors are well advised to be cautious in choosing investments, the Act places the duty of care on the registrant, who is better placed to understand the risks and benefits of any particular investment product. That duty cannot be transferred to the client." "In any event, there was no evidence that Daubney's clients received suitable investment advice from him which they disregarded. Instead, we heard consistent evidence from the investors that they depended on Daubney for his recommendations. We accept the investors' evidence. Also, we find that these investors told Daubney everything he needed to know to assess their risk tolerances and yet his recommended investment approach was entirely unsuitable for them." (*Re Daubney*, paras. 210-211)

[12] The decision on the merits concluded with the following statement:

> Accordingly, we find that Daubney violated the "know-your-client" and suitability requirements of OSC Rule 31-505 by making unsuitable investment recommendations to the Six Investors who form the subject of Staff's allegations and by failing to deal fairly, honestly and in good faith with the investors. We find that Daubney utterly failed to fulfill his obligations as a registrant under the Act, and his conduct caused great harm to the investors who relied on him.
>
> Indeed, this is an egregious case of a registrant's reckless disregard of his obligations under the Act. We find that Daubney has acted contrary to the public interest. (*Re Daubney*, paras. 219-220)

C. SUBMISSIONS

1. Joint Submissions

[13] In joint submissions filed by Staff on May 28, 2008, the Parties request an order terminating Daubney's registration, permanently prohibiting him from becoming or acting as an officer or director of a registrant, and reprimanding him.

a) Termination of Registration and Director and Officer Ban

[14] The Parties submit that this case requires "the most serious sanctions", and further that such sanctions should focus on Daubney's registration status.

[15] In support of this submission, the Parties cite the Commission's finding that Daubney failed to fulfill his obligations as a registrant and caused "great harm" to the Six Investors.

[16] Further, the Parties note the Commission's finding that Daubney was registered as a mutual fund salesperson for a considerable period of time (between 1990 and 2002).

[17] For these reasons, the Parties submit that merely continuing the suspension of Daubney's registration would be inadequate, and an order terminating his registration is required.

[18] Further, the Parties submit that although Daubney is not currently a director or officer of any registrant, according to Commission records, an order permanently barring him from becoming or acting as a director or officer of any registrant firm is required to protect the investing public in the future.

b) Reprimand

[19] The Parties also submit that a reprimand is appropriate in order to express the Commission's disapproval of Daubney's serious and protracted failure to fulfill his obligations as a registrant and acknowledge the losses suffered by his clients.

c) Conclusion

[20] The Parties submit that the proposed sanctions are consistent with those imposed in previous Commission cases involving unsuitable investment advice and breaches of the "know your client" rule. (*Re Verbeek* (2006), 29 O.S.C.B. 69; *Re Marchment & Mackay Ltd.* (1999), 22 O.S.C.B. 6446 (*"Re Marchment"*); and *Re E.A. Manning et al*. (1990), 18 O.S.C.B. 5317 (*"Re E.A. Manning"*))

[21] The Parties' note that these cases also involved other and broader breaches of the Act, and therefore broader sanctions were imposed. However, Daubney's breaches of the Act are all clearly rooted in his status as a registrant and his ability to dispense investment advice and accordingly his registration status is the focus of the proposed sanctions.

[22] The Parties do not seek an order for an administrative penalty, or for reimbursement of Staff's investigation or hearing costs in this matter because any such order "might deplete funds otherwise available to clients who suffered losses" as a result of following Daubney's advice. The Parties note that Daubney declared personal bankruptcy in 2002 and was discharged from bankruptcy in 2003. Further, there is outstanding litigation between Daubney and several of his former clients relating to the leveraged investment advice given by Daubney and the losses the plaintiff-clients claim they suffered as a result.

[23] Finally, the Parties note that the proposed sanctions are joint sanctions. The Parties submit that it is well-established in criminal law that, while a trial judge is not bound by a joint submission on sentencing, she or he must give it serious consideration, and the proposed sentence should not be rejected unless it is "contrary to the public interest and

the sentence would bring the administration of justice into disrepute." The Parties submit that this approach is equally applicable in Commission proceedings. (*R. v. Cerasuolo* (2001), 140 O.A.C. 114 (Ont. C.A.); *R. v. Dorsey* (1999), 123 O.A.C. 342 (Ont. C.A.))

2. Daubney's Submissions

[24] By letter dated June 3, 2008, Daubney's agent confirms that Staff's submissions are joint submissions, and adds that Daubney "is, for all intents and purposes indigent and his health is uncertain at best. Further particulars of his health condition can be provided if required."

3. Further Submissions

[25] Upon review of the Parties' joint submissions, we invited the parties to provide further submissions with respect to whether additional sanctions should be considered.

[26] Having reviewed the Parties' additional submissions filed in response to our request, we find that it is appropriate to order the sanctions proposed in the Parties' joint submissions.

D. ANALYSIS

1. Sanctioning Factors

[27] The Commission's well-established approach to sanctions is reviewed in Staff's May 28, 2008 joint submission, as follows, and we accept it.

[28] In making an order under section 127 of the Act, the Commission is to exercise its public interest jurisdiction in a protective and preventative manner, as described in *Re Mithras Management Ltd.*:

> . . . , the role of this Commission is to protect the public interest by removing from the capital markets − wholly or partially, permanently or temporarily, as the circumstances may warrant − those whose conduct in the past leads us to conclude that their conduct in the future may well be detrimental to the integrity of those capital markets. We are not here to punish past conduct; that is the role of the courts, particularly under section 118 [now 122] of the Act. We are here to restrain, as best we can, future conduct that is likely to be prejudicial to the public interest in having capital markets that are both fair and efficient. In so doing we must, of necessity, look to past conduct as a guide to what we believe a person's future conduct might reasonably be expected to be; we are not prescient, after all. (*Re Mithras Management Ltd.* (1990), 13 O.S.C.B. 1600 at 1610-1611)

[29] The Supreme Court of Canada described the Commission's public interest jurisdiction in the following terms:

> The purpose of an order under s. 127 is to restrain future conduct that is likely to be prejudicial to the public interest in fair and efficient capital markets. the role of the [Commission] under s. 127 is to protect the public interest by removing from the capital markets those whose past conduct is so abusive as to warrant apprehension of future conduct detrimental to the integrity of the capital markets. (*Committee for Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission*), [2001] 2 S.C.R. 132, 199 D.L.R. (4th) at 591)

[30] In *Re Cartaway Resources Corp.*, [2004] 1 S.C.R. 672, the Supreme Court stated: "it is reasonable to view general deterrence as an appropriate, and perhaps necessary, consideration in making orders that are both protective and preventative. (para. 60, Le Bel J.)

[31] In determining the appropriate sanctions in this matter, we must consider the specific circumstances of this case to ensure that the sanctions are proportionate. (*Re M.C.J.C. Holdings Inc. and Michael Cowpland*, (2002), 25 O.S.C.B. 1133 (*"Re M.C.J.C. Holdings"*) at para. 26)

[32] The Commission has accepted that the relevant factors in determining sanctions include the following:

- the seriousness of the allegations proved;
- the respondent's experience in the marketplace;
- the level of a respondent's activity in the marketplace;
- whether or not there has been a recognition of the seriousness of the improprieties;
- whether or not sanctions may deter not only those involved in the case being considered, but any like-minded people from engaging in similar conduct in the capital markets;
- any mitigating factors;
- the size of any profit (or loss avoided) from the illegal conduct;
- the size of any financial sanction or voluntary payment when considered with other factors;
- the effect any sanction might have on the livelihood of the respondent;
- the restraint any sanction might have on the ability of the respondent to participate without check in the capital markets;
- the reputation and prestige of the respondent;
- the financial consequences to a respondent of any sanction; and
- the remorse of the respondent.

(*Re Belteco Holdings* (1998), 21 O.S.C.B. 7743, para. 25-26; *Re M.C.J.C. Holdings*, para. 26)

[33] In *Re M.C.J.C. Holdings*, the Commission observed that these are only some of the factors to consider, observing that, depending on the facts in any given case, "there may be others, and perhaps all of the factors we have mentioned may not be relevant in this or another particular case." (*Re M.C.J.C. Holdings*, para. 26)

2. The Appropriate Sanctions in this Case

[34] In this case, the most relevant factors in determining sanctions are the following.

a) The Seriousness of the Allegations Proved

[35] The Commission found that Daubney "utterly failed to fulfill his obligations as a registrant" with respect to the know your client and suitability requirements of OSC Rule 31-505. This case was not close to the line. Rather, the Commission described it as "an egregious case of a registrant's reckless disregard of his obligations under the Act." (*Re Daubney*, paras. 219-220)

[36] In the decision on the merits, the Commission relied on the following statement from *Re Marchment & Mackay Ltd.* (1999), 22 O.S.C.B. 4705 at 4708:

> The duty to know the client's investment objectives, financial means and personal circumstances, and to recommend only those investments which are suitable for the client is fundamental to the obligation of every dealer and registered representative dealing with the public.

[37] The Commission described the seriousness of Daubney's failure to meet his obligations as a registrant as "amongst the most serious of allegations," and continued:

> As stated by the Commission, the know-your-client and suitability requirements "are an essential component of the consumer protection scheme of the Act and a basic obligation of a registrant, and a course of conduct by a registrant involving a failure to comply with them is an extremely serious matter" (*Re E.A. Manning Ltd.* at 5339).
>
> (*Re Daubney*, paras. 212-213)

[38] Further, the Six Investors suffered great harm as a result of Daubney's misconduct. Given their ages, retirement plans and financial circumstances, and their expressed desire for safe investments, Daubney should have known that his investment recommendations were unsuitable for these investors. The Commission found that Daubney "focused on high rates of return, and virtually disregarded the potential for disaster in the combination of leveraged investing in high-risk investment products." The Commission found that these investors were unsophisticated and relatively vulnerable, and Daubney knew or should have known that they relied on his advice. (*Re Daubney*, paras. 201, 206 and 219)

b) Daubney's Role as a Registrant

[39] As a registrant experienced in the capital markets, Daubney was expected to understand the know-your-client and suitability rules, which "are an essential component

of the consumer protection scheme of the Act and a basic obligation of a registrant". (*Re Daubney*, para. 213, referring to *Re E.A. Manning,* at 5339)

c) The Effect of the Proposed Sanction on the Respondent's Livelihood and Ability to Participate in the Capital Markets

[40] Daubney's registration was suspended by the Commission in January 2003, and he is not currently a director or officer of any registrant. Given Daubney's age and health, we find that the proposed agreed sanctions will effectively bar him permanently from participating as a registrant in the capital markets.

d) Other Factors

[41] Given the egregious nature of Daubney's misconduct, we considered whether additional sanctions should be ordered, including a cease trade order under paragraph 2 of s. 127(1) of the Act, an order under paragraph 3 of s. 127(1) that any exemptions contained in Ontario securities law do not apply to Daubney, an order prohibiting calls to residences pursuant to section 37 of the Act, and an administrative penalty under paragraph 9 of s. 127(1) of the Act. We also considered whether this was an appropriate case for an order of costs under s. 127.1 of the Act.

[42] However, having reviewed the further submissions of the Parties filed in response to our request, we conclude that it is appropriate to accept the Parties' joint submissions in this case. Though we might have given serious consideration to additional sanctions following a contested sanctions hearing, we are satisfied that the proposed joint sanctions, are in the public interest. We find that terminating Daubney's registration and barring him from becoming or acting as a director or officer of a registrant are the appropriate sanctions for Daubney's failure to fulfill his obligations as a registrant. These sanctions prevent future harm by ensuring that Daubney will never again be able to take on a licensed role in the securities industry. Further, our reprimand expresses our strong disapproval of Daubney's misconduct, which was serious and protracted, and caused great harm to vulnerable investors.

E. CONCLUSION

[43] For the reasons given, we conclude it is in the public interest to make the following order.

[44] It is ordered that:

1. The registration granted to Daubney under Ontario securities law is terminated, pursuant to paragraph 1 of subsection 127(1) of the Act;

2. Daubney is prohibited from becoming or acting as director or officer of any registrant, pursuant to paragraph 8.1 of subsection 127(1) of the Act; and

3. Daubney is reprimanded, pursuant to paragraph 6 of subsection 127(1) of the Act.

DATED in Toronto this 14th day of August, 2008.

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Carol S. Perry	Margot C. Howard