IN THE MATTER OF A DISCIPLINE HEARING
PURSUANT TO BY-LAW 20 OF THE INVESTMENT DEALERS
ASSOCIATION OF CANADA

Re:  BMO NESBITT BURNS INC.
RBC DOMINION SECURITIES INC.
TD WATERHOUSE (CANADA) INC.

Heard:  December 16, 2004

District Council:   The Honourable Lloyd W. Houlden, Q.C.
Robert J. Guilday
F. Michael Walsh

Appearances:
For Investment Dealers Association:  Jeffery Kehoe, Natalia Popovic, Belle Kaura
For BMO Nesbitt Burns:  Sharon Haward-Laird
For RBC Dominion Securities:  Jeremy Devereux
For TD Waterhouse (Canada) Inc.:  James C. Tory

DECISION AND REASONS

This hearing proceeded pursuant to Settlement Agreements as joint submissions. The Settlement Agreements are reproduced below:

BMO NESBITT BURNS INC.
SETTLEMENT AGREEMENT

I.  INTRODUCTION

1. The Enforcement Department Staff ("Staff") of the Investment Dealers Association of Canada ("the Association") has conducted an investigation (the "Investigation") into the conduct of BMO Nesbitt Burns Inc. ("the Respondent").
2. The Investigation discloses matters for which the Respondent may be disciplined by a Hearing Panel of the Association, pursuant to Association By-law 20, Part 10 ("Hearing Panel").

II. JOINT SETTLEMENT RECOMMENDATION

3. Staff and the Respondent consent and agree to the settlement of these matters by way of this Settlement Agreement (the "Settlement Agreement") in accordance with By-laws 20.35 to 20.40, inclusive and Rule 15 of the Rules of Practice and Procedure.

4. The Settlement Agreement is subject to acceptance by the Hearing Panel.

5. The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.

6. The Settlement Agreement will be presented to the Hearing Panel at a hearing (the "Settlement Hearing") for its approval. Following the conclusion of the Settlement Hearing, the Hearing Panel may either accept or reject the Settlement Agreement.

7. If the Hearing Panel accepts the Settlement Agreement, the Respondent waives its rights under Association By-laws and any applicable legislation to a disciplinary hearing, review or appeal.

8. If the Hearing Panel rejects the Settlement Agreement, Staff and the Respondent may enter into another settlement agreement; or Staff may proceed to a disciplinary hearing in relation to the disciplinary matters disclosed in the Investigation.

9. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel.

10. Staff and the Respondent agree that if the Hearing Panel accepts the Settlement Agreement, they, or anyone on their behalf, will not make any public statements inconsistent with the Settlement Agreement. Nothing in this section is intended to restrict the Respondent from making full answer and defence to any civil proceedings against it.

11. Staff and the Respondent jointly recommend that the Hearing Panel accept the Settlement Agreement.

12. If the Hearing Panel rejects this Settlement Agreement:

   i. The provisions of By-law 20.10 to 20.24, inclusive, shall apply, provided that no member of the Hearing Panel rejecting this Settlement Agreement shall participate in any hearing conducted by a Hearing Panel with respect to the same matters which are the subject of the Settlement Agreement;
and

ii. This Settlement Agreement and the negotiations relating thereto shall be confidential and without prejudice and may not be used as evidence or referred to in any hearing.

III. STATEMENT OF FACTS

Acknowledgment

13. Staff and the Respondent agree with the facts set out in this Section III for the purposes of this Settlement Agreement only and further agree that this agreement of facts is without prejudice to the Respondent or Staff in any other proceeding of any kind, including, but without limiting the generality of the foregoing, any proceedings brought by the Association or any civil or other proceedings which may brought by any other person or agency. No other person or agency may raise or rely upon the terms of this Settlement Agreement or any agreement to the facts stated herein whether or not this Settlement Agreement is approved by the Hearing Panel.

A. DEFINITION - MARKET TIMING

14. "Market timing" is a term denoting particular market practices and includes (a) frequent buying and selling of units of the same mutual fund (and only holding for a few days) or (b) buying or selling of mutual fund units in order to exploit inefficiencies in the pricing of mutual funds ("Market Timing").

15. Market Timing, while not illegal per se, can adversely affect mutual fund unitholders by diluting the value of mutual fund units to the extent that a market timer is permitted to buy and sell units frequently and take advantage of pricing inefficiencies.

16. Frequent purchases, redemptions and switches can raise transaction costs for funds, generate taxable capital gains for unitholders, disrupt portfolio management strategies and investment style and can force fund managers to sell investments under less than favourable conditions. Market Timing activities can also cause managers to increase borrowing and/or hold a larger cash reserve than necessary or desirable, resulting in diminished returns for long-term investors.

B. SUMMARY of MARKET TIMING ACTIVITY and REVENUE

17. The Respondent was at all material times a Member of the Association with its head office located in Toronto, Ontario.
18. From January 1st, 2002 to December 31st, 2003 (the "Relevant Period") the Respondent executed potentially harmful Market Timing activities.

**i) Accounts Involved**

19. During the Relevant Period the Respondent executed Market Timing activities by four clients through four retail accounts ("the "Clients") and through a proprietary account (the "Proprietary Account") of the Respondent.

20. During the Relevant Period the Respondent executed Market Timing activities for the Clients in transacting in excess of 3,500 round trips (a transfer and return, i.e. 2 trades, of substantially all of the assets invested in a particular mutual fund ("Round Trip")). The Clients market timed in excess of 50 mutual funds within approximately 15 mutual fund companies.


22. The average hold period with respect to a given mutual fund position in the Clients' accounts and the Proprietary Account was fewer than 5 days (the industry norm for minimum hold periods pursuant to standard simplified prospectus language is 90 days).

**ii) Revenue From Market Timing**

23. The Respondent's total gross revenue derived, directly or indirectly, from the Clients' Market Timing activities and the Proprietary Account during the Relevant Period are as follows:

<table>
<thead>
<tr>
<th>Gross Market Timing Revenue</th>
<th>Retail Accounts</th>
<th>Proprietary Accounts</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>$</td>
<td>$</td>
<td>$</td>
<td>$</td>
</tr>
<tr>
<td>Fees/ Commissions</td>
<td>837,302.98</td>
<td>Nil</td>
<td>837,302.98</td>
</tr>
<tr>
<td>Interest Profit</td>
<td>2,563.62</td>
<td>Nil</td>
<td>2,563.62</td>
</tr>
<tr>
<td>Transactional Fees</td>
<td>162,746.00</td>
<td>Nil</td>
<td>162,746.00</td>
</tr>
<tr>
<td>Trailer Fees</td>
<td>251,445.00</td>
<td>97,512.00</td>
<td>347,500.00</td>
</tr>
<tr>
<td>Hedging Profits</td>
<td>Nil</td>
<td>840,000.00</td>
<td>840,000.00</td>
</tr>
<tr>
<td>Proprietary Trading Profits</td>
<td>Nil</td>
<td>1,111,405.00</td>
<td>1,111,405.00</td>
</tr>
<tr>
<td><strong>Total Gross Market Timing Revenue</strong></td>
<td>$1254,057.60</td>
<td>$2,048,917.00</td>
<td>$3,302,974.60</td>
</tr>
</tbody>
</table>
C. THE MARKET TIMING STRATEGY

i) MARKET TIMING ACTIVITIES OF THE CLIENTS—RETAIL

24. The Clients were offshore entities and sophisticated investors that employed a Market Timing strategy.

25. The Market Timing activities executed by the Respondent on behalf of the Clients were in the absence of any special arrangements with mutual fund companies.

26. The value of the aggregate transactions of the Clients was in the range of $90,000 to $1 million.

27. The average time that the mutual fund positions were held in the Clients' accounts was fewer than 5 days.

28. The Respondent received at least 21 written warnings regarding the Market Timing activities in the Clients' accounts. The Respondent notified the Clients of the receipt of the written warnings and the Clients made the determination as to whether or not to continue their activities in that particular mutual fund or mutual fund company.

29. Following the receipt of a written warning from a mutual fund, the Respondent permitted the Clients to continue Market Timing activities in the same mutual fund, in a different mutual fund within the same mutual fund company or a different fund in a different mutual fund company.

30. Despite the receipt of written warnings from several mutual fund companies that were market timed, the Respondent permitted the Clients to continue Market Timing activities.

31. There has been no Market Timing activity in the accounts of the Clients since the fall of 2003.

ii) MARKET TIMING ACTIVITIES IN THE PROPRIETARY ACCOUNT—INSTITUTIONAL

32. The Respondent, through an in house account, employed a Market Timing strategy.

33. During the Relevant Period, the Respondent, through its Proprietary Account, market timed 25 mutual funds within 7 mutual fund companies, including BMO Mutual Funds, for the Respondent's Proprietary Account.

34. The substantial majority of the Market Timing activity by the Respondent occurred in one mutual fund and was conducted by means of a written special arrangement with a mutual fund company. The balance of the Market Timing activity was conducted in the absence of any special arrangements with mutual fund companies.
35. The written special arrangement, entered into between the Respondent and the mutual fund company essentially allowed the Respondent to trade all funds of the mutual fund company without a minimum hold period for a fee which was significantly less than the maximum fee which could have been charged by the mutual fund company pursuant to the funds' simplified prospectus. In turn, the Respondent had to comply with a limit on the number of monthly switches and keep a minimum amount of assets in the funds, otherwise an early redemption fee would apply.

36. The value of the transactions in the in house account was in the range of approximately $400,000 to $10 million.

D. **WRITTEN WARNINGS**

37. The Respondent received at least 21 written warnings from approximately 15 mutual fund companies in respect of the Clients.

38. The majority of the written warnings put the Respondent on notice that Market Timing was potentially harmful to long term unitholders, was not welcome or permitted by the funds and that the mutual fund companies may impose a short term trading fee of up to 2% of the value of the mutual fund units that were held for fewer than 90 days, in accordance with the funds' prospectuses.

39. The language of the majority of the written warnings confirmed that the objective of the short term trading fee was to protect long term unitholders from potentially negative consequences of Market Timing. The mutual fund companies issued the warnings because they had determined that Market Timing was potentially harming the funds and the long term unitholders.

40. Despite the issuance of multiple written warnings by mutual fund companies, the Respondent failed to prevent its' Clients from continuing to market time the mutual funds.

E. **SUPERVISION**

41. Mutual fund companies bear responsibility for identifying and preventing Market Timing; brokerage industry distributors were willing participants in a practice that was potentially harmful to the long term unitholders of the mutual funds.

42. The Respondent failed to implement supervisory systems to address the red flags and thereby detect and prevent potentially harmful market timing practices. Specifically, the Respondent failed to implement supervisory systems to:

   i) adequately supervise the activities of its employees, and
ii) conduct adequate due diligence into the activities of its' employees and clients, in these circumstances.

43. The Respondent failed to take adequate steps to respond to red flag warning signals that it was facilitating the Client, and was itself (through the Proprietary Account), engaging in potentially harmful Market Timing activities.

F. MITIGATING FACTORS

44. In September 2003, regulators in the United States announced investigations into market timing trading practices at mutual funds in the United States. In November 2003, the Ontario Securities Commission ("OSC") launched a review into mutual fund market timing practices in Ontario. In January 2004, the Association sent surveys regarding market timing to its Member Firms. The majority of Member Firms did not have policies or procedures in place to detect or prevent Market Timing activities.

45. The Respondent voluntarily notified the provincial securities regulator of the Market Timing activities in the Proprietary Account.

46. The Respondent repaid the gross trading revenues earned from the Market Timing activity in the Proprietary Account to the respective mutual funds. The payment to the mutual funds was made prior to initiation of the Association investigation and on a voluntary basis.

47. All Market Timing activities of the Clients and of the Respondent in the Proprietary account ceased voluntarily prior to the initiation of the Association investigation.

48. The Respondent co-operated fully with the Association during the course of the investigation.

IV. CONTRAVENTIONS

49. The Respondent admits to the following contraventions of Association By-laws, Regulations, Rulings or Policies:

i. During the period from January 1st 2002 to December 31st 2003, the Respondent failed to implement supervisory systems to address the red flags and thereby detect and prevent potentially harmful Market Timing activities. Specifically, the Respondent failed to implement supervisory systems to:
a) adequately supervise the activities of its employees; and

b) conduct adequate due diligence into the activities of its employees and clients in these circumstances,

and thereby was in violation of Association Regulations 1300.2 and 1300.1(o) and Policy 2.

V. TERMS OF SETTLEMENT

50. The Respondent agrees to the following terms of settlement:

i. Penalties

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Disgorgement of Gross Market Timing Revenues</td>
<td>$3,302,974.59</td>
</tr>
<tr>
<td>(ii) Fine in the amount of</td>
<td>$3,302,974.59</td>
</tr>
<tr>
<td>(iii) Costs</td>
<td>$50,000.00</td>
</tr>
</tbody>
</table>

Sub Total: $6,655,949.18

Less:

Credit in recognition of co-operation

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Fine not applied to Hedging Profit</td>
<td>($840,000.00)</td>
</tr>
<tr>
<td>(ii) Reduction in fine to Proprietary Trading Profits</td>
<td>($1,111,404.99)</td>
</tr>
<tr>
<td>Voluntarily Distributed Back to Mutual Funds</td>
<td></td>
</tr>
<tr>
<td>(iii) Proprietary Trading Profits Voluntarily Distributed</td>
<td>($1,110,404.99)</td>
</tr>
<tr>
<td>Back to Mutual Fund</td>
<td></td>
</tr>
</tbody>
</table>

Sub Total: ($2,962,809.98)

Total: $3,693,139.20
The Respondent will set up an internal committee to consider how to identify and address emerging issues in the securities industry. The Respondent will consult with the Association in setting up the mandate of the committee.

51. Unless otherwise stated, any monetary penalties and costs imposed upon the Respondent is payable immediately upon the effective date of the Settlement Agreement.

52. Unless otherwise stated, any suspensions, bars, expulsions, restrictions or other terms of the Settlement Agreement shall commence on the effective date of the Settlement Agreement.

RBC DOMINION SECURITIES INC.
SETTLEMENT AGREEMENT

I. INTRODUCTION

1. The Enforcement Department Staff ("Staff") of the Investment Dealers Association of Canada ("the Association") has conducted an investigation ("the Investigation") into the conduct of RBC Dominion Securities Inc. ("the Respondent").

2. The Investigation discloses matters for which the Respondent may be disciplined by a Hearing Panel of the Association, pursuant to Association By-law 20, Part 10 ("Hearing Panel").

II. JOINT SETTLEMENT RECOMMENDATION

3. Staff and the Respondent consent and agree to the settlement of these matters by way of this settlement agreement (the "Settlement Agreement") in accordance with Association By-laws 20.35 to 20.40, inclusive and Rule 15 of the Rules of Practice and Procedure.

4. The Settlement Agreement is subject to acceptance by the Hearing Panel.

5. The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.

6. The Settlement Agreement will be presented to the Hearing Panel at a hearing (the
"Settlement Hearing") for its approval. Following the conclusion of the Settlement Hearing, the Hearing Panel may either accept or reject the Settlement Agreement.

7. If the Hearing Panel accepts the Settlement Agreement, the Respondent waives its right under the Association By-laws and any applicable legislation to a disciplinary hearing, review or appeal.

8. If the Hearing Panel rejects the Settlement Agreement, Staff and the Respondent may enter into another settlement agreement; or Staff, may proceed to a disciplinary hearing in relation to the disciplinary matters disclosed in the Investigation.

9. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel.

10. Staff and the Respondent agree that if the Hearing Panel accepts the Settlement Agreement, they, or anyone on their behalf, will not make any public statements inconsistent with the Settlement Agreement. Nothing in this section is intended to restrict Respondent from making full answer and defence to any civil proceedings against it.

11. Staff and the Respondent jointly recommend that the Hearing Panel accept the Settlement Agreement.

12. If the Hearing Panel rejects this Settlement Agreement:

   i. The provisions of By-law 20.10 to 20.24, inclusive, shall apply, provided that no member of the Hearing Panel rejecting this Settlement Agreement shall participate in any hearing conducted by a Hearing Panel with respect to the same matters which are the subject of the Settlement Agreement; and

   ii. This Settlement Agreement and the negotiations relating thereto shall be confidential and without prejudice and may not be used as evidence or referred to in any hearing.

III. STATEMENT OF FACTS

Acknowledgment

13. Staff and the Respondent agree with the facts set out in this Section III for the purposes of this Settlement Agreement only and further agree that this agreement of facts is without prejudice to the Respondent or Staff in any other proceeding of any kind including, but without limiting the generality of the foregoing, any proceedings brought by the Association or any civil or other proceedings which may be brought by any other person or agency. No other person or agency may raise or rely upon the terms of this Settlement Agreement or any agreement to the facts stated herein whether or not this Settlement Agreement is approved by the Hearing Panel.
A. DEFINITION - MARKET TIMING

14. "Market Timing" is a term denoting particular market practices and includes (a) frequent buying and selling of units of the same mutual fund and holding only for a few days or (b) buying or selling of mutual fund units in order to exploit inefficiencies in the pricing of mutual funds ("Market Timing").

15. Market Timing, while not illegal per se, can adversely affect mutual fund unitholders by diluting the value of mutual fund units to the extent that a market timer is permitted to buy and sell units frequently and take advantage of pricing inefficiencies.

16. Frequent purchases, redemptions and switches can raise transaction costs for funds, generate taxable capital gains for unitholders, disrupt portfolio management strategies and investment style and can force fund managers to sell investments under less than favourable conditions. Market Timing activities also can cause managers to increase borrowing and/or hold a larger cash reserve than necessary or desirable, resulting in diminished returns for long-term investors.

B. SUMMARY of MARKET TIMING ACTIVITY and REVENUES

17. The Respondent was at all material times a Member of the Association with its head office located in Toronto, Ontario.


i) Market Timing Activity

19. During the Relevant Period, the Respondent executed Market Timing activities by two retail clients through two retail accounts ("Client A" and "Client B" or collectively the "Clients").

20. The Clients had arrangements with some of the fund companies whose funds they traded that were reduced in whole or in part to writing. The written terms varied from case to case. The arrangements generally reduced or waived fees for short term trading, switching or early redemptions of funds. Several of the arrangements were restricted to specific funds, set limits on the amount that could be invested in each fund or limited the number of switches between funds permitted in a given time period.
ii) Revenues From Market Timing

21. The Respondent's total gross revenues derived, directly and indirectly, from the Clients' Market Timing activities during the Relevant Period are as follows:

<table>
<thead>
<tr>
<th>Gross Market Timing Revenues</th>
<th>Client A</th>
<th>Client B</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest Revenue</td>
<td>$1,119,920.00</td>
<td>$47,103.41</td>
<td>$1,167,023.41</td>
</tr>
<tr>
<td>Management Fees</td>
<td>$3,393,754.00</td>
<td>$165,790.00</td>
<td>$3,559,544.00</td>
</tr>
<tr>
<td>Trailer Fees</td>
<td>$3,563,681.00</td>
<td>$172,402.63</td>
<td>$3,736,083.63</td>
</tr>
<tr>
<td><strong>Total Gross Market Timing Revenues</strong></td>
<td><strong>$8,077,355.00</strong></td>
<td><strong>$385,296.04</strong></td>
<td><strong>$8,462,651.04</strong></td>
</tr>
</tbody>
</table>

C. THE MARKET TIMING STRATEGY

i) CLIENT A

a) Background

22. Client A was an offshore entity and a sophisticated investor that employed a Market Timing strategy.

23. During the Relevant Period, the Respondent executed the Market Timing activities for Client A in excess of 56 mutual funds within approximately 11 mutual fund companies.

24. The trading activities of Client A were conducted by means of written special arrangements with 7 mutual fund companies. The balance of the trading was conducted in the absence of any written special arrangements.

25. The written special arrangements, entered into between the Clients and the mutual fund companies essentially allowed the Client to trade funds of the mutual fund company without a minimum hold period for a fee which was significantly less than the maximum fee which could have been charged by the mutual fund company pursuant to the funds' simplified prospectus. In turn, the Clients had to comply with a limit on the number of monthly switches and keep a minimum amount of assets in the funds, otherwise an early redemption fee would apply.

26. The Respondent executed in excess of 3900 Market Timing Trades on behalf of Client A.

27. The value of the aggregate transactions of Client A ranged from $500,000 to $54,800,000.

28. The average hold period with respect to a given mutual fund position in Client A's account was fewer than 5 days (the industry norm for minimum hold periods pursuant to standard simplified prospectus language is 90 days).
29. Despite the receipt of written warnings from several mutual fund companies, the Respondent permitted Client A to continue the Market Timing activities.

**b) Royal Mutual Funds**

30. During the Relevant Period, for a period of three months, January, February and March 2002, the Respondent executed Market Timing activities of Client A in three funds of Royal Mutual Funds Inc. ("Royal").

31. Over the three month period, the Respondent executed 42 Market Timing Trades on behalf of Client A in three Royal funds.

32. The average value of the transactions in the Royal funds was approximately $1.6 million.

33. The average hold period with respect to Client A's investments in the Royal funds was 5 days.

34. On or about March 28, 2002, an e-mail to the Respondent confirmed an understanding by Royal that Market Timing activities in the Royal funds by Client A would cease immediately and that all units held by Client A would be redeemed by March 28, 2002.

35. In May 2003, an investment advisor employed by the Respondent approached Royal with a proposal for a special arrangement to conduct Market Timing activities on behalf of Client A. The investment advisor advised Royal that such a trading model had been reviewed and accepted by the Respondent's compliance department and had been in place with 10 other mutual fund companies for years.

36. Royal did not accept the proposal.

**ii) CLIENT B**

37. Client B was an offshore entity and a sophisticated investor that employed a Market Timing strategy.

38. During the Relevant Period, the Respondent executed the Market Timing activities for Client B by permitting trading in excess of 34 mutual funds within approximately 9 mutual fund companies.


40. The value of the transactions in Client B's account as a whole ranged from approximately $569,000 to $8,240,000.

41. The average hold period with respect to a given mutual fund position in Client B's account was fewer than 5 days.
42. Despite the receipt of written warnings from several mutual fund companies, the Respondent permitted Client B to continue Market Timing activities.

iii) SOVEREIGN INVESTMENT PROGRAM

43. During the Relevant Period, the Respondent also marketed and distributed 7 pools of mutual funds in the Sovereign Investment Program ("Program"); a pool consisted of 3 classes of units.

44. The Respondent was one of only 4 exclusive distributors of the Program. The Respondent executed the Clients market timing of two of the pools.

45. The Respondent executed approximately 16 Market Timing Trades in the Program within a 2 month period on behalf of Client A and 24 Market Timing Trades in the Program within a 5' month period on behalf of Client B.

46. The average value of the transactions by Client A in one of the pools of the Program was approximately $1 million and approximately $3.5 million in the other pool.

47. The average value of the transactions by Client B in both pools of the Program was approximately $100,000. The absolute value of the transactions in both pools was approximately $4.8 million. This represents approximately 4% of the net assets of one of the pools market timed by Client B.

48. The average hold period with respect to investment in the Program was 4 days or fewer for Client A and was 2 days or fewer for Client B.

49. Any increased transactional costs for the pools market timed by the Clients were borne by the Respondent's other clients, holding the same class of units, as expenses were allocated to each class of units based on its' share of expenses.

D. WRITTEN WARNINGS

50. During the Relevant Period, the Respondent received at least 7 written warnings from 6 mutual fund companies regarding frequent trading by the Clients. Some of the letters said that the trading may affect or be detrimental to their funds, or said that the trading may make the funds more difficult to manage or said that the trading may increase costs. Some of the letters did not refer to any impact on the funds. Some of letters said that the mutual fund companies may impose a short term trading fee of up to 2% of the value of the mutual fund units that were held for fewer than 90 days, in accordance with the funds' simplified prospectuses.

51. The written warnings put the Respondent on notice that Market Timing was potentially harmful to long term unitholders, was not welcome or permitted by the funds and that the mutual fund companies may impose a short term trading fee of up to 2% of the value of the mutual fund units that were held for fewer than 90 days, in accordance with the funds' simplified prospectuses.
52. The language of the written warnings confirmed that the objective of the short term trading fee was to protect long term unitholders from potentially negative consequences of Market Timing. Some of the mutual fund companies issued the warnings because they had determined that Market Timing was potentially harming the funds and the long term unitholders.

53. The written warnings received by the Respondent went unheeded or ignored by the Respondent as it continued to execute the Market Timing activities of the Clients.

E. SUPERVISION

54. Mutual fund companies bear responsibility for identifying and preventing Market Timing; brokerage industry distributors were willing participants in a practice that was potentially harmful to the long term unitholders of the mutual funds.

55. The Respondent failed to take adequate steps to respond to red flag warning signals that it was executing potentially harmful Market Timing practices for the Clients.

56. The Respondent failed to enforce its internal policy related to cut-off times for the accepting and entering of mutual fund orders in allowing Market Timing Client A's Market Timing orders to be entered up to 3:59pm, contrary to its policy which established 3:00pm as the cut-off time.

57. The Respondent failed to implement supervisory systems to address the red flags and thereby detect and prevent potentially harmful Market Timing practices. Specifically, the Respondent failed to implement supervisory systems to: i) adequately supervise the activities of its employees; and ii) enforce, track and distribute the written warnings from mutual fund companies in these circumstances.

F. MITIGATING FACTORS

58. In September 2003, regulators in the United States announced investigations into market timing trading practices at mutual funds in the United States. In November 2003, the Ontario Securities Commission ("OSC") launched a review into mutual fund market timing practices in Ontario. In January 2004, the Association sent surveys regarding market timing to its Member Firms. The majority of Member Firms did not have policies or procedures in place to detect or prevent Market Timing activities. The majority of Member Firms did not have policies or procedures in place to detect or prevent Market Timing activities.

59. In October 2003, after the announcement of investigations in the United States into Market Timing and late trading, but prior to any statement by regulators in Canada, the Respondent directed that the frequent trading in mutual funds by Client A cease.
60. In December 2003, prior to any investigation into or inquiries of investment dealers in Canada with respect to Market Timing, the Respondent voluntarily disclosed to the Association and to the OSC the existence of frequent trading by clients of the Respondent.

61. The Respondent cooperated with Staff in the investigation of this matter.

IV. CONTRAVENTIONS

62. The Respondent admits to the following contraventions of Association By-laws, Regulations, Rulings or Policies:

   i. During the period from January 1st 2002 to December 31st 2003, the Respondent failed to implement supervisory systems to address red flags and thereby to detect and prevent potentially harmful Market Timing practices in mutual funds, for both retail accounts. Specifically, the Respondent failed to implement supervisory systems to:

   a) adequately supervise the activities of its employees;

   b) conduct adequate due diligence into the activities of its employees and clients in these circumstances; and

   c) enforce, track and distribute written warnings from mutual fund companies; and the Respondent failed to enforce its Internal Policy related to cut-off times for the acceptance and entering of mutual fund orders, and thereby was in violation of Association Regulations 1300.2 and 1300.1(o) and Policy 2.

V. TERMS OF SETTLEMENT

63. The Respondent agrees to the following terms of settlement:

   i. Penalties

      i.) Disgorgement of Gross Market Timing Revenues $ 8,462,651.04

      ii) Fine in the amount of $ 8,462,651.04

      iii) Costs $ 50,000.00

   Total: $ 16,975,302.08
ii. The Respondent will set up an internal committee to consider how to identify and address emerging issues in the securities industry. The Respondent will consult with the Association in setting up the mandate of the committee.

64. Unless otherwise stated, any monetary penalties and costs imposed upon the Respondent are payable immediately upon the effective date of the Settlement Agreement.

65. Unless otherwise stated, any suspensions, bars, expulsions, restrictions or other terms of the Settlement Agreement shall commence on the effective date of the Settlement Agreement.

TD WATERHOUSE CANADA INC.
SETTLEMENT AGREEMENT

I.  INTRODUCTION

1. The Enforcement Department Staff ("Staff") of the Investment Dealers Association of Canada ("the Association") has conducted an investigation ("the Investigation") into the conduct of TD Waterhouse Canada Inc. ("the Respondent").

2. The Investigation discloses matters for which the Respondent may be disciplined by a Hearing Panel of the Association, pursuant to Association By-law 20, Part 10 ("Hearing Panel").

II.  JOINT SETTLEMENT RECOMMENDATION

3. Staff and the Respondent consent and agree to the settlement of these matters by way of this settlement agreement (the "Settlement Agreement") in accordance with Association By-laws 20.35 to 20.40, inclusive and Rule 15 of the Rules of Practice and Procedure.

4. The Settlement Agreement is subject to acceptance by the Hearing Panel.

5. The Settlement Agreement shall become effective and binding upon the Respondent and Staff as of the date of its acceptance by the Hearing Panel.

6. The Settlement Agreement will be presented to the Hearing Panel at a hearing (the "Settlement Hearing") for its approval. Following the conclusion of the Settlement Hearing, the Hearing Panel may either accept or reject the Settlement Agreement.
7. If the Hearing Panel accepts the Settlement Agreement, the Respondent waives its right under the Association By-laws and any applicable legislation to a disciplinary hearing, review or appeal.

8. If the Hearing Panel rejects the Settlement Agreement, Staff and the Respondent may enter into another settlement agreement; or Staff may proceed to a disciplinary hearing in relation to the matters disclosed in the Investigation.

9. The Settlement Agreement will become available to the public upon its acceptance by the Hearing Panel.

10. Staff and the Respondent agree that if the Hearing Panel accepts the Settlement Agreement, they, or anyone on their behalf, will not make any public statements inconsistent with the Settlement Agreement. Nothing in this section is intended to restrict the Respondent from making full answer and defence to any civil proceedings against it.

11. Staff and the Respondent jointly recommend that the Hearing Panel accept the Settlement Agreement.

12. If the Hearing Panel rejects this Settlement Agreement:
   
i. The provisions of By-law 20.10 to 20.24, inclusive, shall apply, provided that no member of the Hearing Panel rejecting this Settlement Agreement shall participate in any hearing conducted by a Hearing Panel with respect to the same matters which are the subject of the Settlement Agreement; and
   
ii. This Settlement Agreement and the negotiations relating thereto shall be confidential and without prejudice and may not be used as evidence or referred to in any hearing.

III. STATEMENT OF FACTS

Acknowledgment

13. Staff and the Respondent agree with the facts set out in this Section III for the purposes of this Settlement Agreement only and further agree that this agreement of facts is without prejudice to the Respondent or Staff in any other proceeding of any kind including, but without limiting the generality of the foregoing, any proceedings brought by the Association or any civil or other proceedings which may be brought by any other person or agency. No other person or agency may raise or rely upon the terms of this Settlement Agreement or any agreement to the facts stated herein whether or not this Settlement Agreement is approved by the Hearing Panel.
A. DEFINITION - MARKET TIMING

13. "Market Timing" is a term denoting particular market practices and includes (a) frequent buying and selling of units of the same mutual fund or (b) buying or selling of mutual fund units in order to exploit inefficiencies in the pricing of mutual funds ("Market Timing").

14. Market Timing, while not illegal per se, can adversely affect mutual fund unitholders by diluting the value of mutual fund units to the extent that a market timer is permitted to buy and sell units frequently and take advantage of pricing inefficiencies.

15. Frequent purchases, redemptions and switches can raise transaction costs for funds, generate taxable capital gains for unitholders, disrupt portfolio management strategies and investment style and can force fund managers to sell investments under less than favourable conditions. Market Timing activities can also cause managers to increase borrowing and/or hold a larger cash reserve than necessary or desirable, resulting in diminished returns for long-term investors.

B. SUMMARY of MARKET TIMING ACTIVITIES and REVENUES

16. The Respondent was at all material times a Member of the Association with its head office located in Toronto, Ontario.

17. From January 1st, 2002 to December 31st, 2003 (the "Relevant Period") the Respondent executed potentially harmful Market Timing activities.

i) Market Timing Activities

18. During the Relevant Period, the Respondent executed Market Timing activities on behalf of five clients ("Client A", "Client B", "Client C", "Client D" and "Client E" or collectively the "Clients").

19. The Clients had arrangements with some of the mutual fund companies whose funds they traded that were reduced in whole or in part to writing. The written terms varied from case to case. The arrangements generally reduced or waived fees for short term trading, switching or early redemptions of funds. Several of the arrangements were restricted to specific funds, set limits on the amount that could be invested in each fund or limited the number of switches between funds permitted in a given time period.
ii) Revenues From Market Timing

20. The Respondent's total gross revenues derived, directly or indirectly, from the Client's Market Timing activities during the Relevant Period are as follows:

<table>
<thead>
<tr>
<th>Gross Market Timing Revenues</th>
<th>Client A</th>
<th>Client B</th>
<th>Client C</th>
<th>Client D</th>
<th>Client E</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Management Fees</td>
<td>$3,617,675</td>
<td>$686,337</td>
<td>$38,337</td>
<td>$1,570</td>
<td>$1,812</td>
<td>$5,193,683</td>
</tr>
<tr>
<td>Interest Revenue</td>
<td>$2,045,666</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$0</td>
<td>$2,045,666</td>
</tr>
<tr>
<td>Trailer Fees</td>
<td>$2,776,313</td>
<td>$239,085</td>
<td>$54,572</td>
<td>$7,518</td>
<td>$7,518</td>
<td>$3,085,007</td>
</tr>
<tr>
<td>Total Gross Market Timing Revenues</td>
<td><strong>$8,439,65</strong></td>
<td>$925,422</td>
<td>$92,909</td>
<td>$9,088</td>
<td>$9,33</td>
<td><strong>$10,324,356</strong></td>
</tr>
</tbody>
</table>

C. THE MARKET TIMING STRATEGY

i) MARKET TIMING ACTIVITIES OF THE CLIENTS

A) BACKGROUND

21. Clients A, B and C were offshore entities while Clients D and E were domestic entities. All of the Clients were sophisticated investors that employed a Market Timing Strategy.

22. During the Relevant Period, the Respondent executed the Market Timing activities for the Clients collectively, as follows:

<table>
<thead>
<tr>
<th>Clients</th>
<th># of Funds Market Timed</th>
<th># of Fund Companies Market Timed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Client A</td>
<td>34</td>
<td>4</td>
</tr>
<tr>
<td>Client B</td>
<td>15</td>
<td>5</td>
</tr>
<tr>
<td>Client C</td>
<td>38</td>
<td>17</td>
</tr>
<tr>
<td>Client D</td>
<td>39</td>
<td>20</td>
</tr>
<tr>
<td>Client E</td>
<td>27</td>
<td>15</td>
</tr>
</tbody>
</table>

23. A substantial portion of the Market Timing activities executed by the Respondent for Client A was conducted by means of written special arrangements. There were two written arrangements with two mutual fund companies and one verbal arrangement with one other mutual fund company.
24. A substantial portion of the Market Timing activities executed by the Respondent for Client B was conducted by means of two special arrangements with two mutual fund companies. One of the special arrangements was written and the other was verbal. Additional Market Timing activities were carried on by Client B in the absence of any special arrangements with mutual fund companies.

25. The Market Timing activities executed by the Respondent for Client C were conducted in the absence of any written special arrangements with mutual fund companies.

26. A substantial portion of the Market Timing activities executed by the Respondent for Clients D and E were conducted by means of 13 verbal special arrangements with mutual fund companies. Additional Market Timing activities were carried on by Clients D and E in the absence of any special arrangements with mutual fund companies.

27. The written special arrangements, entered into between the Clients and the mutual fund companies essentially allowed the Clients to trade funds of the mutual fund company without a minimum hold period for a fee which was significantly less than the maximum fee which could have been charged by the mutual fund company pursuant to the funds' simplified prospectus. In turn, the Clients had to comply with a limit on the number of monthly switches and keep a minimum amount of assets in the funds, otherwise an early redemption fee would apply.

B) MARKET TIMING CLIENTS

28. The Respondent executed the Market Timing activities for the Clients in transacting trades for the Clients as follows:

<table>
<thead>
<tr>
<th>Clients</th>
<th>Number of Trades</th>
</tr>
</thead>
<tbody>
<tr>
<td>Client A</td>
<td>&gt;4000</td>
</tr>
<tr>
<td>Client B</td>
<td>&gt;740</td>
</tr>
<tr>
<td>Client C</td>
<td>&gt;379</td>
</tr>
<tr>
<td>Client D</td>
<td>&gt;400</td>
</tr>
<tr>
<td>Client E</td>
<td>&gt;311</td>
</tr>
</tbody>
</table>
29. The average value of the aggregate transactions of the Clients was as follows.

<table>
<thead>
<tr>
<th>Clients</th>
<th>Dollar Range Of Trades</th>
</tr>
</thead>
<tbody>
<tr>
<td>Client A</td>
<td>200,000-82.5 million</td>
</tr>
<tr>
<td>Client B</td>
<td>80,000 — 8.1 million</td>
</tr>
<tr>
<td>Client C</td>
<td>90,000-1.9 million</td>
</tr>
<tr>
<td>Client D</td>
<td>90,000-450,000</td>
</tr>
<tr>
<td>Client E</td>
<td>50,000-304,000</td>
</tr>
</tbody>
</table>

30. The average hold period with respect to a given mutual fund position in the Clients' accounts was fewer than 5 days (the industry norm for minimum hold periods pursuant to standard simplified prospectus language is 90 days).

31. Despite the receipt of written warnings from several mutual fund companies that were market timed in the absence of written special arrangements, the Respondent permitted the Clients to continue Market Timing activities.

C) REJECTION OF MARKET TIMING PROPOSAL BY TD MUTUAL FUNDS INC.

32. During the Relevant Period, the Respondent approached TD Mutual Funds Inc. ("TDMF") with a proposal for a special arrangement to conduct Market Timing activities on behalf of Client A.

33. On May 28 2002, TDMF advised the Respondent in writing that it had rejected the Respondent's proposal to market time its funds. TDMF advised that their analysis indicated that the Market Timing strategy would have a "significant negative impact on the performance of the funds involved."

34. Despite the fact that the Respondent's related entity, TDMF, rejected the Respondent's proposal to market time it's fund and clearly communicated to the Respondent that such rejection was based on the negative impact market timing would have on it's funds, the Respondent continued to facilitate the market timing activities of the Clients without considering the potentially harmful effects of market timing.
D) MARKET TIMING IN TD CANADIAN SMALL-CAP EQUITY FUND

35. During the Relevant Period, the Respondent had a special arrangement with TD Canadian Small-Cap Equity Fund ("TD Small-Cap") to conduct Market Timing activities on behalf of Client B.

36. For a period of nine weeks during the Relevant Period (January 24, 2003 to March 31, 2003), the Respondent facilitated Market Timing activities of Client B in TD Small-Cap. During this time 10 Market Timing Trades were executed by Client B in TD Small-Cap.

37. The average value of the transactions in TD Small-Cap was approximately $2.6 million.

38. The TD Small-Cap prospectus stated in part that the fund is recommended for investors "willing to accept an investment horizon of 5 years or more". The average hold period with respect to Client B's investments was five days and the longest hold period was seven days.

E) SOVEREIGN INVESTMENT PROGRAM

39. During the Relevant Period, the Respondent marketed and distributed seven pools of mutual funds in the Sovereign Investment Program ("Program"); a pool consisted of three classes of units.

40. The Respondent was one of only 4 exclusive distributors of the Program. The Respondent facilitated the Clients to market time two of the pools of mutual funds.

41. For a period of two months during the Relevant Period (August 9, 2002 to September 11, 2002), Client C executed approximately 24 Market Timing Trades in the Program.

42. The average value of the transactions by Client C in one of the pools of the Program was approximately $1 million and approximately $1.5 million in the other pool. The absolute value of the transactions in one pool was approximately $20.8 million and approximately $12 million in the other, 4% and 15% of the pools respectively.

43. The Respondent's other clients, holding the same class of units, bore any increased transactional costs for any pools market timed by the Clients as expenses were allocated to each class of units based on its' share.

D. WRITTEN WARNINGS

44. The Respondent received at least 8 written warnings from 6 mutual fund companies in respect of the Market Timing activities of the Clients. One of the mutual fund companies rejected any future purchase orders by Clients D and E and a second mutual fund company required Client A to cease its Market Timing activities.

45. The written warnings put the Respondent on notice that Market Timing was potentially harmful to long term unitholders, was not welcome or permitted by the funds and/or that the mutual fund companies may impose a short term trading fee of up to 2% of the value of the mutual fund units that were held for fewer than 90 days, in accordance with the funds'
46. The language of the written warnings confirmed that the objective of the short term trading fee was to protect long term unitholders from potentially negative consequences of Market Timing. The mutual fund companies issued the warnings because they had determined that Market Timing was potentially harming the funds and long term unitholders.

47. In one case, following written notification by the mutual fund company that switching back and forth was "not allowed as per our prospectus" and that a two per cent charge would be levied for any future infractions, an investment advisor employed by the Respondent continued to facilitate Market Timing activities in the fund. Forty-five days later, the mutual fund company sent a follow-up written notification marked "Urgent" advising the Respondent that Market Timing Client E was "using a new acct #" and was trading funds without holding for the required 90 days." The notification further advised that "either this client sells all units today or he will be charged 2% ... if he sells before the next 90 days."

E. ACTIVE PROMOTING & ENCOURAGING OF MARKET TIMING ACTIVITIES

48. The Respondent actively encouraged and promoted Market Timing activities in a number of ways. An internal report ("the Internal Report") was prepared at the request of the Respondent in February 16, 2004. In response to issues raised by the Internal Report the Respondent prepared an internal memo dated August 12, 2004 that states as follows: "The conclusions made in that report were reviewed, discussed and rejected by management as unfounded and improperly drawn conclusions.".

49. The Internal Report concluded that the Respondent solicited and negotiated with mutual fund companies to enter into special arrangements to allow the Clients to market time their funds and circumvent switch fees. The Internal Report states that "it could be construed that our IA's directed market timers to fund companies that would permit frequent switching between mutual funds.".

50. The Internal Report states that "senior management at TD Waterhouse may have encouraged and approved the establishment of accounts for these clients. The IAs may have been encouraged to accumulate additional assets for these clients and where feasible possibly encourage the clients to borrow funds. These actions may have been an attempt to generate additional revenues for TD".

51. The Internal Report concluded that the Respondent encouraged Clients D and E to deposit additional assets to "get the account size up to $ 50 million in assets,"

52. The Internal Report concluded that the Respondent facilitated Market Timing activities of Client A by financing its Market Timing activities through a margin loan in the amount of
approximately $42.3 million.

53. The Internal Report concluded that the Respondent facilitated the Market Timing activities by allowing the mutual fund orders of selective clients, Clients A, B, D, and E, to be entered up to 4:00pm EST, whereas the regular system cut off for orders from retail clients is 3:00pm EST, pursuant to the Respondent's internal policies. The Internal Report concluded that as a result of this selective, preferential treatment given to the Clients "TD may have assisted the clients to engage in market timing."

54. The written warnings received by the Respondent went unheeded or ignored by the Respondent as it continued to facilitate the Market Timing activities of the Clients.

F. SUPERVISION

55. Mutual fund companies bear responsibility for identifying and preventing Market Timing; brokerage industry distributors were willing participants in a practice that was potentially harmful to the long term unitholders of the mutual funds.

56. The Respondent failed to implement supervisory systems to address red flags and thereby detect and prevent potentially harmful Market Timing practices. Specifically, the Respondent failed in these circumstances to implement supervisory systems to: i) adequately supervise the activities of its employees; ii) conduct adequate due diligence into the activities of its employees and clients; iii) review and approve the written special arrangements; and iv) enforce, track and distribute the written warnings from mutual fund companies.

57. The Respondent failed to take adequate steps to respond to red flag warning signals that it was facilitating the Clients in engaging in potentially harmful Market Timing activities.

58. An internal memorandum dated September 24, 2003 stated, in part: "I understand XX was asked to leave XYZ because they were uncomfortable with this client being offshore (Bermuda), their lack of understanding of the trading activity and they wanted the account to be serviced by the Institutional division rather than have this client in the retail division. The client moved to TDW with XX in November 2001. XX started at TD on November 26, 2001. The client account was opened on ISM on November 23, 2001."

59. The Internal Report concluded that no due diligence review regarding Clients B, D or E was conducted. The Internal Report states that the question could be raised why due diligence was not conducted for these clients when some form of due diligence was conducted for Client A.

60. The Internal Report concluded that Respondent failed to adequately detect and prevent Market Timing activities in that it did not review and did not have appropriate mechanisms and/or policies in place to approve the written arrangements entered into
between the Clients and the mutual fund companies. The Internal Report indicates "It should be noted that no one other than the IA vetted the agreements with the fund companies."

61. A second internal document concluded that the Respondent's compliance department was aware of the number and frequency of the Market Timing activities, but limited its compliance review to suitability issues and concluded that "overall there were not many compliance queries as market timing is beyond the scope of compliance" and "that there was no unusual activity or patterns in the tested accounts."

62. The second internal document also concluded Respondent's compliance department failed to detect and prevent potentially harmful Market Timing activities in that it did not extend its compliance queries with respect to the Clients accounts to the potentially harmful effects of the Market Timing investment strategy.

63. The Respondent failed to enforce its internal policy related to cut-off times for the accepting and entering of mutual fund orders in allowing the Clients A, B, D and E Market Timing orders to be entered up to 3:59 pm, contrary to its policy which established 3:00 pm as the cut-off time.

G. MITIGATING FACTORS

64. The majority of Member Firms did not have policies or procedures in place to detect or prevent Market Timing activities.

65. The Respondent cooperated with Staff in the investigation in this matter.

IV. CONTRAVENTIONS

69. The Respondent admits to the following contraventions of Association By-laws, Regulations, Rulings or Policies:

i. During the period from January 1st 2002 to December 31st 2003, the Respondent failed to implement supervisory systems to address red flags and thereby detect and prevent potentially harmful Market Timing practices. Specifically, the Respondent failed to implement supervisory systems to:

(a) adequately supervise the activities of its employees in these circumstances;
(b) conduct adequate due diligence into the activities of its' employees and clients, in these circumstances;

(c) review and approve the written special arrangements;

(d) enforce, track and distribute the written warnings from mutual fund companies; to enforce its internal policy related to cut-off times for the acceptance and entering of mutual fund orders, and thereby was in violation of Association Regulations 1300.2 and 1300.1(o) and Policy 2.

V. TERMS OF SETTLEMENT

70. The Respondent agrees to the following terms of settlement:

Penalties

i. Disgorgement of Gross Market Timing Revenues
   $ 10,324,356.69.

ii. Fine in the amount of
    $ 10,324,356.69.

iii. Costs
     $ 50,000.00

Total: $ 20,698,713.38

iv. The Respondent will set up an internal committee to consider how to identify and address emerging issues in the securities industry. The Respondent will consult with the Association in setting up the mandate of the committee.

71. Unless otherwise stated, any monetary penalties and costs imposed upon the Respondent are payable immediately upon the effective date of the Settlement Agreement.

72. Unless otherwise stated, any suspensions, bars, expulsions, restrictions or other terms of the Settlement Agreement shall commence on the effective date of the Settlement Agreement.
The hearing panel has agreed that the settlement should be approved, and we have signed the documents for the purpose.

With the consent of counsel, the three matters were presented to us at the same time. This was appropriate because the penalties are based on the same principles in all three cases.

Although the penalties are very substantial, in view of the material that was presented to us and the submissions of counsel for the Investment Dealers Association, we are of the opinion that the penalties are appropriate in the circumstances.

The matters are serious, and the integrity of the market and the protection of the public require that the penalties should be very substantial ones.

We are pleased to note that the parties are taking steps to prevent the occurrence of such matters in the future. It is part of the penalty that is being imposed that committees should be established for that purpose.

We should also note that the parties cooperated in the investigation. This saved considerable time and money, and allowed the matters to be brought to a head in a very short period of time.

DATED at Toronto, this 8th day of February 2005.

The Honourable Lloyd W. Houlden, Q.C.
Chair

Mr. Robert J. Guilday
Member

Mr. F. Michael Walsh
Member