December 13, 2012

IN THE MATTER OF: JORY CAPITAL INC.

- and -

IN THE MATTER OF: INVESTMENT INDUSTRY REGULATORY ORGANIZATION OF CANADA (IIROC)

REASONS FOR DECISION OF THE MANITOBA SECURITIES COMMISSION

Panel:

Acting Chair:	Mr. J.W. Hedley
Commission Members:	Mr. G.J. Lillies

Appearances:

For Commission	Staff: K.G. Laycock
For Jory Capital Inc.:	A. J. Stacey
For Patrick Cooney:	T.J.D. Kormylo
For IIROC:	L. Herlin

Introduction - the "Order"

On May 4th, the Commission issued an order (the "Order") with the consent of Jory Capital Inc. ("Jory"), Patrick Cooney ("Cooney") and Investment Industry Regulatory Association of Canada ("IIROC"). Relevant excerpts from the Order are as follows:

Pursuant to the power vested in the Commission under section 8(1) of the Act, and without the necessity of any further hearing, the registration of Jory shall be cancelled by the Commission immediately upon the occurrence of any of the following events or on such later date as the Commission may permit for the purposes of an orderly wind-up of Jory: …………

> (d) Jory's Risk Adjusted Capital is negative and is not restored to a positive value within five (5) business days or such later date as IIROC Staff may permit;……

(e) Jory fails to have in place an UDP who is approved by IIROC Staff by August 1, 2012 or such later date as IIROC Staff may permit; or………"

This panel met on September 14th, 2012 and October 31st, 2012, to hear two separate applications consequential to the Order. Both applications were for relief from cancellation of Jory's registration resulting from breaches on the part of Jory. During each hearing, we received evidence, mainly in the form of Affidavits, and heard submissions from counsel for Jory, Cooney, IIROC and Commission staff. Following each hearing, we advised the parties of our respective decisions with brief reasons given orally. We further undertook to prepare written reasons for our decisions and the following are reasons for both decisions.

The Legislation

The legislative basis for both applications can be found in section 31.4(4) of the Manitoba Securities Act (the "Act"):

"If the Commission considers it in the public interest to do so, it may make a decision in respect of:

(a) An internal regulation or proposed internal regulation of a self-regulatory organization; or

(b) A direction, decision, order or ruling made under an internal regulation of the organization."

These matters have been framed not as appeals of an Order of the Commission but rather of decisions made by IIROC. Although the cancellation of Jory's registration would occur as a result of an order of the Commission, the "direction, decision, order or ruling" which Jory disputes were those of IIROC.

We stated at the first hearing that we do not intend to go into detail analyzing "the parameters of section 31.1(4)………". We have had occasion on previous instances to interpret section 34.1. One of these instances involved the parties before us. Although the arguments differed somewhat, we did state in our written reasons that "………if section 34.1 is to have the effect we believe it was intended to have, it must be available to parties legitimately affected by decisions touching on the public interest." (Jory Capital Inc. and IIROC Decision Document dated December 31, 2010). Commission panels have expressed a policy not to interfere lightly with Decisions made by self-regulatory organizations, or SROs, but have stated, for example in the decision previously cited, that we will not allow ourselves to be fettered in matters over which we have authority, meaning matters in which the public interest is engaged.

This is consistent with the submission of counsel for Commission staff that, because of section 34.1 of the Act, this Commission always has jurisdiction to review decisions of self-regulatory organizations.

The Order calls for the cancellation of Jory's registration upon the occurrence of any of the events set forth in a list, including those to which we have referred. Each of the events at issue in the September and October hearings (amongst others which will be briefly described further in these Reasons) would cause immediate cancellation of Jory's registration unless IIROC staff will have decided to permit an extension in time for compliance or remedying the default in question. In each case, as we will discuss, what is at issue is IIROC's "deadline" in respect of each of the two primary events of default.

We have accepted that the Commission has discretion in matters such as the ones before us and the question to us is whether such discretion should be exercised by this panel in the present circumstances and on the facts in evidence, as Jory submits we should do. IIROC argues for a narrow interpretation of the legislation, urging that matters of SRO discretion ought to remain undisturbed, except in rare and exceptional circumstances.

The UDP Issue - September 2012

Facts

By the terms of the Order, Jory was to have an Ultimate Designated Person ("UDP") in place by August 1st, 2012 or such later date as IIROC staff may permit. As of July 30th, 2012, Ms. Brigitte Geisler was been acting as UDP of Jory, with the approval of IIROC, but only on a temporary basis.

Ms. Stephanie Komarnisky was a viable candidate for promotion to the position of UDP but was not yet in a position to take on the role. On July 30th, 2012, Mr. Bruce Thompson, in his capacity as counsel to Jory Capital Inc., requested an extension of that deadline to October 1st, 2012 in order to allow Ms . Komarnisky time to prepare for her promotion to UDP. Jory's request for an extension was granted but with a deadline date of September 5th, 2012, not October 1st, 2012. It was clear that having a temporary UDP would not be approved by IIROC past September 5th.

So, Ms. Komarnisky engaged herself in the process of preparing to become Jory's UDP by September 5th, 2012.

The UDP of an IIROC dealer member performs important functions, namely (dealer member rule 38.5):

1. Supervise the activities of the dealer member that are directed towards ensuring compliance with IIROC's dealer member rules and applicable securities law requirements by the firm and each individual acting on the dealer members behalf, and

2. Promote compliance by the dealer member, and individuals acting on its behalf, with IIROC's dealer member rules and applicable securities laws.

It had appeared of course that the UDP problem would be solved upon the promotion of Stephanie Komarnisky to that position. However, on August 21st, 2012 a telephone call took

place the contents of which and the motivation for which became topics of some vigorous dialogue between Jory, IIROC and their legal counsel.

Jory maintains that Ms. Komarnisky received an unsolicited call from Mr. Carter who "directly and essentially persuaded her that she should not (serve in the role of UDP for Jory)." Jory's counsel asserted that the conduct demonstrated by the phone call is "clear evidence of IIROC's continuing bad faith towards Jory". IIROC, on the other hand, responded that Jory's position regarding the telephone call was baseless and, while the telephone call did take place, it was only because Mr. Thompson had suggested that Mr. Carter (Director, Prairie Region, of IIROC) talk to Ms. Komarnisky about her potential to become UDP for Jory. According to IIROC, Mr. Carter's only motivation was to assist Ms. Komarnisky in appreciating the duties and responsibilities of the UDP, not to persuade her to decline the promotion.

But decline the promotion Ms. Komarnisky did. According to Jory, she did so as a result of her conversation with Mr. Carter. IIROC says that she had already indicated to Mr. Carter prior to the telephone conversation that she would not agree to be UDP.

In any event, our decision did not turn on any finding of the presence, or absence, of bad faith on the part of IIROC. It is not disputed that the telephone call took place; neither is it disputed that Ms. Komarnisky's decision to decline promotion to UDP at best unexpectedly delayed Jory's ability to install a new UDP and the temporary UDP, Ms. Geisler, was going to be unavailable to Jory after October 15th, 2012. Jory requested a second extension of IIROC's deadline to have a UDP in place. The request was denied and IIROC confirmed in a letter to Jory's counsel dated September 4th, 2012 that if Jory did not meet the September 5th, 2012 deadline to have a UDP in place, IIROC intended to ask the Commission to cancel Jory's registration. This resulted in Jory's request of the Commission for a review of IIROC's refusal to extend the UDP deadline and for relief from the anticipated cancellation of Jory's registration.

At the hearing on September 14th, 2012, Jory announced that, almost immediately prior to the day of the hearing, they had completed negotiations with another candidate for the UDP position – indeed a candidate with solid credentials who expressed his availability as soon as he could be recognized by the appropriate regulatory authorities. As well, Ms. Geisler had confirmed that she was prepared to continue to act as UDP until October 15th, 2012 giving Jory until that date to register the new candidate.

We mention here that the facts leading up to the September 14th, 2012 hearing relate to more events than just the failure to have a UDP in place. Counsel for IIROC cited the history of compliance problems on the part of Jory including failures to maintain the required levels of risk adjusted capital and to establish adequate internal controls.

There was also some evidence in respect of the requirement that Jory have a Carrying Broker. That aspect of the hearing created some discussion but, in the final analysis, Jory was left to resolve its requirement to enter into an agreement with a new Carrying Broker without the immediate threat of cancellation of its registration.

IIROC's Position

Despite the revelation that a qualified UDP was available, IIROC's position at the September 14th, 2012 hearing remained unchanged - that is that Jory's registration should be cancelled. IIROC argued that the Order was made to require Jory to get its act in order in respect of compliance generally. Since Jory generally had compliance problems of one sort or another, the Order should be used to deal with them.

As mentioned, IIROC asserted that the Order should only be amended or interfered with in rare circumstances. Even though the Order provided for the exercise on the part of IIROC of discretion regarding deadlines, and even though that discretion had previously been exercised in Jory's favour, further favours to Jory could not be justified in the circumstances of Jory's bad compliance record.

Decision #1

We decided to extend the time for having a UDP in place from September 5th, 2012 to October 15th, 2012. That is the date upon which Ms. Geisler was going to become unavailable. Our intention in that regard was to provide adequate time for the registration of the new UDP candidate.

We agree with IIROC's counsel that this Commission should not interfere, without great caution, in decisions made by IIROC in its discretion. IIROC had the discretion to grant or not to grant extensions of deadlines such as the UDP deadline. It chose not to and has expressed its reasons for not granting Jory's request. As previously indicated, we have said on other occasions that, to the extent reasonably possible, IIROC should be left alone to perform its functions as an SRO, one of which is the enforcement of compliance requirements. However, we have also stated in the past that this Commission can and will exercise its own discretion in a different manner than that of IIROC if the Commission's interpretation of public interest differs from IIROC's.

Although IIROC counsel was not aware until the morning of the hearing that such strides had been made toward the appointment of a qualified UDP for Jory, IIROC still pressed for cancellation of Jory's registration based on the general intent of the Order. In our view, in the final analysis the core issue was still the narrower question of whether an extension should be granted for the placement of a UDP and we made our decision on that issue.

Had the new UDP candidate not been found, we might still have acceded to Jory's request for an extension based on the facts surrounding Ms. Komarnisky's decisions first to apply for the UDP position and then to decline the invitation. As we have indicated, it was not our concern whether the telephone call demonstrated bad faith or simply a justified interest in Ms. Komarnisky's preparation for the role of UDP. The fact was that was the call took place, Ms. Komarnisky changed her mind and as a result Jory found itself facing an imminent and difficult deadline.

After the hearing, we stated in oral reasons that, after considering all the facts presented to us, the "end goal" was to determine that the public be properly served. We stated that this would involve a "weighing and balancing" of elements of public interest which can sometimes be at odds with each other.

One such element is for organizations such as IIROC to protect the public by regulating its dealer members and enforcing its regulations. The other element is the effect of enforcement to "the inconvenience and prejudice to its clients" as we stated in our oral reasons. In this fact situation, a decision not to accede to Jory's request for an extension would have resulted in the cancellation of its registration. Frankly, the prospect of cancelling Jory's registration on the basis of the facts presented to us was, in our opinion, not a viable option.

The RAC Issue - October 2012

Facts

The central issue to the October 31st, 2012 hearing was the failure on the part of Jory to maintain the prescribed level of risk adjusted capital, or RAC. As previously stated, the May 4th, 2012 Order provided that Jory's registration shall be cancelled where its RAC is negative and is not restored to a positive value within five business days, or such later date as IIROC staff may permit.

IIROC filed an Affidavit sworn by Robert DeGoeij in which evidence was provided that Jory was RAC deficient and gave Jory until October 23rd, 2012 to correct the deficiency. As of Monday, October 22nd, 2012, Jory's RAC was minus $94,000.00.

IIROC's internal rules require that a dealer member maintain RAC greater than zero as calculated in accordance with the joint regulatory financial questionnaire and report of IIROC. A dealer member is required to notify IIROC when and if its RAC is less than zero. Mr. DeGoeij's affidavit states that IIROC's longstanding policy is to take steps to convene a hearing if a dealer member does not correct its capital deficiency within two business days. The Order to which we have referred of course provides that Jory may have five days in which to correct a RAC deficiency. The essential issue at play is capital adequacy which, in accordance with rule 2600 of IIROC requires that dealer members must:

1. Establish and maintain internal controls designed to allow dealer members to plan for and monitor their capital;
2. Take preventative measures to avoid a capital deficiency; and
3. Report promptly to IIROC any capital deficiency that has occurred.

Mr. DeGoeij goes on in his affidavit to state that the "financial requirements described above are essential for the determination of the financial solvency of a dealer member and ultimately for the protection of the public, other dealer members, IIROC, and the Canadian Investment Protection Fund."

So, RAC is more to IIROC than simply a compliance issue. If a dealer member is capital deficient, logic implies that it cannot conduct its business in an efficient manner and others along with the dealer member might pay the price. "Others" could include its customers and clients although it should be noted here that, as a Type 2 Introducing Broker, Jory does not handle its clients money. Further, there has never been an allegation that Jory has done anything but serve its clients in an honest, professional and competent manner. Nevertheless, it is acknowledged by

the parties that capital adequacy is a proper subject for self-regulatory discipline as is happening in the present case.

As it happened in October, 2012, as the dialogue between IIROC and Jory began to address the possibility of an immediate suspension over RAC deficiency, Jory informed IIROC that one of its clients had agreed to allow Jory to withdraw certain account administration fees from his account. These fees had previously not been recorded as revenue by Jory pursuant to an agreement with the client and bringing them in as revenue would alleviate Jory's RAC problem, at least temporarily. However, as late as October 25th, 2012, Jory's CFO did not have sufficient documentation to confirm to IIROC that this information was correct. On October 26th, 2012, Jory was able to provide evidence in support of its position that Jory's RAC deficiency was effectively corrected, although narrowly, as of October 23rd, 2012, the date which IIROC had imposed as a deadline.

In the circumstances, and those circumstances include a history of capital deficiency and reporting delinquencies, IIROC was not willing to extend the time imposed for restoration of positive RAC value although, as mentioned, the Order does provide the discretion to do so.

The Parties' and Staff's Positions

Again, the question before us is whether this panel should, standing in IIROC's shoes and given the opportunity to extend the deadline imposed by the Order, substitute IIROC's decision with a different one of our own.

As mentioned, counsel agreed that capital adequacy is an important issue even though Jory's client's funds are not directly at risk during times of capital deficiency.

There was no argument during our hearing as to whether or not this panel may exercise its discretion in a manner different to IIROC's but the parties took different positions as to what the panel's focus should be.

Counsel for staff of the Commission submitted that the panel may indeed view the matter narrowly and focus on the specific issue of the latest period of RAC deficiency and the facts surrounding its apparent correction. However, staff submitted that we are similarly justified in widening the focus and consider the accumulation of issues, the aforementioned preponderance of days in negative RAC and reporting delinquencies and come to the conclusion that it's "just not working". Taking the latter approach would, it is suggested, make us unlikely to substitute our own decision – not to provide a discretionary extension – for that of IIROC.

Counsel for IIROC stressed that to narrow our focus to one strict set of facts would serve only to ignore the reality of Jory's struggle with capital inadequacy, its failure to meet other regulatory requirements and its general record of failures in connection with compliance issues. Alternatively, on the narrow issue of its latest RAC deficiency, IIROC simply states that Jory triggered the May 4th, 2012 Order by having negative RAC for five days, must suffer the consequences of having done so and cannot retroactively alter what took place on October 23rd, 2012, that being the cancellation of its registration for violating the Order.

Counsel for Jory and Patrick Cooney cited several examples in support of his submission that Jory has been in substantial compliance with the Order since it was made. He acknowledged that there are problems with RAC but reminded us of some of the obvious reasons why Jory might understandably have had capital adequacy issues in the past: for example, their increased legal costs over compliance issues and harmful publicity arising out of disciplinary proceedings. These, the argument goes, would compound the struggle for any small firm such as Jory to resolve capitalization issues. As well, another problem has been that Mr. Cooney is spending more time on compliance issues than in dealing with Jory's business.

In general, on the facts as previously described, it is submitted by Jory counsel that we have the option of viewing the RAC issue in a "reasonable practical way" or, as preferred by IIROC, bringing the full force of IIROC's regulatory power to bear.

Decision #2

We decided to lift the suspension of Jory's operation, preferring in these circumstances to provide more "slack" to Jory in hopes that it will correct its compliance record and put the RAC issue and other compliance issues behind it. As we stated at the conclusion of the hearing, we could justifiably done otherwise.

At the conclusion of the hearing, we gave our decision and presented brief oral reasons, quoted in part as follows:

"In IIROC's estimation there is no good reason to believe that Jory will not continue to struggle in this way (capital deficiency). IIROC's position is that failing to give even more slack to Jory than it already has and suspending Jory simply reflects reality going forward. If we agree with IIROC and refuse to lift Jory's suspension, we would be saying one of two things or a combination of both:

1. Regulation such as RAC requirements are enacted for a purpose and must be strictly observed;

2. IIROC's duty to oversee the activities of its dealer members mandates that it apply its expertise and experience to govern its members. Its conclusions, IIROC's conclusions should not be altered lightly at this level.

If we lift the suspension, we will be following Jory's counsel's admonition that today's issue turns on limited and focused evidence, that is, evidence surrounding the close timing of the RAC correction. Otherwise, the Order has been substantially complied with. Jory says that reasonableness and practicality demand that we not be so strict. Staff for the Commission has offered the opinion that this panel is not restricted to dealing with one event but rather conjoin with IIROC in saying enough is enough as far as Jory is concerned.

Today we see things Jory's way. We agree with counsel for staff and for IIROC that we could justifiably do otherwise. But our view is that the public interest is properly served if we are less strict in applying the Order in the circumstances of these particular facts. That is where the RAC

deficiency was corrected by Jory but not communicated to IIROC and that the correction substantially addresses the purposes of RAC regulations.

As to the other examples of Jory's failures to abide by regulatory requirements, all we say is that those examples have not influenced us strongly enough to alter our decision."

Summary

As previously stated, we appreciate that IIROC, as a self-regulatory organization recognized by this Commission, has a duty to protect the public. An SRO cannot do so without establishing rules and requiring compliance with those rules under the threat of penalties of suspension and cancellation of registration. That is clearly in the public interest. Some compliance issues may not appear to have a direct influence on the rights and interests of investors but they ultimately can.

On the other hand, this Commission has on more than one occasion directed its attention, in its analysis of public interest, to the local marketplace served by the Commission. We quote from a previous Commission Decision dated October 10th, 2007:

"We agree with the IDA (now IIROC) panels that Cooney has shown too little concern with honouring the Association's financial compliance rules. We also agree that the public interest requires that there be some significant sanctions imposed. The public interest, however, can be served without incurring the reasonably foreseeable risk of putting a local dealer out of business. In this area the Commission's perception of public interest differs from that expressed by the IDA panels."

Jory has carried on business, compliance record notwithstanding, in this jurisdiction with an apparently good record as far as its clients investment interests are concerned. In balancing the public's interest in IIROC's enforcement of compliance against the gravity of the consequences of enforcement, we determined that our own discretion, on balance, would be weighted more in the latter and decided to allow Jory more time to comply with the Order. The enforcement of compliance rules internal to SRO's such as IIROC is one valuable tool in the protection of the public but not an end to itself.

In our view, that approach is consistent with the legislative intention expressed in subsection 31.1 of The Securities Act.

"*J.W. Hedley*"
J.W. Hedley
Chair

"*J.W. Hedley*"
G.J. Lillies
Member