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IN THE MATTER OF BDO CANADA LLP

REASONS AND DECISION ON A MOTION

Hearing: May 3, 2019

Decision: June 6, 2019

Panel: Timothy Moseley Vice-Chair and Chair of the Panel

Appearances: Doug McLeod For the moving party BDO Canada
Eric Leinveer LLP

Robert L. Gain For Staff of the Commission
Anna Huculak

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REASONS AND DECISION

I. OVERVIEW

- [1] Staff of the Ontario Securities Commission (**Staff** of the **Commission**) alleges that BDO Canada LLP (**BDO**), in conducting audits relating to Crystal Wealth Management Systems Limited (**Crystal Wealth**), breached certain provisions of the *Securities Act*¹ (the **Act**).
- [2] The proceeding against BDO is in its early stages. Staff has made disclosure to BDO of documents and information in Staff's possession relating to the allegations. BDO submits that the disclosure it has received is inadequate. BDO has brought this motion seeking an order of the Commission requiring Staff to make further disclosure. In particular, BDO seeks disclosure of files relating to compliance reviews of Crystal Wealth (the **Compliance Reviews**) conducted by Staff and by staff of the British Columbia Securities Commission (**BCSC Staff**). BDO also objects to Staff's decision not to disclose documents that pre-date January 1, 2012 (three years before the effective date of the earlier of the two impugned audits).
- [3] The motion was heard on May 3, 2019. On May 7, 2019, I issued an order dismissing the motion for reasons to follow. These are my reasons.
- [4] As I explain more fully below, for BDO to be entitled to an order requiring disclosure of any further documents or information regarding the Compliance Reviews, BDO would have to demonstrate a sufficient connection between the allegations against it and the Compliance Reviews. BDO has failed to do so. BDO also failed to articulate a basis for an order requiring disclosure of documents that pre-date January 1, 2012.

II. BACKGROUND

A. Fraud at Crystal Wealth

- [5] Staff previously brought an enforcement proceeding against Clayton Smith, who was the founder and directing mind of Crystal Wealth and of the investment funds managed by Crystal Wealth (the **Funds**). In a settlement of that proceeding,² Smith admitted that from 2012 to 2017, he and Crystal Wealth committed various breaches of Ontario securities law, including by engaging in fraud with respect to two of the Funds. Specifically, Smith agreed that he had caused monies to be advanced from the two funds, purportedly to purchase investments for the funds, but instead the monies went to Smith, to Smith's holding company, or to a related company.
- [6] In April 2017, the Ontario Superior Court of Justice granted the Commission's application to appoint a receiver over Crystal Wealth, the Funds, and Smith (among other entities).³

¹ RSO 1990, c S.5

² The settlement was approved by the Commission in June of 2018: *Clayton Smith (Re)*, 2018 ONSC 33 (CanLII) (**Smith Settlement**)

³ *Smith Settlement* at para 16

B. Allegations against BDO

- [7] Following the settlement with Smith, Staff commenced this proceeding against BDO. In this proceeding, Staff alleges that from 1998 to 2017, BDO was the auditor of Crystal Wealth and of the Funds. Staff also alleges that with respect to the audits of the Funds as at and for the years ended December 31, 2014, and December 31, 2015, BDO falsely represented to the Funds' unitholders that it had performed the audits in accordance with Canadian generally accepted auditing standards (**GAAS**).
- [8] Staff contends that BDO failed to comply with GAAS in three ways:
- a. BDO did not obtain sufficient appropriate audit evidence with respect to the Funds' assets;
 - b. BDO did not undertake its work with sufficient professional skepticism; and
 - c. BDO did not complete the engagement quality control reviews that it had determined were required.
- [9] Staff alleges that as a result, BDO breached:
- a. subsection 78(3) of the Act, which requires the auditor of a mutual fund to "make such examinations as will enable the auditor to make the [required] report"; and
 - b. clause 122(1)(b) of the Act, which prohibits the making of a materially misleading or untrue statement in a financial statement required to be filed or furnished under Ontario securities law.

C. BDO's motion for further disclosure

- [10] Following a first appearance on October 29, 2018, the Commission ordered that by November 9, 2018, Staff disclose to BDO any "non-privileged relevant documents and things" in Staff's possession or control. Staff took steps to comply with that requirement.
- [11] On February 19, 2019, BDO filed this motion, by which it seeks additional disclosure from Staff. BDO's concerns fall into three categories:
- a. First, BDO contends that there were various technical issues with certain electronic disclosure that Staff had made, and that as a result BDO was prevented from carrying out a proper review of that disclosure. At the hearing of this motion on May 3, 2019, the parties agreed that the technical issues had been resolved.
 - b. Second, BDO asks that the Commission require Staff to disclose to BDO all documents and things in Staff's possession or control relating to:
 - i. compliance reviews of Crystal Wealth and its Funds commenced by Staff in 2011 and 2014 (the **OSC Compliance Reviews**);

- ii. compliance reviews of Crystal Wealth commenced by staff of the British Columbia Securities Commission (the **BCSC**) in 2013 and 2015 (the **BCSC Compliance Reviews**);⁴ and
- iii. “any and all other compliance reviews or investigations conducted by OSC or BCSC Staff of Crystal Wealth or its representatives”.
- c. Third, BDO objects to Staff’s decision not to disclose any documents that pre-date January 1, 2012.

III. ANALYSIS

A. Issues

[12] This motion presents the following issues:

- a. What is the extent of Staff’s disclosure obligation in an enforcement proceeding?
- b. Should Staff be required to disclose the contents of Staff’s files relating to the OSC Compliance Reviews?
- c. If Staff’s disclosure obligation does extend to include the file contents of the OSC Compliance Reviews, what steps if any should Staff be required to take with respect to BCSC Staff’s files relating to the BCSC Compliance Reviews?
- d. Should Staff be required to disclose documents that pre-date January 1, 2012?

B. What is the extent of Staff’s disclosure obligation in an enforcement proceeding?

1. The disclosure obligation generally

[13] Rule 27(1) of the *Ontario Securities Commission Rules of Procedure and Forms*⁵ (**OSC Rules**) requires Staff to provide to every other party “copies of all non-privileged documents in Staff’s possession that are relevant to an allegation”. This rule embodies a disclosure standard similar to that imposed on the Crown in criminal proceedings by *R v Stinchcombe*.⁶

[14] Staff must initially assess which non-privileged documents it considers to be relevant to an allegation. In exercising that judgment, which is later reviewable by the Commission, Staff must:

- a. include not only documents on which Staff intends to rely, but also documents that might reasonably assist a respondent in making full answer and defence to Staff’s allegations, including by helping the respondent make tactical decisions;
- b. assess the relevance of documents in the context of the specific allegations being made by Staff;

⁴ Staff asserts that it is aware of only one compliance review conducted by BCSC Staff. Given my decision on this motion, it was unnecessary for me to resolve the conflict between Staff’s assertion and BDO’s request.

⁵ (2017), 40 OSCB 8988

⁶ [1991] 3 SCR 326

- c. reasonably anticipate defences or issues that a respondent might properly raise, in order to inform Staff's assessment of relevance;
 - d. include both inculpatory and exculpatory documents; and
 - e. err on the side of inclusion.⁷
- [15] BDO submitted, Staff conceded, and I agree, that the confines of disclosure are not conclusively dictated by Staff's view of the case. A respondent may review the disclosure it receives and consider whether the disclosure appears to be complete. If a respondent believes that it is not, the respondent may request further disclosure from Staff, and if still not satisfied may seek the necessary order from the Commission.
- [16] A respondent's belief that the disclosure provided is incomplete could arise for varying reasons, including for example where the respondent contemplates a defence that Staff did not foresee, despite Staff's reasonable efforts to anticipate potential defences. Following initial disclosure, therefore, the burden lies on the respondent to articulate a basis for requesting further disclosure.
- [17] While Staff's disclosure obligation is broad, the obligation is not unlimited. Relevance ultimately depends on there being a sufficient connection between the document in question and the respondent's ability to make full answer and defence to Staff's allegations.
- [18] BDO argued strenuously that on a motion such as this, the Commission is not to make an admissibility ruling as if this were the merits hearing at which Staff's allegations were being litigated. I agree, but while relevance for the purpose of disclosure may be more expansive than admissibility at a hearing, there are still limits, in that relevance is determined with reference to the specific allegations.
- [19] BDO further submitted that Staff's disclosure obligation extends beyond those documents that are relevant, to documents that might possibly be relevant. However, Rule 27(1) of the OSC Rules explicitly imposes the standard of "relevant to an allegation", and nothing broader. In my view, the approach set out in paragraph [14] above, which incorporates a reasonableness standard as well as the obligation to err on the side of inclusion, accurately reflects Rule 27(1) and the applicable authorities, and adequately responds to BDO's submission on this point.

2. Is "Staff work product" an exception to the disclosure obligation?

- [20] Staff's written submissions refer to a category of documents and information it calls "Staff Work Product", that Staff submits need not be disclosed because those documents and information are irrelevant. In its written submissions, Staff includes within this category the following:
- a. internal Staff notes, analyses or communications;

⁷ *Deloitte & Touche LLP v Ontario (Securities Commission)*, (2002) 159 OAC 257, 2002 CanLII 44980, at paras 40, 41 and 44; *Biovail Corp. (Re)*, 2008 ONSEC 14, (2008) 31 OSCB 7161 at paras 15, 32, 40, 41; *Shamblau (Re)*, (2002), 25 OSCB 1850 at para 16; *R v Taillefer* (2003), [2003] 3 SCR 307 at para 59

- b. guidance to Staff field team reviewers in respect of the OSC Compliance Reviews;
- c. communications between Staff and other regulators; and
- d. other similar documents and information.

- [21] It is true that some documents falling within this category would not generally need to be disclosed. However, in my view, the term “Staff Work Product”, as defined by Staff in its written submissions, is overly broad, is imprecise and is not helpful in analyzing the issues that this motion presents. To illustrate the point, it includes internal Staff notes, which may record statements made by a respondent relating directly to the allegations in the case. In addition, or instead, the notes may record a Staff member’s opinions about such statements. Those two different types of content should attract different considerations when determining relevance.⁸
- [22] Accordingly, deciding whether a document ought to be disclosed must involve reference to the document’s content. The mere fact that a document is generated by Staff as opposed to gathered by Staff from a third party would not necessarily be determinative of whether the document is relevant and disclosable. Documents gathered by Staff from a third party are sometimes referred to as “fruits of the investigation”, although as Staff submitted on this motion, that term might also include Staff’s note made of a meeting with a third party.
- [23] In *Phillips (Re)*,⁹ the Commission considered the same issue presented by this motion. There, the Commission defined “Staff work product” more narrowly, as “internally-generated documents evidencing Staff’s analysis, commentary, opinion or discussions about commencing proceedings”, and held that Staff was not required to disclose “Staff work product” because it was irrelevant to the issues that the Commission would consider at the merits hearing.¹⁰ In oral submissions, Staff counsel adopted a definition that is substantially similar to this narrower characterization.
- [24] That definition is more helpful, in that it more faithfully reflects the principles involved. However, like “fruits of the investigation”, the term “Staff work product” is of limited value across multiple cases, since the boundaries are not always consistently defined. In addition, each of the two categories may, depending on the context of the particular case in which the question arises, contain both relevant and irrelevant documents. Ultimately, any determination as to whether a document must be disclosed will depend on relevance, as discussed at paragraph [14] above.

⁸ The Alberta Securities Commission reached a similar conclusion in *Re Fauth*, 2017 ABASC 3 at para 55 (**Fauth**)

⁹ (2012) 35 OSCB 10957 (**Phillips**)

¹⁰ *Phillips* at para 34, citing *Shambleau v Ontario (Securities Commission)*, (2003) 26 OSCB 1629, [2003] OJ No 4089 (Div Ct)

3. By disclosing some documents that relate to an event or an issue, can Staff be taken to have conceded that it must disclose all documents relating to that event or issue?

- [25] Before turning to apply the general standard to the facts of this case, I must consider BDO's submission that by initially disclosing some documents that related to or mentioned the Compliance Reviews, Staff should be taken to have conceded that the Compliance Reviews are relevant to the allegations and that the files relating to them must therefore be disclosed in full.
- [26] BDO offered no authority for this proposition, and I reject it.
- [27] Staff's obligation to err on the side of inclusion is an important principle that promotes procedural fairness for a respondent. BDO's proposed approach could act as a disincentive for Staff to take an expansive view of relevance, because a choice to disclose one document of borderline relevance might trigger an obligation to make extensive disclosure of irrelevant documents.
- [28] Furthermore, any given document might have a portion that is clearly relevant to one of Staff's allegations, and a second portion that is irrelevant to the allegations. It would be illogical if the requirement to disclose the document because of the relevance of the first portion created an obligation to disclose documents that are irrelevant but that have a subject in common with the second portion.

C. Should Staff be required to disclose the contents of Staff's files relating to the OSC Compliance Reviews?

1. Introduction

- [29] Having established the general rule regarding Staff's obligation to make disclosure, I turn to consideration of the main issue on this motion. Specifically, should Staff be required to disclose the files relating to the OSC Compliance Reviews?
- [30] BDO's request differs from that more frequently seen on motions of this kind, where respondents want to learn about the investigation that led up to the enforcement proceeding. BDO is not seeking disclosure of documents relating to Staff's investigation of BDO. The requested disclosure is at least two steps removed from that investigation: one step because a compliance review of an entity is, by definition, distinct from the investigation that gives rise to an enforcement proceeding against that entity; and the second step because in the present case, Crystal Wealth, not BDO, was the subject of the Compliance Reviews.

2. Information reasonably available from Crystal Wealth

- [31] BDO's central submission on this motion is that the Compliance Reviews are "integral to BDO's defence as [they] will provide crucial insight into the information that was reasonably available from the Crystal Wealth Entities during the relevant period".¹¹
- [32] I do not accept that submission, for two reasons.

¹¹ BDO's written submissions, para 5

- [33] First, I see nothing in the Statement of Allegations that raises the question of what “was reasonably available from” Crystal Wealth and the Funds. Of the three allegations against BDO in this proceeding, set out in paragraph [8] above, the only one that has any apparent connection to the quantity of information obtained is the first; *i.e.*, whether the audit evidence that BDO did obtain was sufficient to comply with GAAS. However, apart from suggesting that such information would provide “context” (a suggestion I did not find persuasive), BDO did not explain why an inquiry into what information was reasonably available to BDO would assist a determination of whether what BDO did obtain was adequate. Absent a concrete explanation, and an ability for Staff to respond, it is not for me to speculate.
- [34] Second, even if an inquiry into what was reasonably available to BDO from Crystal Wealth were a proper component of Staff’s case against BDO, it is not apparent to me, and BDO did not explain, how Staff’s experience in requesting information from Crystal Wealth might assist. Staff conducts compliance reviews pursuant to the statutory authority found in section 20 of the Act, and in conducting those reviews is empowered to enter a registered firm’s premises, and to examine and make copies of the firm’s books, records and documents. An auditor’s ability to obtain and review information serves a different purpose, derives from a different source, has a different scope, is subject to different limitations, involves different considerations by the entity seeking information, and leads to different outcomes if difficulties are encountered. All of those differences would prompt different considerations by Crystal Wealth or its principals in responding to requests for information. In my view, the distinctions are numerous and fundamental, and any connection there might be is too tenuous to establish the necessary degree of relevance.

3. Overlap between BDO’s audits and the Compliance Reviews

- [35] BDO seeks to strengthen the connection between its audit work and the work underlying the Compliance Reviews, by submitting that the Compliance Reviews were “regarding many of the same issues underlying Staff’s current allegations against BDO”,¹² and that Staff was “engaged in a substantially similar exercise to the audits conducted by BDO.”¹³
- [36] Staff disagrees. In response, Staff submits that a compliance review is primarily an operational review to assess a registered firm’s compliance with Ontario securities law. A compliance review extends to such things as supervision, marketing, disclosure of fees and commissions, and responses to previously identified compliance deficiencies. While Staff will typically review the firm’s financial statements to assess the firm’s financial condition and its compliance with capital requirements, a compliance review is not, and does not include, an audit of the firm’s financial statements; nor does it provide any assurance about those statements.
- [37] I prefer Staff’s submission. BDO and Staff were engaged in very different exercises.
- [38] BDO submits, and I agree, that an evaluation of its compliance with GAAS would necessarily include consideration of its assessment as to Crystal Wealth’s

¹² BDO’s written submissions, para 11

¹³ BDO’s written submissions, para 16

compliance with GAAP, since that is an essential component of an audit. It is also true that Staff, when conducting a compliance review, would likely do some work to assess compliance with GAAP, in order to support a conclusion as to the firms' compliance with capital requirements, for example.

- [39] However, the fact that BDO's audits considered some of the same things that Staff looked at in the Compliance Reviews does not establish that access to the Compliance Review files might assist BDO in defending the allegation that BDO failed to comply with GAAS. According to the Statement of Allegations, the standard against which BDO will be measured is GAAS, not the manner in which Staff discharged a very different, and much broader, obligation.
- [40] At the hearing of this motion, BDO suggested other potential defences that it might assert: "that even a nominal defect [in the audits] would have had no impact on GAAP; that the context was such that the audits were, in the ultimate conclusion, absolutely correct; that there was no harm to the public or to investors; and that the underlying thrust of all of these allegations is without merit."¹⁴ I fail to see a link between any of these potential defences and the Compliance Reviews.

4. Staff's actions in connection with the Compliance Reviews

- [41] This absence of a connection is further highlighted by BDO's written submissions:
- ...BDO is not able to understand the basis upon which OSC and BCSC Staff conducted their reviews, including, critically, the reasons that Staff did not take issue with Crystal Wealth's operations on the same issues which underlay the allegations against BDO. BDO has no insight into any decisions by OSC and BCSC Staff to conclude their reviews without further inquiries or conditions imposed upon Crystal Wealth.¹⁵
- [42] Any decision made by Staff as to how to proceed during or following a compliance review is dependent on a number of factors. Many of those factors (*e.g.*, available resources, competing priorities, applicable regulatory standards) are entirely unrelated to the question of whether BDO's audits complied with GAAS. The process of gaining "insight into" Staff's decisions with respect to the Compliance Reviews would be a fishing expedition that the disclosure obligation is not designed to enable, and that process would not assist in determining the sufficiency of the steps that BDO took during the audits.
- [43] This is consistent with the Commission's decision in *Phillips*, discussed above in paragraph [23]. The opinion of a non-expert member of Staff would have no probative value before the Commission as to whether BDO complied with GAAS. This would be so even if the Staff member's opinion were squarely on that central issue; *i.e.*, the very issue that the Commission is responsible for deciding. It would be equally if not even more the case if that opinion were with respect to a different issue; *e.g.*, whether the firm was in compliance with its capital requirements.

¹⁴ Hearing Transcript, *BDO Canada LLP (Re)*, May 3, 2019, at 32, lines 12-17

¹⁵ BDO's written submissions, para 34

5. Conclusion about the Compliance Reviews generally

[44] BDO's submissions on this motion imagine a more wide-ranging set of allegations than are contained in the Statement of Allegations. Any determination of relevance must be made with reference to the allegations as they are, not as they are imagined to be. At the hearing on the merits, Staff's case will be limited by the boundaries of the Statement of Allegations as drafted. Accordingly, it would be inappropriate to order disclosure based on some broader but non-existent version.

[45] Within the confines of the Statement of Allegations as drafted, and for the reasons set out above, I agree with Staff's submission that documents, or portions of documents, that are contained in the Compliance Review files and that reflect Staff's commentary, opinion, analysis, guidance to field review teams, and similar content, are not relevant and need not be disclosed.

D. If Staff's disclosure obligation does extend to include the file contents of the OSC Compliance Reviews, what steps if any should Staff be required to take with respect to BCSC Staff's files relating to the BCSC Compliance Reviews?

[46] BDO submits that Staff did not take sufficient steps to obtain from BCSC Staff the files relating to the BCSC Compliance Reviews.

[47] I have no basis to conclude that the nature or scope of the BCSC Compliance Reviews are distinct from the OSC Compliance Reviews in any way that is related to the issues on this motion. Given my decision that the OSC Compliance Reviews are not relevant to the allegations against BDO and therefore are not subject to disclosure, the same conclusion would apply to the BCSC Compliance Reviews. Therefore, I need not consider the issue of whether Staff should be required to take any steps to obtain the BCSC Compliance Review files.

E. Should Staff be required to disclose documents that pre-date January 1, 2012?

[48] BDO objects to Staff's decision not to disclose documents dated on or before December 31, 2011. Staff submits that it has erred on the side of inclusion by disclosing documents for the three years preceding each of the impugned audits. For example, while documents created in 2013 are relevant to the audit as at and for the year ending December 31, 2014, it is not clear that documents created in 2012 would be relevant. Nonetheless, Staff has disclosed such documents.

[49] Staff drew the line, however, at three years. Absent a reason to believe that any documents created more than three years before the audit date would be relevant, I can see no basis to require disclosure. BDO provides no specific reason; rather, it submits that such documents would provide "relevant context". Without more, that assertion is insufficient for me to conclude that Staff's chosen cut-off date is improper.

IV. CONCLUSION

[50] For the reasons set out above, I concluded that the Compliance Reviews are not relevant for the purposes of disclosure, and I dismissed BDO's motion. However, some parting comments are necessary with respect to the disclosure that has been made.

- [51] At the hearing of the motion, Staff advised that it has erred on the side of inclusion and has already disclosed all externally gathered evidence, and all documentation of communications with external third parties. Staff has not disclosed notes of internal meetings or discussions, internal guidance to field team reviewers, internal analyses generated following the Compliance Reviews, or drafts of any of the foregoing.
- [52] Staff also asserted that it has redacted some information on some documents it has disclosed. These redactions have been made in order to conceal information in a manner consistent with the narrower definition of "Staff work product" referred to in paragraph [23] above.
- [53] Staff's actions, as described, are consistent with these reasons. However, after hearing these assertions by Staff, BDO's counsel expressed skepticism as to whether Staff had in fact fully complied with Staff's own view of what should be disclosed. Those reservations were based on inferences drawn from references in documents that were disclosed. In response, Staff counsel repeated his belief that Staff had fully complied, but he was unable to be absolutely unequivocal, given that the Staff members involved with this matter have changed over time.
- [54] I was not directed to any basis upon which I could conclude that Staff has not made the necessary disclosure. I did express orally to Staff at the hearing my view that no matter the outcome of the motion, Staff should double-check the accuracy of Staff counsel's statements and the completeness of Staff's disclosure. If Staff has not yet done so, it should do that promptly, and should communicate with BDO's counsel as necessary.
- [55] I am grateful for the thorough submissions and able assistance of all counsel on this motion.

Dated at Toronto this 6th day of June, 2019.

"Timothy Moseley"
Timothy Moseley