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**BULLETIN # 3448**

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## Discipline

### Discipline Penalties Imposed on Richard Reynaud Gareau; Violation of Regulation 1300.1 (a) and 1300.1 (c) (now Regulation 1300.1(q)).

Person Disciplined	A Hearing Panel appointed pursuant to IDA By-law 20 has imposed discipline penalties on Richard Reynaud Gareau (“Gareau”) at all material times a Registered Representative (“RR”) at the Prince Albert, Saskatchewan sub-branch office of Credential Securities Inc. (“Credential”), a Member of the Association.
By-laws, Regulations, Policies Violated	In a written decision released on July 29, 2005, which followed a disciplinary hearing held on February 14 and June 20, 2005 in Prince Albert, Saskatchewan, a Hearing Panel found that Gareau violated Association Regulation 1300.1 (a) in that he failed to use due diligence to learn the essential facts relative to orders accepted in that he did not adequately inform himself as to the nature or details of a Bell Canada International Inc. 6.75% Convertible Subordinated Debenture due February 15, 2002 (“BCI Deb”) before recommending the purchase of this security to as many as fourteen (14) of his clients.  The Hearing Panel further found that Gareau failed to use due diligence to ensure that the recommendations made for the accounts of fourteen (14) of his clients were appropriate for those clients and in keeping with their investment objectives, contrary to Association Regulation 1300.1 (c).  The panel dismissed the other allegation against Gareau which alleged that he failed to disclose features of the BCI Deb to his clients before recommending the purchase of this security to as many as fourteen (14) of his clients, contrary to Association By-law 29.1.
Penalty Assessed	The Hearing Panel imposed a fine of \$20,000 against Gareau (\$10,000 for each violation). The Hearing Panel ordered that Gareau pay \$5,000 towards the Association’s costs of this matter. The Hearing Panel further ordered that Gareau is prohibited from re-approval in the securities industry until the fine and costs have been paid in full. Finally, the Hearing Panel stated that it understood that Association

regulations will require Gareau to write and pass exams related to the Canadian Securities Course and the Conduct and Practices Handbook because he has not been registered for more than three years. If this requirement had not been in place, the Hearing Panel would have made an order to that effect.

## Summary of Facts

The facts of the case, which were all agreed upon by both the Association and Gareau, stated that Gareau was employed as a RR from May 23, 2000 to July 2, 2002. He was supervised by Spencer Edward Graham (“Graham”) who worked out of Credential’s Regina, Saskatchewan office.

Gareau does not have any prior disciplinary history.

### *BCI Deb*

On February 10, 1999, Bell Canada International (“BCI”) issued a prospectus (the “Prospectus”) for the issuance of a BCI Convertible Subordinated Debenture due February 15, 2002 (the “BCI Deb”). The Prospectus stated that on the maturity date, BCI may, at its option, elect to satisfy its obligation to repay the principal amount by delivery of common shares of BCI. The Prospectus contained a risk section that is eight pages in length.

On March 13, 2001, BCI filed an Annual Information Form (“AIF”) for the year ended December 31, 2000. The AIF stated that BCI’s parent company is a wholly owned subsidiary of Bell Canada Enterprises (“BCE”). The AIF stated further that the BCI Deb is unsecured and convertible on the maturity date into common shares of BCI. As a risk factor, the AIF stated that BCI experienced losses in the past and may incur additional losses in the foreseeable future.

Both the Prospectus and the AIF were available on the System for Electronic Document Analysis and Retrieval (“SEDAR”).

Gareau recommended the BCI Deb to 14 of his clients. At the material time, there was less than a year to maturity of the BCI Deb. With a 6.75% coupon rate and trading below par, the BCI Deb had a significantly higher yield than the six-month T-Bill rate of 4.10% or the one-year GIC rate of 3.18% that were available on July 31, 2001. Further, BCI common shares dropped over 99% in value in the period from January 2001 to January 2003. In particular, from January 2001 to July 2001 the BCI common share value had dropped by about 50%. Moody’s Investors Service assigned a B3 rating to the BCI Deb. A B3 rating from Moody’s is described as highly speculative.

### *Due Diligence*

Although Gareau looked on SEDAR, he did not notice either the Prospectus or the AIF. Gareau did not know that the Prospectus existed, nor did he have any knowledge of any financial information for BCI, including the value of the underlying BCI common shares. On July 25, 2001, Gareau telephoned Graham to ask him about his thoughts regarding the BCI Deb. Graham advised Gareau that “it’s Bell, so it should be fine.”

On July 30, 2001, Gareau received a faxed Information Sheet regarding the BCI Deb from Merrill Lynch. This sheet made reference to the Prospectus and stated that the BCI Deb was, at the option of BCI, convertible into the common shares of BCI. Gareau confirmed that he had received this information sheet. While he was initially alarmed that the security was convertible at BCI's option, he was comforted that the conversion would be into BCI common shares. He made no further inquiries about BCI or the BCI Deb. Gareau did not think that this conversion was likely.

Gareau felt that the BCI Deb was an attractive, very low-risk investment, especially at the initial stages of investing, because it was trading at a discount, had a very reasonable rate of return and it was subsidiary of Canada's largest telecommunications company. He relied on Graham's opinion, along with the opinion of the Merrill Lynch bond desk, and the fact that Bell Canada had lent its name to BCI. Gareau focused on the inherent strength of Bell Canada Enterprises as he felt that corporate responsibility would fall on Bell Canada Enterprises if BCI was unable to pay the debt.

On July 27, 2001, Gareau began purchasing the BCI Deb for his clients and eventually sold the security to 14 clients in addition to selling it to members of his family. The BCI Debenture accounted for approximately 15% of Gareau's book.

The essence of Gareau's defence was that he believed the BCI Deb to be a low risk investment and he relied on the advice of Graham, his superior, who was held out to be an expert.

The Hearing Panel found that, while in some circumstances reliance upon a person like Graham might meet the requirements of due diligence notwithstanding that a Registered Representative has a responsibility to his clients to ensure a reasonable amount of independent due diligence, the reliance upon Graham in this case did not absolve Gareau of his responsibility. The conclusion may have been different had Gareau not received indications that the BCI Deb might not be the solid investment he perceived it to be. While the reliance on Graham was an important factor in this case, this reliance did not absolve Gareau.

#### *Unsuitable Investment Recommendations*

The investment objectives of the 14 clients to whom Gareau recommended the BCI Deb demonstrated that clearly all or virtually all of the investors sought low risk investments. Many were unsophisticated investors who indicated to Gareau that their main concern was to preserve capital or have liquidity. In particular, one client stressed to Gareau that they could not afford to lose "one red cent" of their investment. Another investor intended to use her money in the investment to pay her income tax. Others saw the BCI Deb as a short term investment of retirement funds, some intending to retire within a very short period of time. Also, for several of the investors, their investment in the BCI Deb on Gareau's advice represented a significant proportion of their net worth.

The Hearing Panel found that the clients' objective to buy low risk investments was anything but ambiguous. Because of Gareau's failure to exercise due diligence, he did not ensure that his recommendations were appropriate for his clients and in keeping with their investment objectives.

The total losses incurred by the 14 clients as a result of Gareau's recommendation of the BCI Deb to them was \$724,803.46. He did not earn any commissions as a result of these sales as he was a salaried employee of Credential.

*Count Not Made Out*

Another count alleged that Gareau breached Association By-law 29.1 by failing to disclose features of the BCI Deb before recommending its purchase to his clients. The relevant feature that Gareau allegedly did not disclose was that the BCI Deb was convertible into the common shares of BCI at maturity.

A majority of the Hearing Panel found that there was no breach in this case. By-law 29.1 is intended to focus primarily on quasi-criminal and unethical conduct rather than negligent conduct. There was no evidence that Gareau acted unethically in the sense that he acted for an improper purpose. If anything, this was a case of negligence rather than one of personal gain or conflict of interest. Accordingly this allegation was dismissed.

*Penalty*

In assessing the penalty in this matter, the Hearing Panel found that, as a RR, Gareau had a duty to exercise care in assessing investment vehicles for his clients. This duty included taking steps to fully understand the essential nature of investments (due diligence) and to determine whether the investment was appropriate given the clients' stated objectives. Gareau fell short in these areas. A significant amount of money was lost by clients as a result of his conduct and he continued to make recommendations causing greater losses, even after information was brought to his attention which might cause a reasonable person to reconsider their initial advice. On the other hand, Gareau's responsibility is diminished by the fact that he placed reliance on the advice given to him by Graham. It is completely understandable and expected that the advice of an internal expert in the firm should be relied upon. The Hearing Panel found that the reliance does not extend to fully exculpate Gareau, but they also found that it did diminish somewhat his personal responsibility. In addition, this was the first instance of disciplinary action brought against Gareau.

Gareau has not been employed in the securities industry since July 2, 2002.

Please see Association Bulletin # 3434 for the disciplinary action taken against Graham in respect of this matter.

Kenneth A. Nason  
*Association Secretary*