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Date: 2017-12-04

IN THE MATTER OF
EARL MAREK

Reasons And Decision On A Review Of A Decision Of The Investment Industry Regulatory Organization Of Canada
(Sections 8 and 21.7 of the *Securities Act*, RSO 1990, c S.5)

Hearing:	November 8, 2017	
Decision:	December 4, 2017	
Panel:	Timothy Moseley	Commissioner and Chair of the Panel
	AnneMarie Ryan	Commissioner
	Peter Currie	Commissioner
Appearances:	V. Ross Morrison	For Earl Marek
	Kathryn Andrews Andrew Werbowski	For Staff of the Investment Industry Regulatory Organization of Canada
	Alvin Qian Carlo Rossi	For Staff of the Ontario Securities Commission

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REASONS AND DECISION

I. OVERVIEW

[1] In October 2016, a hearing panel of the Investment Industry Regulatory Organization of Canada (**IIROC**) issued a merits decision (the **Merits Decision**),[1] in which it found that Earl Marek, an IIROC registrant, had contravened an IIROC rule by facilitating off-book share purchases for two clients without the knowledge and approval of his Member firm. In a penalty decision issued in February 2017,[2] the IIROC panel ordered, among other things, that Mr. Marek be suspended from registration for one year and that he pay a fine of $50,000.

[2] Mr. Marek applies to the Ontario Securities Commission (the **Commission**) for a review of the IIROC decisions. He contends that the two brothers who purchased the shares (PL and DL; together, the **L Brothers**) were not clients of his at the time of those off-book transactions, and that the IIROC panel should not have found that the allegation against him was established.

[3] The term "client" is not defined in the *Securities Act* (the **Act**),[3] or in any relevant regulation or rule. We must therefore look to the surrounding circumstances. Do the facts of this case support the IIROC panel's finding that the L Brothers were Mr. Marek's clients? This is the central question in this proceeding.

[4] As we explain in more detail below, we conclude that the IIROC panel's decision was correct. This is so for a number of reasons, including that:

a. Mr. Marek recommended to the L Brothers that they buy shares of Facebook Inc. prior to an initial public offering (**IPO**) of those shares;

b. Mr. Marek told them that the transaction would go through his firm Macquarie Private Wealth Inc. (**Macquarie**) and that Macquarie would be paid an administration fee for the transaction;

c. Mr. Marek told the L Brothers that he hoped this was the beginning of a longer-term relationship, and the L Brothers expected that it would be; and

d. the L Brothers reasonably believed that they were clients of Mr. Marek and of Macquarie, and there is no evidence that Mr. Marek did anything at the time of the transaction to disabuse them of that understanding.

II. BACKGROUND FACTS

[5] Because the term "client" is not defined, determination of whether a client relationship exists in a particular case must be made with regard to all the relevant circumstances. We therefore begin with a review of the factual background as found by the IIROC panel. In this proceeding, while Mr. Marek challenged the IIROC panel's conclusions, he did not dispute the background facts. Those facts include the following.

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[1] *Re Marek*, 2016 IIROC 36.
[2] *Re Marek*, 2017 IIROC 13.
[3] RSO 1990, c S.5.

[6] In late 2011 and early 2012, Mr. Marek's son was employed by a company of which PL was the president. Mr. Marek's son told PL about an opportunity to buy pre-IPO Facebook shares from Mr. Marek, who would have a block of these shares, and who wanted to sell some to mitigate his risk. PL said he was interested.

[7] In January 2012, Mr. Marek met with PL and his brother DL at PL's company's offices. DL owned and operated a separate business that shared office space at that location.

[8] At the meeting, Mr. Marek discussed the price at which the pre-IPO shares would be available, the estimated IPO price, the future prospects for Facebook shares, and the merits of investing in Facebook. Mr. Marek also advised that there was some urgency, because the transaction had to be completed before the IPO. Mr. Marek told the L Brothers that if they did not buy the shares, the shares would be sold to other investors.

[9] Mr. Marek said that he was with Macquarie, that the process of acquiring the shares would be smoother if the transaction went through Macquarie, and that Macquarie would receive an administration fee of approximately $1.00 per share. Mr. Marek told the L Brothers that when the shares came in, he would set up the necessary accounts at Macquarie. All expected that this was the beginning of a longer-term relationship.

[10] The L Brothers said they were very interested in buying Facebook shares. The three met a second time at PL's company's offices, and were joined by Mr. Marek's son. At that meeting, the L Brothers understood, as they had throughout, that they would be buying the shares directly from Mr. Marek. They said they wished to buy 1,000 shares each at a price of approximately US$28 per share.

[11] In early February 2012, shortly after that second meeting, Mr. Marek sent an email containing wire transfer instructions for the funds. Those instructions proved to be incomplete. At the L Brothers' request, Mr. Marek provided additional information.

[12] By this time, the L Brothers had learned, from the information that Mr. Marek had given them, that the funds were being sent to New Economy Holdings Limited via Cayman Institutional Bank. The L Brothers did not know of that corporation, but were told that it was a company set up to broker the transaction with a representative of Facebook.

[13] The L Brothers were also surprised to learn that the funds were to be sent to Cayman Institutional Bank instead of to Mr. Marek directly. However, they followed Mr. Marek's instructions. Each brother sent US$28,900, as instructed. Several days later, Mr. Marek advised that the money had been received.

[14] PL saw Mr. Marek every few weeks over the ensuing months. They discussed the performance of Facebook shares, and talked about other investment opportunities. PL saw nothing amiss.

[15] In October 2012, PL opened an account at Macquarie in the name of his company. Later that month, pursuant to a request from PL's company's accountant, PL wrote to Mr. Marek and asked for proof of purchase of the

Facebook shares. PL did not receive a satisfactory response. PL made numerous subsequent attempts, all of which were equally unsuccessful.

[16] Also in late 2012, DL received a New Client Application Form from Macquarie. He completed it, and Mr. Marek picked it up. Mr. Marek advised DL that the Facebook shares were eligible to be deposited into an RRSP account.

[17] By June 2013, neither of the L Brothers had received any confirmation of receipt of the Facebook shares. PL advised Mr. Marek by email that if the matter was not immediately resolved, PL's financial controller would file a formal complaint against Mr. Marek and Macquarie. Mr. Marek replied, in part:[4]

> I want to make it clear that this was a 'off-book opportunity' – nothing to do with Macquarie or any other investment firm, as the funds went directly from you to an account in the Caymans… I was not a middle man, as the funds did not go through me. I merely brought the 'opportunity' to your attention… These shares were being sold by a Facebook consultant… No one realizes this is taking an insane amount of time more than me as I bought 3300 shares…

[18] In November 2013, Mr. Marek sent an email addressed to "Facebook investors", including PL, regarding the Facebook shares. The email said, in part and in bold: "Please delete my Macquarie e-mail address effective immediately and only use [Mr. Marek's personal email address] for all correspondence."[5]

[19] At least as of the date of the IIROC merits hearing, neither of the L Brothers had received his Facebook shares or a return of his US$28,900.

III. ISSUES

[20] In the IIROC proceeding, IIROC Staff alleged that "[o]n or about February 2012, [Mr.] Marek facilitated off book transactions for two clients without the knowledge or approval of his Member firm, contrary to IIROC Dealer Member Rule 29.1."[6]

[21] It is undisputed that the L Brothers' purchases of Facebook shares were "off book" with respect to Macquarie, in that the firm was unaware of the transactions. It is also beyond doubt (and uncontested in Mr. Marek's notice of application and written submissions) that Mr. Marek facilitated the subject transactions. As noted above, Mr. Marek disputes that the L Brothers were clients. Mr. Marek does not challenge the penalties imposed by the IIROC panel, except to say that if the Merits Decision is set aside, the penalties should be set aside as well.

[22] The central question in this case, therefore, is whether the IIROC panel erred in concluding that the L Brothers were Mr. Marek's clients. That question presents the following issues for us to consider:

a. What is the standard of review of an IIROC decision by the Commission?

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[4] Merits Decision at para 40.
[5] Merits Decision at para 41.
[6] Merits Decision at para 1.

b. Do the circumstances of this case lead to the conclusion that the L Brothers were in a client relationship with Mr. Marek at the time that he facilitated the transactions?

c. If the L Brothers were not clients at the relevant time, should the Commission substitute a different decision for that of the IIROC panel?

IV. ANALYSIS

A. What is the standard of review of an IIROC decision by the Commission?

[23] Mr. Marek brings this application under section 21.7 of the Act, which provides that a person directly affected by a decision of a recognized self-regulatory organization (**SRO**) such as IIROC may apply to the Commission for a review of the decision. By virtue of subsection 21.7(2) of the Act, section 8 of the Act applies to this proceeding and authorizes the Commission to "confirm the decision under review or make such other decision as the Commission considers proper."

[24] Despite this broad authority, the Commission acts with restraint in interfering with a decision of an SRO. It was common ground at the hearing before us that the applicable test is that set out in the oft-cited Commission decision in *Re Canada Malting Co.*[7] In that case, the Commission held that it ought to interfere only where the applicant meets the "heavy burden" of demonstrating that at least one of the following applies:

a. the SRO proceeded on an incorrect principle;

b. the SRO erred in law;

c. the SRO overlooked material evidence;

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

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

[25] As is noted above in paragraph [4] and for the reasons explained below, our ultimate conclusion is that the IIROC panel was correct in finding that the L Brothers were clients. As a result, we need not apply the criteria set out in *Re Canada Malting Co.*, and we need not consider what the result would have been had we not found that the L Brothers were clients.

[26] We turn now to the reasons for our conclusion that the L Brothers were indeed clients of Mr. Marek's at the relevant time.

B. Do the circumstances of this case lead to the conclusion that the L Brothers were in a client relationship with Mr. Marek at the time that he facilitated the transactions?

1. Introduction

[27] No provisions of the Act, or of regulations or rules made under the Act, or of IIROC rules, define the term "client"; nor do they, in any other way, expressly

[7] (1986), 9 OSCB 3565 at 3587.

resolve the question of when a client relationship begins. That question is significant for investors and registrants alike, given the numerous protections and obligations that attach to that relationship.

[28] Neither IIROC Staff nor Commission Staff provided us with any authorities in which the parties contested the question of whether a client relationship existed. Of the decisions that Mr. Marek provided, we address below the two that are relevant, at paragraphs [44] and [50]. Neither decision disposes of the central question in this case.

[29] In the absence of conclusive authorities or regulatory provisions, we consider factors that, in our view, ought to be taken into account. At the hearing before us, Mr. Marek and IIROC Staff implicitly adopted this approach, by citing various factors and by making differing submissions as to the weight that ought to be attached to each factor.

[30] In considering potential factors and in assessing the weight to be attached to each, we are guided by the purposes of the Act set out in section 1.1:

a. to provide protection to investors from unfair, improper or fraudulent practices; and

b. to foster fair and efficient capital markets and confidence in capital markets.

[31] We caution that while the non-exhaustive list of factors below may assist in other cases, the determination of a relationship between adviser and client is highly contextual. We now consider those factors that are relevant in this case.

2. Factors

(a) Activity requiring registration

[32] In the context of this proceeding, the first of the two purposes of the Act cited in paragraph [30] above is especially relevant. When dealing with a registrant, an investor is typically at a disadvantage with respect to matters that are within the expertise of the registrant, including the processes involved in completing a trade in securities. Investors are therefore vulnerable to unfair, improper and fraudulent practices. The comprehensive regulatory code that governs registrants is designed to minimize that risk for the investor.

[33] Subsection 25(3) of the Act provides that no person shall engage in the business of advising anyone with respect to investing in, buying or selling securities, unless the person is appropriately registered. A registrant like Mr. Marek, who is engaged in the business of advising clients with respect to investing in securities, engages in that business each time they give such advice.

[34] At their first meeting in January 2012, Mr. Marek and the L Brothers discussed "the merits of Facebook, including whether buying Facebook at a pre-IPO price was a good investment, the price at which the shares would be available, the estimated IPO price and the future prospects for Facebook shares."[8] Mr. Marek testified that he "probably" told the L Brothers he thought it was a good opportunity, "because [he] did believe it was."[9]

[8] Merits Decision at para 22.
[9] Transcript of IIROC merits hearing, April 28, 2016, at p 13.

[35] A statement like that from Mr. Marek is the very essence of professional advice relating to investing in securities. Mr. Marek is in the business of giving that advice to clients. It therefore follows that the communication of such advice gives rise to a strong presumption of a relationship of adviser and client.

[36] That presumption is rebuttable, not absolute. One can imagine circumstances in which such advice is given without any intention by the adviser to create a client relationship, without any expectation by the investor that such a relationship exists, and without any subsequent contact between the two. That is not this case, however.

[37] We find that Mr. Marek's conduct at the January 2012 meeting gives rise to a strong presumption of a client relationship between him and the L Brothers.

(b) Funds used to purchase the Facebook shares

[38] Mr. Marek submits that it ought to have been clear to the L Brothers that he was not acting as their adviser on the transaction, because the funds were going to a third party. We do not accept this submission, for several reasons.

[39] The IIROC panel found that days before Mr. Marek gave the L Brothers the wire instructions for the purchase funds, he recommended that the purchase go through Macquarie, and advised that Macquarie would be paid the administration fee. The panel also found that Mr. Marek did nothing to correct that understanding on the part of the L Brothers, at least until Mr. Marek's June 2013 email referred to in paragraph [17] above.

[40] The L Brothers' only information about how to complete the transaction and where their funds were going came from Mr. Marek. Until Mr. Marek gave them the wire instructions, the L Brothers had no way of knowing this information. Even once they received the wire instructions, the L Brothers still did not have the full picture of the route that the funds were to take. They were not obliged to understand the route, and they were entitled to rely on the clear instructions from Mr. Marek. It would have been reasonable for them to infer that the third-party recipient of the funds was merely an agent.

[41] Further, we note that neither of the L Brothers was cross-examined at the merits hearing. It is inappropriate now to question their belief at the time of the transaction, when they were not confronted with that question and given an opportunity to explain.

[42] Accordingly, we do not find that the fact that the funds were sent to a third party supports Mr. Marek's position that there was no client relationship.

(c) Benefit

[43] In written submissions, Mr. Marek argues that "the hallmark of an IIROC client relationship is compensation: if the registered representative does not receive compensation for the investment then there is no client relationship."[10]

[44] In support of that proposition, Mr. Marek cites *Re Castonguay*,[11] an IIROC case in which it was alleged that the respondent registrant had facilitated a client transaction without the knowledge and consent of his employer, and that the

[10] Applicant's Memorandum of Fact and Law at para 17.
[11] 2012 IIROC 73.

respondent had failed to inform his clients of an essential fact relating to two securities offerings. The IIROC panel found in favour of the respondent, on the basis that while the respondent had a pre-existing client relationship with the investors, the investment was not in securities and did not go through the respondent or the respondent's firm, and the investors did not believe that the investment was to go through the firm.

[45] In our view, those distinguishing facts were determinative. While the panel in *Re Castonguay* observed that the respondent derived "no direct benefit" from the investment, nothing in the panel's decision stands for the proposition that direct compensation is an essential element of a client relationship. In contrast to *Re Castonguay*, the L Brothers' investment was in securities, and they believed (because Mr. Marek told them) that the transaction would go through Macquarie. We do not find *Re Castonguay* to be persuasive of Mr. Marek's position with respect to compensation, and we do not accept his categorical submission that if an investor pays no compensation to the adviser, no client relationship can exist.

[46] Even if that were correct, however, it is inaccurate to say that Mr. Marek received no benefit or compensation. In the Merits Decision, the IIROC panel expressly found that: "[n]o fee was to be paid to [Mr. Marek] but he would get the benefit of being about to manage the shares through the Macquarie account."[12] In other circumstances, there might well be no cash compensation at the beginning of a client relationship, *e.g.*, if the firm waived transaction fees for an initial transaction, or if an account were transferred in from another firm and there were no transactions right away that would generate compensation. It would be incongruous, and contrary to the mandate of investor protection, to find that no client relationship existed in those circumstances.

[47] In this case, as the IIROC panel found, Mr. Marek did benefit. We consider that fact to be persuasive, although not conclusive, as to the existence of a client relationship with the L Brothers.

[48] In addition, we note the undisputed evidence of Mr. Marek's statement to the L Brothers that Macquarie would receive an administration fee for the transaction. Even if, as far as the L Brothers knew, no portion of that fee would go to Mr. Marek, the existence of the fee would support an inference that they were clients of the firm. If that inference were correct, their representative at the firm would have been Mr. Marek.

(d) Account opening documentation

[49] Mr. Marek notes that neither of the L Brothers completed a new account application with Macquarie until late 2012, many months after they wired the funds for the Facebook shares. Mr. Marek submits that this fact supports a conclusion that while the L Brothers became Mr. Marek's clients later that year, they were not clients in February 2012, the time period relevant to IIROC's allegation against him.

[50] Mr. Marek cites the IIROC decision in *Re Turenne*,[13] in which the panel rejected the respondent's contention that the source of funds borrowed by the respondent was not a client. The panel noted that the lender had signed account opening

[12] Merits Decision at para 54.
[13] 2015 IIROC 23.

documents at the respondent's firm at the relevant time. Mr. Marek submits that the panel's conclusion that the lender was a client was based in part on the fact that the account was open. We agree. However, the inverse is not necessarily true. In other words, it does not follow that the absence of an open account precludes the existence of a client relationship.

[51] Such a general rule would be illogical, and would undermine investor protection. The opening of an account ought to be done promptly when a client relationship begins, but the firm's or the individual adviser's failure to take the necessary steps in a timely way must not deprive the investor of the protections that attach to the relationship. Similarly, an adviser ought not to be able to avoid their obligations by delaying, whether deliberately or not, the formal documentation of the relationship.

[52] We conclude that the absence of formally opened accounts does not help to answer the question of whether, in this case, a client relationship existed in February 2012.

(e) The investors' belief

[53] The IIROC panel concluded that from February 2012, the L Brothers believed that they were Mr. Marek's clients and that they acted as if they were.

[54] An investor's belief, even if reasonable, will not necessarily be determinative as to whether a client relationship exists. However, some weight ought to be given to such a belief, if reasonably held, since the investor may act in reliance on that belief. The L Brothers' belief was eminently reasonable, given Mr. Marek's advice that the transaction would go through his firm and that the firm would be paid the administration fee. From the L Brothers' perspective, Mr. Marek orchestrated every step of the transaction up to and including the transfer of funds to purchase the Facebook shares.

[55] In our view, the L Brothers' reasonable belief that they were clients in February 2012 is persuasive evidence that such a relationship existed at that time.

(f) IIROC panel's finding of a client relationship

[56] We have identified above some factors that are relevant to determining the central question in this case. Before reaching our conclusion on that question, we wish to address Mr. Marek's submissions that the IIROC panel did not expressly find that the L Brothers were Mr. Marek's clients, and that the panel failed to consider the criteria for determining the question. Rather, says Mr. Marek, the panel simply assumed, without analysis, that there was a client relationship.

[57] We disagree. In the Merits Decision, the IIROC panel did not use the word "client" in a way that suggested that it reached that conclusion, until after the panel had conducted a thorough review of the evidence of the L Brothers, Mr. Marek and his son, and others. It is clear from the various references to "client" in the concluding "Decision" section of the reasons that the panel rejected Mr. Marek's position, expressly referred to earlier in the Merits Decision, that the L Brothers were not clients at the time of the Facebook transaction.

[58] Further, the IIROC panel's consideration of the question and of the reasons for its conclusion are reflected in the Merits Decision, in which the panel states that in "February of 2012, PL and DL believed they were clients of Macquarie, and

they acted in a manner and were treated by [Mr. Marek] as if they were clients. The documentary formalization of their relationship came later."[14]

(g) Conclusion as to the client relationship

[59] We do not accept Mr. Marek's submission that the contextual approach described above involves too much uncertainty as to when a client relationship begins and is therefore untenable for registrants and their insurers. We recognize that the framework set out in this decision does not provide a single bright-line test that will make it simple to make that determination in every case. The various steps involved in formalizing a client relationship can arise in different ways and different sequences. Those permutations do not lend themselves to a single rule of universal application.

[60] The principle of investor protection dictates that the benefit of any reasonable uncertainty in a particular case should inure to the benefit of the investor. Individual registrants and firms have an obligation to make clear, to investors who might reasonably believe they are clients, whether that belief is correct. Doing so will enable the investors to govern their actions accordingly.

[61] We find no factors in this case that lead us to doubt the existence of a client relationship. Rather, all of the relevant factors contribute to our conclusion that the L Brothers were Mr. Marek's clients in February 2012, at the time of the Facebook transaction. Specifically:

a. at his first meeting with the L Brothers, Mr. Marek engaged in registrable activity by giving advice as to the merits of a specific securities transaction;

b. Mr. Marek told the L Brothers that the transaction would go through Macquarie and that Macquarie would be paid an administration fee;

c. Mr. Marek orchestrated all steps of the transaction, including giving directions as to payment of the funds;

d. Mr. Marek told the L Brothers that he hoped this was the beginning of a longer-term client relationship with them; and

e. the L Brothers reasonably believed throughout that they were clients of Mr. Marek, and there is no evidence that Mr. Marek did anything until June 2013 to disabuse them of that belief.

[62] The IIROC panel's finding that the client relationship existed in February 2012 was amply supported by the evidence, and we find no error in the panel's decision.

C. If the L Brothers were not clients at the relevant time, should the Commission substitute a different decision for that of the IIROC panel?

[63] Given our conclusion that the L Brothers were Mr. Marek's clients at the relevant time, and that the IIROC decision is correct, we need not consider the third issue; that is, whether the Commission should substitute a different decision for that of the IIROC panel.

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[14] Merits Decision at para 143.

V. CONCLUSION

[64] For the above reasons, the application for a review of the IIROC decisions is dismissed and the IIROC decisions are confirmed.

Dated at Toronto this 4th day of December, 2017.

"*Timothy Moseley*"

Timothy Moseley

"*AnneMarie Ryan*"

AnneMarie Ryan

"*Peter Currie*"

Peter Currie