CIRCULAIRE 136-25
31 octobre 2025

BOURSE DE MONTRÉAL INC.

DÉCISION DISCIPLINAIRE

BMO NESBITT BURNS INC. ET FRANCO CARELLI

La Division de la Réglementation de Bourse de Montréal Inc. (la « Bourse ») a déposé des plaintes disciplinaires contre BMO Nesbitt Burns Inc. et M. Franco Carelli, respectivement un Participant Agréé et une Personne Approuvée, alléguant des infractions aux règles de la Bourse.

La plainte disciplinaire contre BMO Nesbitt Burns Inc. alléguait que :

1. Le 19 mars 2019 et le 31 mai 2019, BMO Nesbitt Burns Inc. a contrevenu à l'article 7.6 - « Devancer une Opération » des règles de la Bourse, car elle a pris avantage d'un ordre d'un client pour devancer l'opération et a effectué des opérations basées en tout ou en partie sur des informations privilégiées concernant des opérations imminentes portant sur des titres, des options ou des contrats à terme qui risquaient d'affecter les cours de tout autre titre, option ou contrat à terme;

2. Le 19 mars 2019 et le 31 mai 2019, BMO Nesbitt Burns Inc. a contrevenu à l'article 7.3 - « Obligation de meilleure exécution » des règles de la Bourse, car elle n'a pas fait preuve de diligence afin d'exécuter un ordre client selon les conditions d'exécution les plus avantageuses pouvant être raisonnablement obtenues compte tenu des circonstances liées à l'opération ou à la stratégie de négociation et des conditions du marché au moment de l'opération;

3. Le 19 mars 2019 et le 31 mai 2019, BMO Nesbitt Burns Inc. a contrevenu à l'article 6.202 - « Négociation contre l'ordre d'un client (application) », aux sous-alinéas 6.205 b) ii) et iii) - « Opérations préarrangées » et à l'article 6.114 - « Priorité des ordres » des règles de la Bourse », car, tout en exécutant sciemment une opération sur contrats à terme contre l'ordre d'un client pour son propre compte, elle n'a pas saisi l'ordre du client en premier dans le système de négociation électronique, n'a pas donné la priorité à un ordre du client et n'a pas exposé l'ordre du client au marché pendant le délai minimal prescrit par les règles de la Bourse;

4. Le 19 mars 2019 et le 31 mai 2019, BMO Nesbitt Burns Inc. a contrevenu à l'article 6.115 - « Identification des ordres » des règles de la Bourse, car elle ne s'est pas assurée de l'identification correcte des ordres lors de leur saisie dans le système de négociation (ordre pour le compte client et ordre pour le compte d'une firme);

5. Entre le 19 mars 2019 et le 10 octobre 2019, BMO Nesbitt Burns Inc. a contrevenu à l'article 3.100 - « Supervision, surveillance et conformité » des règles de la Bourse, car elle n'a pas établi et maintenu un système lui permettant de surveiller les activités de chacun de ses employés et Personnes Approuvées, qui est conçu pour assurer de manière raisonnable que les règles de la Bourse soient respectées, plus précisément parce qu'elle ne disposait pas d'un système de surveillance raisonnablement conçu pour prévenir ou détecter le devancement d'une opération par ses Personnes Approuvées et ses employés;

6. Le 19 mars 2019 et le 31 mai 2019, BMO Nesbitt Burns Inc. a contrevenu à l'article 3.100 - « Supervision, surveillance et conformité » des règles de la Bourse, car elle n'a pas établi et maintenu un système lui permettant de surveiller les activités de chacun de ses employés et Personnes Approuvées, qui est conçu pour assurer de manière raisonnable que les règles de la Bourse soient respectées, plus précisément parce qu'elle ne disposait pas d'un système de surveillance raisonnablement conçu pour prévenir ou détecter les violations des articles 6.114 - « Priorité des ordres », 6.115 - « Identification des ordres », 6.202 - « Négociation contre l'ordre d'un client (application) », 6.205 - « Opérations préarrangées » et 7.3 - « Obligation de meilleure exécution » des règles de la Bourse;

7. Le 19 mars 2019 et le 31 mai 2019, BMO Nesbitt Burns Inc. a contrevenu à l'article 3.101 - « Obligation de supervision des Participants Agréés » des règles de la Bourse, car elle ne s'est pas assurée que tous ses employés et Personnes Approuvées se conforment à l'article 7.6 - « Devancer une Opération » des règles de la Bourse.

La plainte disciplinaire contre M. Franco Carelli alléguait que, le 19 mars 2019 et le 31 mai 2019, il a contrevenu à l'article 7.6 - « Devancer une Opération » des règles de la Bourse, car il a profité d'un ordre d'un client pour devancer l'opération et a effectué des opérations basées en tout ou en partie sur des informations privilégiées concernant des opérations imminentes portant sur des titres, des options ou des contrats à terme qui risquaient d'affecter les cours de tout autre titre, option ou contrat à terme.

Le 29 octobre 2025, à la suite d'une audience tenue les 2, 3, 4, 5 et 6 juin 2025, un Comité de Discipline dûment constitué en vertu des règles de la Bourse a déclaré M. Franco Carelli coupable de l'infraction alléguée, a déclaré BMO Nesbitt Burns Inc. coupable des infractions alléguées aux chefs d'accusation 1, 2, 3, 5, 6 et 7 et a acquitté BMO Nesbitt Burns Inc. de l'infraction alléguée au chef d'accusation 4.

La décision du Comité de Discipline est jointe. Une traduction de la décision originale rendue en anglais sera publiée ultérieurement.

Pour de plus amples renseignements, veuillez communiquer avec les Affaires juridiques de la Division de la Réglementation par courriel à l'adresse mxrlegal@tmx.com.

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CANADA
PROVINCE OF QUÉBEC
File No. EN-DC-23005

In the matter of:

BMO Nesbitt Burns Inc. ("**BMONBI**")**,** an Approved Participant of Bourse de Montréal Inc. (the "**Bourse**")

- and-

Franco Carelli, a former Approved Person of the Bourse ("**Carelli**")

JUDGMENT

A. INTRODUCTION

1. The hearing in this case was held in this case on June 2, 3, 4, 5 and 6, the parties having requested that the name of the client of BMONBI and Franco Carelli (sometimes hereinafter collectively referred to as "**Respondents**") involved in this case be kept confidential in the judgment of the Disciplinary Committee (the "**Committee**"). Accordingly, said client will be referred to as "**Client**" and the names of its representatives involved in the relevant transactions will also be kept confidential.

2. The two Complaints in this case resulted from a series of hedging trades conducted by Carelli on behalf of BMONBI, his employer, on March 19 and May 31, 2019, the Bourse having charged Carelli with front running under section 7.6 of the Bourse rules, while BMONBI was charged with front running, as well as 6 other counts, as appears below.

3. The following persons testified at the hearing:
   a) Sylvain Lambert, investigator for the Regulatory Division of the Bourse ("**Lambert**")
   b) David Moore, Chief Compliance Officer at BMONBI ("**Moore**")
   c) Franco Carelli, liquidity provider for BMONBI ("**Carelli**")
   d) James J. Angel, expert («**Angel**»)
   e) Naresh Tejpal, expert ("**Tejpal**").

4. References to exhibits herein will be denoted by the letter "E", followed by the exhibit number.

5. The Complaints herein against Respondents read as follows:

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FRANCO CARELLI

1. On March 19th, 2019 and on May 31st, 2019, Franco Carelli contravened article 7.6 - Front Running Prohibited" of the Rules of the Bourse (the "**Rules**"), as he took advantage of a customer's order by trading ahead of it, and engaged in Transactions based in whole or in part on non-public information concerning pending transactions in Securities, Options or future contracts, which were likely to affect the market prices of any other Securities, Options or future contracts,

the whole rendering Franco Carelli subject to a disciplinary complaint pursuant to article 4.200 of the Rules and to the sanctions listed in article 4.400 of the Rules.

BMONBI

1. On March 19th, 2019 and on May 31st, 2019, BMONBI contravened article 7.6 - "Front Running Prohibited" - of the Rules of the Bourse (the "**Rules**"), as it took advantage of a customer's order by trading ahead of it, and engaged in Transactions based in whole or in part on non-public information concerning pending transactions in Securities, Options or future contracts, which are likely to affect the market prices of any other Securities, Options or future contracts;

2. On March 19th, 2019 and on May 31st, 2019, BMONBI contravened article 7.3 - "Best Execution Required" - of the Rules, as BMONBI did not diligently pursue the execution of a client order on the most advantageous execution terms reasonably available under all of the circumstances relating to the Trade or Trading Strategy and the then current market conditions at the time of the Trade;

3. On March 19th, 2019 and on May 31st, 2019, BMONBI contravened article 6.202 - "Trading Against Customer Orders (Cross-Trades)", subparagraphs 6.205 (b) ii) and iii) – "Prearranged Transactions", and article 6.114 – "Order Priorities" of the Rules, as BMONBI, while knowingly taking the opposite side of a customer order of Futures for its own account, did not enter the customer order first on the Electronic Trading System, did not give priority to a customer order and did not expose the customer order to the market for the minimum prescribed time period established under the Rules;

4. On March 19th, 2019, and on May 31st, 2019, BMONBI contravened (…) article 6.115 - "Order Identification" - of the Rules, as BMONBI did not ensure the proper identification of orders when entering them into the trading system (order for the account of a customer and order for the account of the firm) (…);

5. Between March 19th, 2019 and October 10th, 2019, BMONBI contravened article 3.100 - "Supervision, Surveillance and Compliance" of the Rules, as BMONBI did not establish and maintain a system to supervise the activities of each of its employees and Approved Persons that is reasonably designed to achieve Compliance with the Rules, more specifically as it did not have a surveillance system in place reasonably designed to prevent or detect the trading practice of "front running" by its Approved Persons and employees;

6. On March 19th, 2019 and on May 31st, 2019, BMONBI contravened article 3.100 - "Supervision, Surveillance and Compliance" - of the Rules, as BMONBI did not establish and maintain a system to supervise the activities of each of its employees and Approved Persons

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that is reasonably designed to achieve Compliance with the Rules, more specifically as it did not have a surveillance system in place reasonably designed to prevent or detect violations of articles 6.114 - "Order Priorities", 6.115 - "Order Identification", 6.202 – "Trading Against Customer Orders (Cross-Trades)", 6.205 – "Prearranged Transactions", and 7.3 – "Best Execution" of the Rules;

7. On March 19th, 2019, and on May 31st, 2019, BMONBI contravened article 3.101 - "Approved Participant's Supervisory Responsibility" - of the Rules, as BMONBI did not ensure that one of its employees and Approved Persons complied with Article 7.6 of the Rules (Front Running Prohibited).

the whole rendering BMONBI subject to a disciplinary complaint pursuant to article 4.200 of the Rules and to the sanctions listed in article 4.400 of the Rules.

6. The questions in issue are as follows:

a) Did Respondents engage in front running in contravention of the Rules when they engaged in proprietary CGB trades between the time they first learned of Client's intention to purchase CGB contracts on March 19 and May 31, 2019 and the moment the Client's trades were entered in the Bourse's electronic trading system, without giving Client the benefit of those proprietary trades?
b) Did BMONBI give Client the "best execution" pursuant to the Rules by not giving Client the benefit of those proprietary trades?
c) Did BMONBI breach the Rules by entering its own sell orders in the electronic trading system (wherein it was taking the opposite side of the Client's orders) before entering the Client's buy orders?
d) Did BMONBI breach the Rules by misidentifying the sell trades related to Client's orders as being those of the Client rather than those of BMONBI?
e) Did BMONBI breach the Rules by failing to establish and maintain, between March 19 and October 10, 2019, a system to supervise the activities of each of its employees and Approved Persons that was reasonably designed to achieve compliance with the Rules, more specifically as it did not have a surveillance system in place reasonably designed to prevent or detect the trading practice of front running by its Approved Persons and employees?
f) Did BMONBI breach the Rules between March 19 and May 31, 2019, by failing to establish and maintain a system to supervise the activities of each of its employees and Approved Persons that was reasonably designed to prevent and detect violations of the Rules relating to order priorities, order identification, trading against customer orders, pre-arranged transactions and best execution?
g) Did BMONBI fail to ensure, between March 19 and May 31, 2019, that one of its employees and Approved Persons complied with article 7.6 of the Rules?

B. THE FACTS

7. BMONBI is a national investment firm which offers a wide variety of services to its clients, one of which involves trading in Canada government bonds and futures contracts relating to same.

8. Carelli was employed by BMONBI from December 1999 until his retirement in 2023, and was working, at the time of the alleged infractions, as a fixed income proprietary trader and market maker for fixed income products, which included facilitating buy side client trades

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in Canada government bonds (known as "**cash bonds**") and related futures contracts (known as "**CGBs**"), his principal role being to provide the liquidity required to facilitate such trades through hedging activities (by trading futures contracts such as CGBs) carried out to cover the risks associated with his market making activities.

9. Facilitating client trades in cash bonds and CGBs did not normally generate significant revenues for BMONBI, who engaged in such activities as a service to its clients, who also confided significant transactions to BMONBI in other much more lucrative areas.

10. Unlike CGBs, cash bonds are traded "over the counter", by chat, voice call or electronic trading platforms, usually by participant employees known as "agency traders".

11. CGBs are futures contracts on Canada government bonds which, unlike the cash bonds, are traded over the Bourse (TMX), which is why the Bourse has jurisdiction over the impugned futures trades and related activities in this case.

12. A transaction involving a minimum of 1500 futures contracts is known as a "block trade", to which special rules apply. Transactions involving fewer contracts may be conducted as day trades or "pre-arranged trades", to which other rules apply.

13. BMONBI and other Canadian institutions who do business in the U.S.A. are prevented by the "Volcker Rule" (part of American legislation, the Dodd-Frank Act) from engaging in proprietary trading in short-term securities such as derivatives, futures and options.

14. However, among a number of exceptions to this general rule, they are allowed to trade outside the U.S.A. in products such as CGBs as part of hedging activities related to providing liquidity to facilitate trades for clients. Taking on liability positions and hedging to facilitate client trades involves taking on risk, which must be managed by the liquidity provider, whose objective is to finish each day of trading with minimal residual exposure.

15. A client wishing to buy CGBs through a pre-arranged trade will contact the agency trader or client representative of the brokerage firm with which it deals to arrange the transaction, the relevant communications being conducted over the telephone (which conversation is recorded) or by chat, which communication is also conserved, with said forms of communication sometimes being conducted concurrently by the participants. According to Carelli, most client CBG trades are processed by agency traders, the liquidity provider's role being to provide a suitable price and then manage the firm's risk through the hedging of futures products.

The events of March 19, 2019

16. The relevant events of March 19, 2019, which are recorded in the transcripts of two telephone conversations (E-5B and E-6B), a Bloomberg chat conversation (E-4), a condensed table of relevant transactions of that date prepared by the Bourse (E-3), and Carelli's trading data of that date (E-7B), all of which are encapsulated in a chronological history of relevant events prepared by the Bourse (E-7A), may be summarized as follows:

a) at 14:42:08 on March 19, 2019, Carelli (then based in Montreal) and Steve Sevsek (a salesman at BMONBI's fixed income desk in Toronto, tasked with maintaining client relationships) engaged in a brief telephone call (E-5B) in which Sevsek alerted Carelli of the need to join a call and chat room discussion regarding a

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transaction Client wished to make involving approximately $60 million (Can.) in cash bonds and an unspecified number of CGBs;

b) Careli testified that, based on his experience, an institutional client who requests a price will almost always go through with the prospective transaction;

c) with this experience in mind, and as appears from E-3, E-7A and E-7B, during the next 101 seconds, Carelli placed a series of four buy orders on behalf of BMONBI, starting with an order at 14:42:44 for 50 CGBs at $138.01, another at 14:43:06 for 100 CGBs at $138.02, then another order for 100 CGBs at $138.02 at 14:43:22, and a final order for 50 CGBs for $138.03 at 14:43:49, Carelli's previous buy order for CGBs having been placed nearly two hours earlier at 12:54:16 (E-7B, page 3);

d) Carelli also testified that he placed an order for the purchase of 50 CGBs at 14:43:49, 23 seconds after Client had specified the number of CGBs it wished to buy (see sub-paragraph (h) below), when Carelli must have felt even more certain that a deal would be struck with Client;

e) the first of these orders (50 CGBs) was only filled after the cross trade, while the last three (250 CGBs) were filled to the extent of 247 contracts (E-3);

f) just prior to calling Carelli, Sevsek initiated (at 14:42:07) a Bloomberg chat discussion (E-4) which was joined by Carelli (at 14:42:23), Brad Wishak (a futures agency trader for BMONBI in Toronto) at 14:42:30, and Client's representative, Mr. X, at 14:42:35;

g) at 14:42:52, another telephone conversation was initiated between Carelli, Brad Wishak and Bryce Stroble (E-6B), the latter being another futures agency trader for BMONBI in Toronto, during which these three exchanged comments regarding the ongoing chatroom negotiation of the transaction with Client;

h) at 14:43.26, X informed the chatroom participants (E-4) that Client wished to purchase 546 CGB contracts and 30 XQM9s (an unrelated trade);

i) at 14:43:30, after having placed 3 of the 4 buy orders described in sub-paragraph (c), Carelli instructed his colleagues over the telephone (E-6B) to offer Client a price of $138.04 (mentioning only the last two digits of the target price, $0.04, as is customary in the trade), which price was offered to Client at 14:43:48 (E-4 and E-7A), Respondents alleging that this price was slightly higher than the price of ongoing market trades at that point;

j) at 14:44:13, X accepted the offer to buy 546 CGBs at the maximum price of $138.04 (E-4, E7A), by which point Carelli had already placed buy orders for a total of 300 CGBs at $138.03 or less, as appears from sub-paragraph (c) above;

k) at 14:44:28, Carelli put in a buy order for 150 CGBs at $138.03, which was filled quickly, then another buy order for 200 CGBs at $138.03 at 14:44:49, which was also filled at the bid price;

l) at 14:45:12, a sell order for 546 CGBs was entered at $138.04 and identified as a Client trade, followed by a buy order at 14:45:30 for 546 CGBs at $138.04, which was also entered as a Client trade, although BMONBI admits that the first of these two trades should have been designated a firm trade;

m) Lambert testified that this error in designation was corrected shortly thereafter by BMONBI, but that the market was nevertheless misled by this erroneous entry, although this latter affirmation was contested by Respondents;

n) the end result of the hedging trades made by Carelli on March 19, 2019 is that he placed orders for a total of 650 CGBs on behalf of BMONBI between the time (14:42:08) he first learned of Client's intention to buy $61 million in cash bonds and an unspecified number of CGBs, and the time (14:45:30) BMONBI placed the buy order for 546 CGBs on behalf of the Client;

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o) in paragraph 5 of the Summary of Facts attached to the original Disciplinary Complaint against BMONBI (the "**Summary of Facts**"), the Bourse only impugns the last three trades (totaling 400 CGBs) as alleged front running, these three trades (the "**Impugned Trades**") having been made between the moment (14:43:26) the Client first specified the number (546) of CGB contracts it wished to purchase and the actual posting of Client's buy order on the electronic trading board by BMONBI at 14:45:30 (E-7A), as mentioned by BMONBI in the letter it remitted to Carelli on June 13, 2019 (E-24, page 3), which letter focused on the trades between the Client's acceptance of the price and the posting of its buy order;
p) these three Impugned Trades were made within 83 seconds of the time (14:43:26) of the time Client specified that it wished to buy 546 CGBs;
q) Lambert testified that BMONBI did not give Client the benefit of the trades made by Carelli prior to the posting of Client's buy order, including the Impugned Trades;
r) the summary of activities at E-7A indicates that, following the posting of the buy order for 546 CGBs at 14:45:30, 239 contracts were cross-traded by BMONBI at $138.03 and 307 contracts were cross-traded at the agreed limit price of $138.04;
s) according to Lambert, the average price of the 600 CGBs Carelli purchased before the posting of Client's order 546 CGBs was $138.02667, while the average price paid by Client was $138.037875, such that Client would have paid $6120 less if it had been given the benefit of all of the lower-priced fills obtained by Carelli;
t) however, the Bourse's counsel admitted during her summation that, if the infraction was limited to the Impugned Trades (400 CGBs), the difference in price would only be $3150.

17. While admitting that his recollection of the events of March 19 was vague, Carelli referred to his letter dated April 11, 2019 (E-20, page 73) to Rajiv Menon ("**Menon**"), a junior analyst in BMONBI's first line of supervision, written in response to an RFI (request for information) from the Bourse regarding the March 19 trades which was triggered by a warning from SOLA, the Bourse's proprietary trading platform. In this letter, Carelli affirmed that his above CGB trades on March 19, 2019 were made "**to hedge up our short position from previous trades and also the 29s (cash bond trade)…I was solely trying to hedge our books from a previous short and hedging the 2029's bonds after we gave and client accepted the prices**".

18. Carelli said that the CGB market on March 19, 2019 was between $138.03 and $138.04 and denied that his CGB trading of March 19 removed liquidity from the market, adding that these trades gave him a better sense of where the market was at that time.

19. Carelli testified that a client who wishes to buy a substantial number of CGBs will go to a liquidity provider rather than purchase them on the market in order to improve the chances of getting a better price. The client who deals through a liquidity provider has the certainty of a guaranteed maximum price, while the liquidity provider and his/her firm assume the risk of delivering the futures contracts at such limit price.

20. Carelli stated that, in this case, the Client (whom he described as a sophisticated investor) agreed to pay a maximum price of $138.04, that it effectively paid an average price slightly below that ($138.037875, according to Lambert) and that it was happy with the outcome, even if it did not receive the benefit of the lower-priced fills achieved by Carelli, which he affirmed did not constitute taking advantage of the Client's order. He said that the overall effect for BMONBI of the transactions of March 19, 2019 was a wash, with marginal profit or loss.

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21. Carelli admitted that he was not sure whether the Client was aware of his hedging activities, an admission reiterated in BMONBI's Gatekeeper Report dated June 26, 2019 (E-30, final paragraph) and corroborated by Moore in his testimony, or whether the Client tracked market trading activity such as his.

The events of May 31, 2019

22. The relevant events of May 31, 2019, which are recorded in the transcripts of five telephone conversations (E-11B, E-12B, E-13B, E-14B and E-15B), two Bloomberg chat conversations (E-10 and E-16), a table of Carelli's trading data on that date prepared by the Bourse (E-17B) and a condensed table of transactions (E-9), all of which are encapsulated in a chronological history of relevant events prepared by the Bourse (E-17A), may be summarized as follows:

a) according to Carelli, May 31, 2019, being the last day of the month, was a busy trading day for futures, as market traders were trying to close their books by the end of the day in a neutral position for the month;
b) several minutes prior to its call regarding the CGB trade on that date, the Client had requested a large trade for $141.94 million in cash bonds (not purchased on the Montreal Exchange), as appears from the Bloomberg chat with the Client (E-10, page 3, 13:15:54) and the recording of a short call between Sevsek and Carelli which started at 13:15:58 and ended around 13:17:04 (E-11B);
c) Carelli testified he was short about 1300 CGB contracts after that cash bond order was executed by the agency trading desk;
d) Carelli was advised by Stroble of Client's desire to purchase 549 CGBs at 13:20:41 (E-13B) and stated that he was concerned about Client's order for 549 CGBs because that would aggravate his short position on this critical last day of the month, when there were more buyers than sellers on the market, which made it difficult to buy bonds, all of which explains his dismay upon learning of the Client's belated decision to buy 549 CGBs at 13:20:41 (E-13B);
e) At 13:19:26, X and Olivia Li ("**Li**"), another futures agency trader for BMONBI, engage in a conversation (E-12B) during which Client requests and agrees (at 13:21:10) to buy 549 CGBs at $142.73, after Carelli had provided that price at 13:21:09 (E-13B);
f) Li stated (E-25, para. 3) that "the price of $142.73 was slightly higher than the best bid price on the board at the time of the order";
g) at 13:21:12, Carelli places an order for 100 CGB contracts at $142.69 (E-9), which order is filled at that price in lots of 58 contracts (at 13:21:12) and 42 contracts (at 13:21:38);
h) at 13:21:33, Li places a sell order under Client's name at $142.73 (E-9), just before the second portion of Carelli's above-mentioned buy order is filled, Li having later admitted this sell order should have been described as a firm trade (E-25, page 2, para. 4);
i) at 13:21:58, Li enters a buy order acknowledgment for 549 CGBs at $142.73, again attributing it to the Client (E-9);
j) in between these buy and sell orders for 549 CGBs, Carelli places another order at 13:21:44 for 100 CGBs at $142.70, which is partially filled by 71 contracts at $142.70 at 13:21:55 (E-9 and E-17A);
k) Carelli testified that these two hedging orders (also referred to as the "**Impugned Trades**") were made to cover the major short position caused by the cash bond transaction, which version first appears in E-20, at page 77;

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l) the summary of CGB trades by Carelli on May 31, 2019 (E-17A, which starts at 12:05:03) show that Client accepted Carelli's offer to provide 549 CGBs at $142.73 at 13:21:10, subsequent to which he placed the Impugned Trades of that date within the next 94 seconds;

m) the summary of activities at the top of page 3 of E-17A indicates that following the posting of buy order for 549 CGBs at 13:21:58, 205 CGBs were cross-traded by BMONBI at $142.71 and 344 CGBs were cross-traded at the agreed limit price of $142.73

n) according to Lambert, the average price paid by Client for the 549 CGB contracts was $142.725883, while the average price paid by BMONBI for the 171 CGB contracts purchased by Carelli between the time he learned of Client's order and the placing of that order by Li was $142.694152, such that Client paid $5426.07 more than if BMONBI had given it the benefit of Carelli's purchase of 171 contracts (also referred to as the "**Impugned Trades**");

o) Lambert again maintained that the erroneously labelled Client sell order for 549 CGBs at 13:21:33 misled the market, despite its having been corrected shortly thereafter, and that Carelli's hedging activity had the effect of removing liquidity from the market before the posting of Client's buy order, which affirmations were contested by Respondents;

p) BMONBI claims it lost approximately $200,000 in filling Client's orders on May 31, 2019, but did not produce any documentary evidence to corroborate this claim, which provoked an objection from the Bourse's counsel. Furthermore, Carelli seemed to suggest that this loss was entirely attributable to the cash bond trading on that date (E-20, pages 43 and 77), while Respondents' counsel allege, in para. 56 of their Plan of Argument, that this loss was attributable (in unspecified proportions) to both the cash bonds and the CGBs;

q) In any event, the Committee maintains the Bourse's objection regarding the amount of the loss allegedly suffered by BMONBI as a result of its trading activities for Client on May 31, 2019, because of the best evidence rule. Furthermore, the Committee is of the view that the existence or quantum of such a loss would not be relevant to determining the guilt or innocence of the Respondents herein;

r) Carelli also admitted in direct examination that he could not say whether Client was aware of his hedging activities on either date, which admission was reiterated by BMONBI, as we will see below.

Investigations by the Bourse and BMONBI

23. Lambert, who took over the Bourse's investigation in this case after the departure in October 2021 of the initial investigator, Ms. Jessica Vu ("**Vu**"), testified that the Bourse's investigations of the events of March 19 and May 31, 2019 were initiated by alerts from the Bourse's market surveillance system (known as "SOLA") which flagged potential front running by BMONBI after the events of those dates (see E-20, pages 10 and 29). These investigations were eventually merged into a single investigation, which uncovered the other alleged infractions which are mentioned in the Complaints filed against the Respondents herein.

24. The earliest documentary evidence of these investigations filed in the record is an email from Menon to Carelli dated April 11, 2019 (E-20, page 73), where Menon informs Carelli that the "Bourse wants us to shed some light on why firm orders were entered prior to client orders". The chronology of events prepared by BMONBI (E-49) mentions that the first communication from the Bourse regarding the events of March 19, 2019, was received on April 5, 2019.

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25. Carelli responded by email on April 11, 2019, focusing mainly on his hedging activity of March 19 (E-20, page 73).

26. At the time of the alleged infractions in this case, BMONBI had the following three lines of defence to enforce supervision and compliance with market rules, including those of the Bourse, as described by Moore and corroborated at E-2, page 9, para. 11, and E-20, page 109:

a) the first was the Trade Floor Supervision ("**TFS**"), whose staff (including Jason Park, Dave Persaud and Menon) were responsible for overseeing how the trading staff carried out their daily duties;
b) the second was the Capital Markets Surveillance team headed up by Moore;
c) the third was the audit team, which conducts routine audits of the enterprise.

27. BMONBI had two surveillance systems in place to detect irregularities such as front running, each of which operated independently of the other:

a) the PMD (Price, Manipulation and Detection) system, an in-house report producing system used by the TFS to conduct daily derivatives surveillance, and flag potentially manipulative and deceptive trading practices, including front running; and
b) the SMARTS systems, a browser-based application owned and operated by the NASDAQ, which was used by the Capital Markets Surveillance team to monitor potentially manipulative trading activity.

28. In his letters to Vu dated September 23, 2019 (E-2, pages 7 et seq.), September 21, 2020 (E-20, pages 5 et seq.) and December 8, 2020 (E-22), Moore brought the following facts to light:

a) The SMARTS system did not send out any alerts for potential front running regarding the Impugned Trades of March 19 and May 31, 2019 (E-2, page 10, para. 13).
b) Moore explained (E-20, page 7, para. 2) that the SMARTS alert system to detect possible front running was calibrated by BMONBI in such a way that the total value of the client trade had to exceed a certain percentage of the average daily traded value for the relevant security and that BMONBI had chosen (prior to the trades of March 19 and May 31, 2019) the suggested default value of 2% to trigger such alerts, which default option appears in the 2020 version (E-20, page 94, Value Multiplier Proprietary), presumably in order to reduce the number of false positive alerts.
c) BMONBI eventually recalibrated the SMARTS system (which has 2500 parameters requiring calibration) to provide alerts for all transactions having an accumulated value in excess of 0.1% of the average daily traded value for the relevant security.
d) In his letter of September 23, 2019 (E-2, page 11, para. 14), Moore stated that "Compliance is currently undertaking a review and evaluation of the SMARTS alert thresholds and parameters to ensure certain thresholds are calibrated accordingly going forward", said recalibration having apparently been finally approved on or about October 10, 2019 (E-20, pages 102 and 103).
e) The PMD is an in-house report-producing system used by the TFS for daily derivatives surveillance and manipulative and deceptive practices, which filters

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BMONBI's trade management system for firm trades executed in front of potentially market moving client transactions and identifies exceptions for review.

f) As explained by Moore to the Bourse in his letter dated December 8, 2020 (E-22, page 2, para. 2), the PMD was set to send an alert whenever the number of CGB trades exceeded 200 contracts, such that alerts were in fact triggered by the higher volume CGB trades of March 19 and May 31 but that, as explained below, no irregularity was found to exist by the TFS representative who analyzed the trades.

g) When asked on November 13, 2019, by his superior, Dave Persaud, to explain why he did not find any irregularities in the trades of March 19 and May 31 after receiving the PMD alerts, Menon responded as follows (E-20, page 88):
"My basic dismissal for both these alerts were that since Franco and Brad are from different trading desks, Franco will not be a participant of the chats with Brad's end client. Also, for the second one, the number of contracts on our alert was only 2 and 2 contracts is very small to move the market. We have an enhanced review now in place where we look at chats and voice records for firm trades done prior to any client trades at better fills (duration one hour prior) for any members from Jason Park's team."

h) Menon had provided a similar explanation in his email dated September 6, 2019 (E-20, page 82, top half) and had provided earlier that day (E-20, pages 82 and 83) a copy of BMONBI's procedure 8.1.2 regarding Front Running (which had last been revised in December 2018, E-20, page 86), which discussed article 6305, the precursor to article 7.6, which came into effect on January 1, 2019, which will be discussed further below.

i) Menon does not seem to have been aware of the fact that, although BMONBI's agency traders and liquidity providers operated out of different offices, it was normal for them to exchange information about pending client trades, as acknowledged by Moore;

j) For some unexplained reason, the PMD system did not flag the 169 other CBG contracts purchased by Carelli on May 31, 2019, as appears from BMONBI's Futures FRT Exception Report, which only flagged 2 CGB trades (E-29, page 2, at 13:21:45), leading Menon to comment "**Firm contracts only 2 – no concern no much to move the market**" (E-29, page 4).

k) Lambert was critical of the PMD system's failure to identify more than 2 of the 171 CGB contracts traded by Carelli on that date, while Moore said that the fact that the system picked up 2 potentially dubious contracts was enough of a signal to Menon to inquire more deeply into the situation, which he failed to do, and that discussions were subsequently held with Menon to avoid a recurrence. Moore added that BMONBI adjudicates approximately 63,000 alerts per quarter.

l) In his letter of September 23, 2019 (E-2, page 10, para. 13), which dealt with the Impugned trades of March 19 and May 31, Moore stated that although "Compliance did not find material evidence indicating any attempt to front-run the client's orders…Compliance did, however, note a potential issue concerning best execution and/or priority of transactions…because Mr. Carelli continued to enter hedging orders both before and after the pre-negotiation discussions with the client…Following these events, Mr. Carelli was reminded that from the time a client order is placed, that client must be given the benefit of any better priced orders in the market until the client's order is filled, unless explicit consent is provided by the client to allow the firm to trade alongside the client order" (E-2, page 10, para. 13).

29. On July 15, 2019, Moore requested Thy Nagesvaran, a Compliance officer working on Moore's team, to provide him with "a write-up why our monitoring did not catch" the

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Impugned Trades of March 19 and May 31 and an assessment of possible remedial measures (E-20, page 62).

30. In his reply of the same date (E-20, pages 61 and 62), Mr. Nagesvaran explained the reason why the SMARTS system did not provide alerts on those dates, as set forth above, indicating that “after consulting with our partner in Nasdaq, an adjustment was made to reduce the client trade size threshold to 0.1% of total daily volume” which new threshold apparently generated “a considerable higher number of false positives”.

31. He also explained that BMONBI’s PMD system had in fact flagged the suspect trades on March 19 and May 31, but that it had theretofore been the TFS policy to “conduct further analysis on potential Front Running if the firm and client trades were confined to traders on the same desk” which would then “include reviewing communications conducted via chat or phone” (E-20, page 61). As mentioned above, this was not done because of Menon’s mistaken belief that Carelli and Wishart were at different desks and therefore isolated from each other. Nagesvaran concluded by stating that “TFS has revised their review of the Front Running reports to include additional scrutiny of **any** firm trades conducted ahead of client facilitation orders by the agency desk which also include a review of potential communications between all parties involved”.

32. Moore testified that Menon incorrectly assumed that BMONBI’s liquidity provider (Carelli) and its futures agency traders (Wishak, Stroble and Li) were in separate offices (or “desks”) and therefore not in contact with each other regarding the trades of March 19 and May 31, and that he therefore did not verify BMONBI’s records of telephone conversations and chatroom discussions. Menon’s conclusion in this regard is confirmed by the note at the bottom of page 2 of the PMD exception report for March 19, 2019 (E-28, page 2).

33. On June 16, 2019, BMONBI sent a one-page Gatekeeper Report (E-30) to the Bourse, signaling only two “Possible Violations”; namely, regarding article 6.114 (Order Priorities) and 7.3 (Best Execution Required). The report did not expressly refer to a possible violation of article 7.6 (Front Running), although it did mention Carelli’s above-described hedging activities.

34. It appears (E-20, page 58) that there was a prior discussion at BMONBI about expressly referring to a possible violation of article 7.6 in the Gatekeeper Report, but that a decision was made not to do so, Moore having testified that his team ultimately determined that there was no front running, as mentioned in BMONBI’s letter to the Bourse dated December 18, 2020 (E-24, page 1).

35. When asked why she entered the May 31 sell order for 549 CGBs as a “client” order, Ms. Li responded as follows (E-25, page 2, question 4):

> “The Firm order was inadvertently marked as a Client order because that is the default setting for our agency desk, which most frequently enters orders on behalf of clients.”

36. Moore testified that posting the firm sell order first was done deliberately, arguing that placing a buy order first would be interpreted by traders from other firms as a sign for them to bid higher, knowing that the bidder was committed to a trade, thereby jeopardizing the execution of the transaction and that, for this reason, putting the buy order first would “not make sense”. He added that the client consent to this way of proceeding, as required by article 6.205 of the Rules, was implicit and that such consent could easily be corroborated by the client, if and when requested by the Bourse.

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37. In paragraph 26 of the Summary of Facts, the Bourse recognized that the said mismarkings of the sell orders on March 19 and May 31 were corrected within 45 and 80 minutes respectively, but Lambert maintained that the market was nevertheless misled by these shortlived mismarkings, because (in his view) the market reacts differently to a client order as opposed to a firm order. Respondents' witnesses denied that the market screens show whether a buy or sell order is for a client or a firm.

38. On June 19, 2019, Menon circulated a memo (E-32) addressed to the futures agency traders and the other members of the TFS attaching a "guidance with respect to facilitating client orders", entitled "Agency Orders and Firm Hedging", the relevant extracts of which read as follows:

> "Hi team,
>
> We would like to bring to your attention an important aspect of the rules of the Montreal Exchange when executing crosses with clients.
>
> Under the Rules of the Exchange when facilitating client orders - especially in instances where we are crossing with them – we cannot trade ahead of the client order at a **better** price once a client order has been received unless we have **explicit** consent for the customer to take the better fills in inventory. This is true even if the purpose is to hedge our own risk regardless of whether we are hedging pre-existing risk or risk with the agreed upon trade.
>
> If we continue with the same processes being used for client facilitation, the most effective solution is to ensure that we have the client's explicit consent to trade ahead of them prior to crossing against their order. We understand this is not required on equity markets but it is required on the Montreal Exchange."

39. Similar advice was given on June 13, 2019 by BMONBI in what appears to be a generally circulated message entitled "Compliance Bites" (E-31 and E-20, page 104).

40. Lambert took issue with BMONBI's position in these two communications wherein BMONBI advised its trading staff that they could trade ahead of a client order (once that order was received and before it was posted) and keep any better fills for the firm if they had the client's "explicit consent", the Bourse's position being that (unlike article 6.114, Order Priorities) no such exception (even client consent) is contemplated in article 7.6 of the Rules.

41. Carelli was given an undated letter (E-24, page 3), which the Bourse alleges in section 5 of its Summary of Facts was remitted to him by Jason Park on June 13, 2019 (which is consistent with the two emails found at E-20, page 53, and corroborated by Respondents' counsel at para. 64 of their Plan of Argument), a draft of which was circulated amongst the members of the Compliance team, including Moore. This letter, which BMONBI stated would "be kept on file and any further contravention of regulatory requirements will be subject to potential disciplinary measures", informed Carelli that "a detailed review of your trade activity for CGBM19 on March 19, 2019 as well as for CGBU19 on May 31, 2019 determined that the activity is in contravention of MX Rules of the Bourse Article 7.6 – Front Running Prohibited", the details of which trading activity were then set forth.

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42. The letter stated that "there was no indication the client was aware of this trading activity" (ahead of the posting of its buy order), and that "we were offside on the rule as firm orders **continued** to be entered after (Client) had consented to the price of the client order".

43. Moore testified that this letter was drafted by Nagesvaran and given to Carelli before BMONBI's investigation was completed (by the filing of the Gatekeeper Report on June 26, 2019, E-30) and that he now doesn't agree with the conclusions of said letter or that it "properly characterizes" the conduct which took place, although he admits he may have "looked at it briefly" at the time. Curiously, he added that Nagevaran was conflating the front running rule (article 7.6) with articles 6.114 and 6.205, even though these two latter provisions are not referenced in the letter (E-24).

The expert testimony herein

44. Respondents filed the expert reports of Professor James J. Angel ("**Angel**") and Naresh Tejpal ("**Tejpal**"), as E-47 and E-51 respectively.

45. The Bourse objected to paragraphs 1, 4, 6, 8, 16(a), 19, 33, 34, 49 and 53 to 58 inclusive of Angel's report (E-47), which deal mainly with the issue of front running and best execution and the Client's implicit approval of same. Although the jurisprudence will sometimes allow an expert to opine on an ultimate issue, it has been consistently recognized that the court or tribunal is not bound by such opinions. In this case, the issue is moot in view of the Committee's findings on front running and best execution which are contrary to the experts' opinions herein.

46. As appears from his CV, Angel has been a professor since 1991 at the McDonough School of Business at Georgetown University, in Washington, D.C., and has taught during his career about capital markets, investments and fixed income securities as well as complex financial instruments and derivatives.

47. His research "involves the nuts and bolts of how financial markets work" (E-47, para. 10) and he has visited over 85 licensed exchanges around the world to learn more about how markets work. While attending an academic conference in Montreal several years ago, Angel solicited an invitation to visit the Montreal Exchange and tour its trading floor. He first read the Rules of the Bourse last fall as part of preparing his report.

48. The parties agreed that Angel was qualified to testify as an expert on exchange traded derivative markets and trading practices.

49. As appears from paragraph 16 of his report (E-47), Angel's mandate in this case was to review the Impugned Trades of March 19 (incorrectly referred to as March 31 in this section of his report) and May 31, 2019, and opine on:

(a) "whether the Respondents engaged in front running within the meaning of Article 7.6(a) of the Rules of the Montreal Exchange;
(b) whether "BMONBI provided best execution to the client within the meaning of Article 7.3 of the Rules";
(c) the "risks associated with entering a client order ahead of the firm's order in a client-principal cross transaction in the circumstances of the TMX market for CGB contracts" on March 31 (sic) and May 31, 2019;

(d) whether, having regard to the context and circumstances of March 31(sic) and May 31, 2019, "there a basis to conclude that a sophisticated institutional fund manager client would have implicitly consented to the entry of the executing broker's order ahead of the client's order?".

50. Angel confirmed that he was not asked to consider or opine on article 7.6(b) of the Rules, Respondents' counsel having declared that BMONBI considered said provision inapplicable in this case.

51. At the hearing, Angel testified as follows in his direct examination:

(a) he affirmed that the rules regarding best execution and front running are similar globally;
(b) he defined front running by a broker as harming your customer by trading against your client and thereby bidding up the price before executing the client order;
(c) he defined best execution as doing your best to get the best deal for your client, considering all relevant market factors;
(d) he argued that Carelli did not "take advantage" of Client's orders because he did not start trading until the client had confirmed a meeting of the minds regarding the orders (including the desired number of CGB contracts and the price) by saying "done" or words to that effect, such that "the (Client's) trades were already completed";
(e) the Impugned Trades by Carelli on these two dates could not qualify as front running because they did not affect the prices paid by Client, as these were prearranged trades with a "worst price" limit.

52. In his analysis of the trades of March 19, 2019 (E-47, paras. 20 to 37), Angel makes the following allegations:

(a) BMONBI's inventory of June 2019 CGBs was in a short position before receiving the Client's order and it would therefore "normally be purchasing contracts in the normal course of business to cover its short position", given that "liquidity providers such as BMONBI generally like to hold as little inventory as possible, because inventory is expensive and risky to hold" (E-47, para. 21);
(b) Carelli's three Impugned Trades between 14:43:49 and 14:44:49 were not front running because they were placed after BMONBI's "binding commitment" (at 14:43:48) to source 546 CBG June 2019 contracts at a maximum average price of $138.04 (E-47, para. 33);
(c) the price of $138.04 quoted by BMONBI for 546 contracts was better than the best available price available at 14:43:26 on the market for an order that size, and that Client would have paid an average price of $138.045 had it attempted to buy all 546 contracts immediately (E-47, para. 25);
(d) had the Client attempted to buy 546 contracts at 14:43:49, it would have paid an average price of $138.049 (E-47, para. 32);
(f) Carelli's skillful placing of the three Impugned Trades allowed BMONBI to fill Client's order at an average price of $138.037875, which was lower than the quoted price of $138.04 and lower than the price(s) Client would have paid had it attempted to buy the 546 CBG contracts in a single bid (E-47, para. 36);

53. Angel made the following allegations in his report regarding the trades of May 31, 2019 (E-47, paras. 38 to 53):

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a) BMONBI's book was in a short position on that date because of the Client's previous purchase of cash bonds in the approximate amount of $142 million;
b) Carelli quoted a "worst price" of $142.73 to Stroble at 13:20:54 (E-47, para. 43), which price was then communicated to the Client by Li at 13:21:11 (E-47, paras. 44 and 45);
c) Carelli then placed his two impugned orders for 100 contracts at 13:21:12 and 13:21:44, which Angel says did not constitute front running because the "worst price" of $142.73 had already been "locked in" at 13:21:11 (E-47, paras. 47 to 49);
d) the price obtained by Carelli's trading strategy, by "breaking the order into smaller parts and executing them" resulted in a far better price for the Client than entering the entire 549-contract order to the market first, which "could have disrupted the market and moved the price adversely" (E-47, paras. 41, 42, 50 to 52).

54. Angel therefore concluded his report as follows (E-47, paras. 55 to 58);

a) "The impugned trades on March 19, 2019 and May 31, 2019 were not frontrunning by BMONBI within the meaning of Article 7.6(a), as they were entered into after BMONBI had made a binding price commitment to the client. One cannot front run after the price to the client has been established."
b) "BMONBI's trading activities in both cases were consistent with its duty to seek best execution for the client. BMONBI demonstrated reasonable care in getting the most advantageous execution terms possible, given the market conditions at the time. In both cases, the client received prices far superior to what was available in the limit order book at the time of the order".
c) "Had BMONBI entered the client's order into the market ahead of the firm's order, it is quite possible that the large size of the order relative to the liquidity displayed in the market would have disrupted the market, resulting in more price impact and volatility in Canadian Government Bonds and futures than necessary. The price impact could have resulted in BMONBI getting worse prices on its covering trades. BMONBI would have had to price the market impact into the price it provides to client, reducing execution quality to the client."
d) "A sophisticated institutional fund manager client would understand how BMONBI adds liquidity and would have implicitly consented to how BMONBI handled the trade by entering its own orders into the market before the client's. In both cases, the client had accepted a firm price from BMONBI and would not have cared how or when BOMNBI later covered its resulting position."

55. Angel's cross-examination revealed the following:

a) he was never shown the documents in E-20, including the various letters therein authored by Moore and others, nor was he shown Moore's letter dated September 23, 2019 (E-2, page 7);
b) he was not made aware of any front running alerts triggered by the trades of March 19 and May 31, 2019;
c) his above-described (and last) visit to the Bourse was about 20 years ago, while at a conference in Montreal;

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56. Tejpal's CV describes himself as an "experienced trader, regulator, and compliance officer with 35 years of experience in the financial services industry", who has worked in these fields of activity for BMO, CIBC, RBC and the Investment Industry Association of Canada.

57. The parties agreed that Tejpal was qualified to testify as an expert on regulatory compliance and exchange traded derivatives. A summary of Tejpal's "anticipated non-opinion evidence" was provided as Appendix B to his report (E-51).

58. The salient points of Tejpal's testimony are as follows:

a) liquidity providers manage risk by hedging, hoping to maintain a neutral position;
b) CGB futures contracts are used for hedging underlying cash bonds;
c) Tier 1 and 2 supervision teams of firms like BMONBI will use automated alert systems, which may or may not be the same;
d) alert systems are not perfect or foolproof and need to be recalibrated all the time, in an ongoing attempt to strike a reasonable balance between too many and too few alerts;
e) for prearranged transactions such as in this case, when the price quoted by the firm is above the market price, firms do not give the benefit of lower-priced fills purchased on the way up to the agreed price, because the client has agreed to pay a fixed price, leaving all of the risk to the trader;
f) when shown Moore's clear statement to the contrary in his letter to the Bourse dated September 23, 2019 (E-2, tenth page, final paragraph of section 13), Tejpal said he disagreed with Moore;
g) he reviewed Angel's report and agreed with its conclusions, but did not himself review the supporting data (chat, telephone and trading records).

C. ANALYSIS

Count 1 – Front Running

59. Article 7.6 of the Rules reads as follows:

"**Front Running Prohibited**

No Approved Participant, Person employed by or acting on behalf of an Approved Participant or Person associated with an Approved Participant shall:

a) take advantage of a customer's order by trading ahead of it; or
b) engage in Transactions based in whole or in part on non-public information

concerning pending transactions in Securities, Options, or future contracts, which are likely to affect the market prices of any other Securities, Options or future contracts, unless such Transactions are made solely for the purpose of providing a benefit to the client who is proposing or engaged in the Trade."

60. Although the Rules do not define "front running", Lambert and Bourse's counsel took the position that hedging is permitted between the moment a deal is struck between the client and the Approved Participant confirming the relevant details of a trade and the posting of client's order on the market, as long as the client receives the benefit of such hedging trades, which position is said to be consistent with the wording of articles 7.6 (a) and (b), as no

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advantage is thereby procured by the Participant and the entire benefit of the hedging trades is given to the client.

61. Respondents' counsel invoked Lambert's admission that the Bourse has never issued guidance to this effect, although this fact (even if true) does and should not affect the interpretation of article 7.6.

62. Respondents' counsel invoked Circular 077-19 of the TMX dated May 22, 2019 (E-53), which solicited comments on proposed amendments to article 6.206 of the Rules to allow additional reporting time for large block transactions involving at least 3500 CGBs, citing only the final sentence of the following passage (at page 6 of E-53):

> "It should be noted that the proposition has no impact on the compliance, supervision and reporting rules on the Bourse. Participants engaged in block transactions (no matter the size of the trade and the reporting time delay applicable) should comply with the Rules on the Bourse and are subject to the Regulatory Division of the Bourse oversight. As a reminder, participants must at all times adhere to the principles of good business practice in the conduct of their affairs. **Specifically for block transactions, the Bourse would like to remind participants that practices such as front running (article 7.6) are prohibited**. The Bourse feels that increasing the reporting time delay would also help prevent undesirable behaviors from market participants, given the fact that it may be easier to identify participants involved in large CGB block transactions. Allowing an insufficient amount of time for these participants to execute their hedging strategy might create unhealthy awareness and lead to unnecessary market disturbances".

63. Respondents argue that the final sentence of this passage from the Circular constitutes recognition by the Bourse of the acceptability of hedging (in a proprietary manner) prior to posting a client order on the electronic trading board as being an exception to the front running rule.

64. The Committee cannot agree with such a broad interpretation of the Circular, as the above-cited passage was part of a request for comments and expressly reaffirms the preeminence of article 7.6, including the prohibition in 7.6(a) against taking advantage of a customer's order and the requirement in 7.6(b) that trading based on non-public information concerning a pending transaction is allowed solely for the purpose of providing a benefit to the concerned client.

65. Respondents also invoked a letter dated September 9, 2011 from the TMX Group Inc. to Ontario Securities Commission and the AMF (E-54) responding to a request to provide input on CSA Consultation Paper 91-402 on Derivatives: Trade Repositories regarding the reporting of OTC derivatives transaction data to trade repositories, as well as the operation and governance of such repositories, in which the following statement was made:

> "The TMX supports the Committee's recommendation to exempt block trades from real-time reporting requirements. Real-time reporting of block trades can threaten anonymous trading, make hedging more expensive and therefore discourage parties from providing liquidity".

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66. The Committee fails to see how this isolated passage from a letter relating to the establishment of a derivatives trade repository sheds any light on the interpretation of article 7.6.

67. In interpreting article 7.6, care must be taken to avoid indiscriminately applying less restrictive definitions of front running recognized in other jurisdictions, as these may stipulate exceptions which are not found in the Bourse Rules.

68. For example, the Committee refers to the following extracts from Rule 4.1 of the Universal Market Integrity Rules (UMIR), cited by Respondents in para. 77 of their Plan of Argument:

> "(1) A Participant with knowledge of a client order that on entry could reasonably be expected to affect the market price of a security or a derivative, shall not, prior to the entry of such client order….enter a principal order or a non-client order on a marketplace…for the purchase or sale of the security, derivative or any related security or related derivative;
> (2) A participant does not contravene subsection (1) if …an order is entered or trade made for the benefit of the client for whose account the order is to be made …or an order is solicited to facilitate the trade of the client order… or a principal order is entered to hedge a position that the Participant had assumed before having actual knowledge of the client order provided the hedge is … commensurate with the risk assumed by the Participant and (is) entered into in accordance with the ordinary practice of the Participant when assuming or agreeing to assume a position in the security".

69. Thus, article 7.6 stands on its own and the Committee has no choice but to interpret it according to the clear and limited terms in which it is drafted. Article 7.6 cannot be interpreted in the same manner as UMIR Rule 4.1 unless the text is amended to include similar exceptions.

70. The following jurisprudence submitted by Respondents regarding front running is not helpful in interpreting article 7.6. as the decisions involve instances of clear self-dealing by brokers based on knowledge of confidential information, rather than hedging in association with a client order:

- Re Biscotti (1992), 1992 CarswellOnt 1469, 16 OSCB 31
- Re Greco (2004), 2004 CarswellOnt 3207, 27 OSCB 6975
- Re Fediuk, 2005 CarswellNat 7229

71. The following jurisprudence has consistently held that statutory and regulatory texts which are clear and unambiguous must be simply applied, without importing unexpressed exceptions, and that recourse to legislative purpose is appropriate only where the text is ambiguous and admits of more than one reasonable interpretation:

- Ontario vs Placer Dome Canada Limited, (2006) 1 S.C.R. 715, para. 23
- Shell Canada Limited vs Her Majesty The Queen et al, (1999) 3 S.C.R. 622, paras. 40 and 43
- Agence du Revenu du Québec c. Des Groseillers et al, 2021 QCCA 906, paras. 49 to 51.

72. The Impugned Trades were made by Carelli within 83 and 94 seconds after his awareness of Client's intention to buy a certain number of CGB contracts on March 19 and

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May 31, 2019, respectively (after almost two hours had passed since the bond trade on March 19 and 5 minutes since the bond trade request on May 31, 2019). In light of Carelli's admission that his practice was to assume a transaction would almost always result after Client expressed an interest in buying CGBs, the Committee concludes from Carelli's similar pattern of conduct on both dates (and timing thereof) that the Impugned Trades were made because of Carelli's knowledge of the non-public information of the Client's intention to buy CGBs on those dates and his desire to cover BMONBI's risk on the anticipated transactions.

73. In any event, in view of BMONBI's obligation to procure the best price for the Client (subject to the "worst price" limits), BMONBI had a duty from (at least) the moment of its awareness of Client's intention to buy a specific number of CGBs, to prioritize the interests of the Client over its own interests, even if Carelli was truly hedging via the Impugned Trades to cover previously incurred risks from bond trading.

74. Respondents argue (in para. 54 of their Plan of Argument) that they did not "trade ahead" of Client's orders because the Impugned Trades invoked by the Bourse occurred after a meeting of the minds (or "handshake") between BMONBI and Client regarding the CGB transactions in this case, of which the market had no knowledge. With respect, if the words "trading ahead of it" (i.e. the client order) referred to the handshake confirming the client order rather than its posting on the market, then Participants would only be deemed to infringe article 7.6 by trading before the "handshake" (or meeting of the minds), which makes no sense, because such an interpretation would only apply to trades made by the firm before its awareness of a pending order.

75. Furthermore, the Committee considers that the words "trading ahead of it" in article 7.6(a) refer to the moment the client order is posted on the electronic trading system.

76. In this regard, the Committee notes that the French text of article 7.6(a) draws a clear distinction between an order and the resulting transaction:

> " **Devancer une Opération**
>
> Aucun Participant Agrée, personne employé par un Participant Agrée ou agissant au nom d'un Participant Agrée ou Personne associé à un Participant Agrée ne doit:
>
> a) prendre avantage d'un ordre d'un client pour devancer l'Opération ».

77. The word «Opération» is defined as follows:

> « **Opération** (Trade or Transaction) signifie un contrat pour l'achat ou la vente d'un Produit Inscrit ».

78. The Committee is also of the view that the offending trades contemplated in article 7.6 are (in this case, at least) proprietary trades posted on the market between the time that the participant and client confidentially agree on the terms of the trade and the moment the client's order is posted on the electronic trading board.

79. There is no doubt that the Client's orders to buy 546 and 549 CGB contracts on March 19 and May 31, 2019, at the agreed upon "at worst" prices constituted "non-public information" and that Carelli traded ahead of the moment the Client's orders (for 546 and 549 CGBs) were posted (and then executed).

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80. Angel's report confirms that the state of the markets on March 19 and May 31, 2019 was such that the trades sought by the Client could not be realized at the desired limit prices by placing a single order on the board (E-47, paras. 32 and 40 to 42).

81. The Committee considers that the Impugned Trades carried out by Carelli reduced the availability (liquidity) of CGB contracts available to fill the Client's orders and were therefore likely to affect the market prices of the remaining CGB contracts required to fill the Client's orders.

82. The question now becomes, for the purposes of article 7.6(a), were Respondents "taking advantage" of the Client's orders by carrying out the Impugned Trades?

83. Respondents argue that hedging prior to posting the Client's order is a legitimate way of facilitating that order and assuming risk from the Client and that, in doing so, they did not "take advantage" of the Client.

84. Respondents counsel, in his opening remarks, stated that the quotes given by Carelli to the Client were made on an "at worst" price basis (see, as well, para. 41 of Respondents' Plan of Argument and para. 21 of Respondents' Reply dated September 22, 2023), meaning that the ultimate price paid by the Client could be lower than the maximum quoted price, depending on market conditions.

85. This was confirmed by BMONBI, which ultimately filled the orders for slightly less than the maximum quoted prices because of the lower-priced fills obtained by the agency traders. Thus, the CGB contracts picked up by BMONBI's agency traders at lower than the quoted "at worst" prices on March 19 and on May 31 were delivered to Client at those lower prices, not the quoted "at worst" prices.

86. However, the prices ultimately charged by BMONBI to the Client did not give the latter the benefit of the Impugned Trades (from Carelli's hedging before the posting of Client's orders) on March 19 and May 31, 2019, the Bourse having initially calculated those benefits as being $6299.75 on March 19 and $5425.99 on May 31, although the Bourse's counsel conceded during her summation that these figures might be $3150 and $5426.07 respectively (if restricted to the Impugned Trades).

87. If, as implicitly suggested by Angel (E-47, paras. 34, 47, 49 and 55, where he refers to "locked in" or "established" prices) and Tejpal, the Client had committed to buying the CGB contracts at the quoted worst prices (and not a penny less), BMONBI would not have given Client the benefit of the lower priced fills obtained by the agency traders and then crossed when posting the Client's buy orders. If BMONBI did give Client the benefit of these lower-priced fills, why would the same rule not apply to the lower priced fills obtained by Carelli from the Impugned Trades?

88. Respondents argue, in para. 87 of their Plan of Argument, that "it is unreasonable to insist that Mr. Carelli should have given up every better priced resting offer in the market after he had already committed to a very favorable price for the sub-block and the bonds. Certainly, (Client), a highly sophisticated institutional investor, which was watching the market closely on both days, never had that expectation".

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89. If, as stated by BMONBI and Carelli (see para. 96 below), there was no indication that Client was aware of the Impugned Trades, the Committee cannot accept Respondents' argument that Client had no expectation of receiving the benefit of said trades, leaving aside the fact that no proof was led to establish this contention.

90. Furthermore, if BMONBI retained for itself the benefit of the Impugned Trades, it cannot be said that these trades were made solely for the benefit of the Client. On the contrary, they appear to have been made to limit BMONBI's risk in fulfilling its obligations under each limit price transaction.

91. In fact, BMONBI recognized its contractual obligation to give Client the benefit of the Impugned Trades in Moore's letter to the Bourse dated September 23, 2019 (E-2, 10th page, para. 13), unless there was an agreement with client to the contrary, at a time when BMONBI's investigation of these events was supposedly completed. This was not a legal statement based on an erroneous interpretation of the Rules. It was in fact an admission regarding the terms of the contractual relationship between BMONBI and Client.

92. The Committee is of the view that BMONBI's obligation, in quoting the "at worst" or maximum prices on March 19 and May 31, 2019, was not an undertaking to deliver the desired number of CGBs at the quoted prices, but to deliver them at the best price possible (which should include lower priced fills from hedging) and, in any event, for no more than the quoted "at worst" prices. Thus, there was an undertaking to deliver the desired number of CGBs at the best possible price, subject to the worst (maximum average) prices quoted by Carelli. This was recognized by Angel in paragraph 2 of his report (E-47).

93. Although Tejpal voiced his disagreement with Moore's said statement, he was not in a position to contradict Moore's factual admission as to the nature and terms of the contractual agreement between BMONBI and the Client in this specific case.

94. Furthermore, Moore did not expressly retract this admission, apart from saying that it was the result of a "more conservative" approach.

95. Moore's admission was also confirmed by BMONBI in its Compliance Bite dated June 13, 2019 (E-31) and in its undated letter to Carelli in June 2019 (E-24).

96. Angel opined that a sophisticated client would normally have been aware of and consented to Respondents' hedging activities, but this opinion is contradicted by BMONBI's admission that "there does not seem to be any indication that the client was aware of said activities" in its said letter to Carelli (E-24) and in its Gatekeeper Report dated June 26, 2019 (E-30), where it stated that "**upon further review of the communications related to these orders, it appears the client may not have been aware that the firm would be hedging the risk in its own account at prices below the agreed upon block price**". A similar admission was made by Carelli in his testimony, as noted in paragraph 22(r) above.

97. Respondents' counsel argue, in paragraphs 21 and 22 of their Plan of Argument, that Lambert admitted that no one at the Bourse's Regulatory Division ever spoke to any representative of the Client during its investigation, that the Bourse's failure to call the Client to testify as to whether it was harmed or disadvantaged by Respondents' conduct should give rise to an adverse inference in that regard, and that ""BMONBI was not required to inconvenience its client to reinforce facts that are plainly obvious", given the high degree of Client's sophistication in trading cash bonds and CGBs.

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98. Lambert's testimony relied almost exclusively on the documentary record provided by BMONBI during the Bourse's investigation. If there was anything incorrect or misleading in that record, it was up to Respondents to adduce appropriate probative evidence in that regard at the hearing. Otherwise, the evidence in the record makes proof against all parties concerned, on which the Committee is entitled to rely.

99. In view of Respondents above-mentioned admissions that the Client "may not have been aware that the firm would be hedging the risk in its own account at prices below the agreed upon" price, the Committee cannot accept Respondents' argument that it was "plainly obvious from the record" that Client was in fact aware of the nature and extent of the Impugned Trades.

100. The Committee must therefore give greater credence to Respondents' said admission than to the experts' assertion to the contrary, in the absence of contradictory testimony from the Client.

101. In view of the foregoing, the Committee finds that Respondents did "take advantage" of the Client's orders on March 19 and May 31, 2019 by trading ahead of them for BMONBI's own benefit, as it did not pass on the benefits of the Impugned Trades to the Client, which it was bound to do pursuant to the "at worst" price agreements.

102. As regards, article 7.6(b), on which neither of Respondents' experts opined, Respondents' counsel argued that it did not apply to this case by attributing a restrictive interpretation to the words "which are likely to affect the market prices of any <u>other</u> Securities, Options or future contracts".

103. In other words, according to Respondents' suggested interpretation, article 7.6(b) is breached in this case only if the "Securities, Options or future contracts" likely to be affected by the impugned transactions are not the same type as the security, option or future contract that is the subject of the impugned transaction.

104. Counsel for the Bourse disputed this interpretation and invoked the French text of article 7.6(b), the drafting of which she argued militates against Respondents' interpretation.

105. While the Committee does not agree that the French and English texts are materially different on this point, it does not consider that Respondents' restrictive interpretation of article 7.6(b) is justified or that it is consistent with the obvious objective of the rule.

106. It would be illogical and contrary to the intention of preventing front running, which prohibition exists as much to protect clients as well as other market participants, to prohibit front running in a transaction involving (for example) June 2019 CGBs only where it is likely to affect trading in cash bonds or July or August 2019 CGBs or options on other derivatives tied to June 2019 market results, but not other June19 CGBs. There is no logical reason (in this scenario) that article 7.6(b) should not also apply to transactions likely to affect the market prices of other June 2019 CGBs. That is precisely why front running is proscribed.

107. Lambert and Carelli disagreed on whether the Impugned Trades "were likely to affect the market prices" of CGB contracts being traded on the two dates in issue. However, the Committee is of the view that the words "which are likely to affect the market prices of any other Securities, Options of future contracts" qualify the words "non-public information concerning pending transactions", which (in this case) refers to the Client's orders, not Carelli's Impugned

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Trades, which fall within the ambit of the term "Transactions" in the first line of 7.6(b). This interpretation of 7.6(b) is accepted by Respondents in paras. 62 and 82 of their Plan of Argument and by the Bourse in paras. 5 and 12 of the Summary of Facts.

108. Furthermore, Angel recognized in his report (E-47, paras. 22 to 24, 41 and 42) that the Client's orders of 546 and 549 CGBs would have disrupted the market on March 19 and May 31, 2019.

109. For these reasons, the Committee finds Respondents guilty under article 7.6(a) and 7.6(b) of the Rules, as alleged in Count 1.

Count 2 – Best Execution

110. Count 2 alleges that, as regards the Client orders for 546 and 549 CGBs on March 19 and May 31, 2019, BMONBI "did not diligently pursue the execution of a client order on the most advantageous execution terms reasonably available under all of the circumstances relating to the Trade or Trading Strategy and the then current conditions at the time of the trade".

111. Article 7.3 of the Rules reads as follows:

> "**Best Execution Required**
>
> a) Approved Participants shall take reasonable care consistent with just and equitable principles of trade and diligently pursue the execution of each client order on the most advantageous execution terms reasonably available under all of the circumstances relating to the Trade or Trading Strategy and the then current market conditions at the time of the Trade.
>
> b) To assess the most advantageous execution terms reasonably available, Approved Participants should consider general factors including, but not limited to: Trading Strategy, Trade price, speed of execution, certainty of execution, and overall cost of execution. In the case of strategy or spread Trades, Approved Participants shall consider these factors as they relate to the execution of the overall strategy, rather than the execution of each individual leg of the Trade."

112. The Bourse alleges that BMONBI's failure to give Client the benefit of the Impugned Trades constitutes a violation of the Best Execution rule.

113. BMONBI argues, in paras. 57 to 60 of its Plan of Argument, that it did in fact provide best execution, as the desired number of CGB contracts (546 on March 19 and 549 on May 31) were not available on the quoted market in the requested quantities and prices, and that Client ultimately paid less than the "at worst" prices ($138.04 and $142.73) quoted by Carelli on both dates.

114. In view of our finding above that BMONBI is guilty of front running for having failed to give Client the benefit of the Impugned Trades, the aggregate value of which was calculated by the Bourse to be $11,725.74, and later reduced (during summation) to $8576.07, it follows that such failure also precludes a finding of best execution in favour of BMONBI.

115. Consequently, the Committee finds BMONBI guilty under Count 2.

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Count 3 – Order Priorities

116. Count 3 (amended) alleges that BMONBI contravened articles 6.114, 6.202 and 6.205(b)(ii) and (iii) of the Rules by knowingly taking the opposite side of the Client's orders of futures for its own account, without (i) entering the Client's orders first on the Electronic Trading System, (ii) giving priority to Client's orders and (iii) exposing the Client's orders to the market for the minimum prescribed time of 5 seconds.

117. The relevant extracts of articles 6.202, 6.205(b)(ii) and (iii) and 6.114 read as follows:

i) **6.202 Trading Against Customer Orders (Cross-Trades)**

An Approved Participant may not knowingly, directly or indirectly, take the opposite side of a customer order for the Approved Participant's own account… unless:

a) the customer order has first been entered on the Electronic Trading System and exposed to the market for the minimum prescribed period established in Article 6.205; or
b) the Transaction is otherwise, and explicitly permitted by, and carried out in accordance with the Rules; including, but not limited to, prearranged transactions pursuant to Article 6.205.

ii) **6.205(b)(i), (ii) and (iii) Prearranged Transactions**

b) The parties to a Transaction may engage in communications to prearrange a Transaction on the Electronic Trading System in an eligible derivative in the minimum amount specified where one party wishes to be assured that there will be a counterparty willing to take the opposite side of the Transaction, in accordance with the following conditions:

i) A customer consents to the approved Participant engaging in prearranging communications on the customer's behalf. The consent of the client, in whatever form, must be communicated to the Bourse upon request.

ii) After the first order for the prearranged Transaction is entered into the Electronic Trading System the parties may not enter the second order for the prearranged Transaction until the following specified time period has elapsed as follows: 5 seconds
iii) The party that initiates communication regarding a prearranged Transaction shall have their order entered into the Electronic Trading System first, unless the parties as part of their negotiation agree otherwise. The consent of the client, in whatever form, must be communicated to the Bourse upon request; provided however, that in a prearranged Transaction between an Approved Participant and a customer for an Equity, ETF or Index Option, the customer's order shall always be entered into the Electronic Trading System first, regardless of which party initiated the communication.

iii) **6.114 Order Priorities**
The management of orders' priorities is made on the basis of the chronology of their receipt. The orders initiated for the Firm Account of Approved Participants must be made on an order ticket at the same conditions as those for client orders. In all

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cases, each Approved Participant is responsible for insuring that, at the same price and time stamp, it gives priority to client orders over its own professional orders, unless the client has expressly waived the priority of their order and that such waiver is documented by the Approved Participant.

118. It is clear from paragraphs 21 and 22 of the Bourse's Summary of Facts that count 3 of the Complaint is aimed at the sequencing of the Sell/Buy orders for 546 and 549 CGBs on March 19 and May 31, 2019, respectively.

119. There is no doubt that the Client initiated the communications regarding its two orders, that BMONBI's cross-trade sell orders for 546 and 549 CGBs on the two dates were posted before the Client's cross-trade buy orders for the same numbers of CGBs, and that Client's said buy orders were therefore not exposed to the market for the minimum period of 5 seconds before BMONBI's sell orders.

120. BMONBI made no proof that Client's consent was obtained to post BMONBI's sell orders first.

121. However, Angel corroborated Moore's testimony that placing the Client's buy orders first "made no sense" when he affirmed in his report that:

a) placing the "entire the customer order into the book before putting in the orders that it placed to fulfill the order…would likely have moved the price significantly against the customer because the order was so large compared to the displayed liquidity" (E-47, paras. 6, which affirmation is reiterated in paras. 37, 42 and 57);
b) "any sophisticated customer would have approved BMONBI's actions in filling the order as it resulted in significant price improvement for the customer" (E-47, para. 6).

122. These statements by Angel, which are corroborated by reference to actual market conditions on March 19 and May 31, 2019, do not contravene the jurisprudence cited by the Bourse in support of its aforementioned objection (paragraph 45 above) and are properly admissible in evidence.

123. Furthermore, pursuant to its submissions in paras. 27 and 28 of its Reply, BMONBI presented credible uncontradicted evidence that the most efficient and advantageous manner to execute the cross-trades for the prearranged transactions in this case was to post BMONBI's sell orders first, followed by the Client buy orders.

124. Although BMONBI's argument in this regard is enticing, the Committee feels compelled to apply the clear and unambiguous wording of articles 6.202 and 6.205(ii) and (iii), which require proof of actual consent from the client, rather than an uncorroborated argument based on implicit consent.

125. BMONBI could have brought the Client to testify that such a consent was procured in timely fashion but failed to do so for reasons best known to it.

126. Consequently, the Committee finds BMONBI guilty under count 3.

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Count 4 – Order Identification

127. Count 4 (amended) alleges that BMONBI contravened article 6.115 of the Rules by failing to ensure the proper identification of the orders for 546 and 549 CGBs when entering them by initially attributing BMONBI's sell orders to the Client.

128. The relevant extract of article 6.115 of the Rules reads as follows:

> **6.115 Order Identification**
>
> Approved Participants must ensure the proper identification of orders when entered into the Trading System in order to ensure compliance with the provisions of Article 6.114 regarding management of priorities.

129. BMONBI has admitted misidentifying its sell orders for 546 and 549 CGBs on March 19 and May 31, 2019, by initially ascribing them to the Client rather than BMONBI.

130. These mismarkings were corrected within 45 minutes and 80 minutes respectively on March 19 and May 31, as admitted by the Bourse in para. 26 of its Summary of Facts herein. Moore testified that these mismarkings were not systemic in nature.

131. No explanation was provided for the mismarking of March 19, while (as noted above), Li explained that the mismarking of BMONBI's sell order for 549 CGBs on May 31, 2019, as a Client order was due to a default setting in BMONBI's system E-25, para. 4), and that said mismarking was corrected shortly afterwards. The Committee assumes that the March 19th mismarking occurred for the same reason.

132. The Bourse recognizes the fact that both mismarkings were corrected within less than two hours is a mitigating factor (Summary of Facts, para. 27) but nevertheless, insisted on charging BMONBI for this breach of the Rules.

133. Lambert testified that these mismarkings were apparent to market traders, who were therefore misled by same. His testimony in this regard was credibly contradicted by Moore, Carelli and Tejpal, who testified that order markers are not visible to the market. Thus, the Committee is of the view that the Bourse has not established beyond a preponderance of probability that the mismarkings were apparent to market traders or that any prejudice resulted from same.

134. The Bourse cited two decisions regarding order misidentification:

a) in RBC Dominion Securities (2022 IIROC 19), the failure to include proper order designations was said to have occurred (inter alia) on 174,820 occasions during a four-year period, which justified a consent fine of $140,000;
b) in M Partners Inc. (2018 IIROC 25), the participants were found to be in breach of a settlement agreement for prior similar offences related to proper recording of orders, the whole in breach of their own internal policies and procedures in that regard, all of which led to consent fines and costs totalling $200,000.

135. The Committee is of the view that the two inadvertent and non-systemic transgressions which occurred in this case which were quickly corrected within less than two hours and caused

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no prejudice do not justify the filing of a formal complaint, on the basis of the Latin maxim "de minimis non curat lex", which was explained as follows in the Supreme Court decision of Ontario vs Canadian Pacific Inc., (1995) 2 S.C.R. 1031:

> "In particular, because the legislature is presumed not to have intended to attach penal consequences to trivial or minimal violations of a provision, the absurdity principle allows for the narrowing of the scope of the provision. In this respect, the absurdity principle is closely related to the maxim, **<u>de minimis non curat lex</u>** (the law does not concern itself with trifles). The rationale of this doctrine was explained by Sir William Scott in the case of The "Reward" (1818) 2 Dods. 265, 165 E.R. 1842, at pp. 269-70 and p. 1484:
>
> "The Court is not bound to a strictness at once harsh and pedantic in the application of statutes. The law permits the qualification implied in the ancient maxim **<u>De minimis non curat lex</u>**. – Where there are irregularities of very slight consequence, it does not intend that the infliction of penalties should be inflexibly severe. If the deviation were a mere trifle, which, if continued, in practice, would weigh little or nothing on the public interest, it might properly be overlooked."

136. This principle was again recognized or applied and/or in the following decisions:

a) Minéraux Mart Inc. vs Ministre de l'Environnement, 2021 QCTAQ 09229
b) Chambre de l'assurance des dommages vs Fournier, 2011 CanLII 81637
c) Chambre de la sécurité financière ("CSF") vs Fernandez, 2005 CanLII 108
d) CSF vs Bergeron, CDOO-0522, 25 avril 2005
e) CSF vs Leclerc et al, 2015 QCCDCSF 46
f) Chauvin vs Ducharme, 2007 QCCQ 12455

137. In view of the foregoing, the Committee finds BMONBI not guilty under count 4.

Counts 5 and 6 – Improper Supervision

138. Count 5 alleges that BMONBI was in breach of article 3.100 between March 19 and October 10, 2019, "as it did not establish and maintain a system to supervise the activities of each of its employees and Approved Persons that is reasonably designed to achieve Compliance with the Rules, more specifically as it did not have a surveillance system in place reasonably designed to prevent or detect the trading practice of "front running" by its Approved Persons and employees".

139. Count 6 alleges that BMONBI was in breach of article 3.100 on March 19 and May 31, 2019, as "it did not have a surveillance system in place reasonably designed to prevent or detect violations of" articles 6.114, 6.115, 6.202, 6.205 and 7.3 of the Rules.

140. Article 3.100 of the Rules reads as follows:

> **3.100 Supervision, Surveillance and Compliance**
>
> a) Each approved Participant at the time of its approval and so long as it remains approved, must establish and maintain a system to supervise the activities of each employee, Approved Person and agent of the Approved Participant, that is reasonably designed to achieve compliance with the Regulations of the Bourse and

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with any legislation and regulations applicable to Securities and Derivative Instruments activities. Such a supervisory system must provide, at a minimum, the following:

(i) the establishment, maintenance and enforcement of written policies and procedures acceptable to the Bourse regarding the conduct of the type of business in which it engages and the supervision of each employee, Approved Person and agent of the Approved Participant that are reasonably designed to achieve compliance with the applicable legislation and regulation;

(ii) procedures reasonably designed to ensure that each employee, Approved Person and agent of the Approved Participant understand their responsibilities under the written policies and procedures in subparagraph (i);

(iii) procedures to ensure that the written policies and procedures of the Approved Participant are amended as appropriate within a reasonable time after changes in applicable laws, regulations, Rules and policies and that such changes are communicated to all relevant personnel;

(iv) sufficient personnel and resources to fully and properly enforce the written policies and procedures in paragraph (i);

(v) the designation of supervisory personnel with the necessary qualifications and authority to carry out the supervisory responsibilities assigned to them;

(vi) procedures for follow-up and review to ensure that supervisory personnel are properly executing their supervisory functions; and

(vii) the maintenance of adequate records of supervisory activity, compliance issues identified and the resolution of those issues;

b) Notwithstanding any other provision in the Regulations of the Bourse, each Approved Participant must comply with:

(i) The Electronic Trading Rules, especially regarding risk management and supervisory controls, policies and procedures, the authorization to set or adjust these risk management and supervisory controls, policies and procedures, as well as the use of automated order systems: and

(ii) The requirements of any legislation applicable to the regulation of brokerage and accounts.

141. On September 17, 2017, the Regulatory Division of the Bourse issued guidelines regarding article 3.100 (Tab 21 of the Bourse's Book of Authorities), the stated purpose of which was to "share the underlying principles and questions it considers when assessing the reasonableness of an Approved Participant's supervisory system", the relevant highlights of which may be summarized as follows:

a) a reasonably designed supervisory system is a "best-effort obligation";
b) policies and procedures must be kept up to date;
c) personnel should have sufficient knowledge of the Participant's policies and procedures and be familiar with the Rules of the Bourse;
d) operations and trading activities must be supervised;
e) identified compliance issues must be reviewed and escalated and, when required, investigated;

142. The relevant extract from BMONBI's Trade Floor Supervision Procedures (E-26) regarding front running, provided to the Bourse in late September 2019, which is recited in paragraph 29 of the Summary of Facts, reads as follows:

“**8.1.2 Front Running**

BMO Capital Markets employs logical separation between agency and proprietary businesses to mitigate the potential exposure of customer orders to manipulative trading behaviour. This separation is supplemented by daily transactional reviews.

The purpose of the review is to detect situations where a Firm trader has traded in front of a potentially market moving Client transaction for the benefit of the Firm. In conducting the review, the reviewer should consider the potential for the Firm trader to have prior knowledge of the client order, the size of the client relative to the liquidity of the underlying instrument and the potential of the client order, relative to market conditions, to have an impact on the price of the underlying instrument.”

143. The document (E-26) goes on to specify that potentially market moving transactions include all client transactions within 180 seconds of the Firm trade which are cumulatively equal to or greater than 200 CGB contracts.

144. With regard to the allegations in paragraphs 30 to 38 of the Summary of Facts and discussed above, the evidence established that:

a) BMONBI breached its said policy on both dates by inviting the firm trader (Carelli) to “negotiate the price with (the Client) while he continued to trade for the firm on the same security”, thereby allowing Carelli to have prior knowledge of the Client’s orders;
b) the SMARTS system did not send out any alerts regarding the Impugned Trades on either March 19 or May 31, 2019, because of the inadequate default calibration chosen by BMONBI, which only detected possible front running trades greater than 2% of the daily trading volume in CGBs (E-20, page 61);
c) although BMONBI should have been aware of this deficiency in the SMARTS system on or shortly after March 20, 2019, it did not readjust the calibration until October 10, 2019 to capture all trades in excess of 0.1% of the daily traded value in CGBs, which change in calibration increased sensitivity of the system by a factor of 20 and which Moore admitted was an important change;
d) the PMD system sent out future front trading alerts on both dates, but the TFS associate (Rajiv Menon) who looked into this alert inscribed the note “**Franco for firm and Brad for client - no concern**” on the March 19 Front Running Trade Exception Report (E-28, page 2), having later explained (see para. 28(g) above and E-20, pages 82 and 88) that his adjudication of these alerts was based on his erroneous assumption that Carelli and the agency trader operated from separate desks, such that Carelli did not participate in the chats with Client and therefore had no knowledge of its orders, Menon having admitted that he therefore did not look further into chat and voice records which proved the contrary;
e) there is no evidence that anyone at BMONBI verified Menon’s said analyses of the Impugned Trades in a timely fashion;
f) furthermore, the PMD system only detected 2 of the 200 CGB contracts included in the Impugned Trades of May 31, 2019, which Menon cited as being “very small to move the market” (E-20, page 88), once again minimizing the significance of the Impugned Trades on that date;
g) neither the SMARTS or PMD systems were as robust as the Bourse’s SOLA system, which immediately detected the possibility of front running trades on March 19 and May 31, 2019;

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h) BMONBI's compliance training materials and procedures manual in 2019 still referred in several instances to Rules from 2018 (and in one case to an allegedly outdated 2012 notice from the MX, E-27, page 5), despite the amendments (albeit largely cosmetic in nature) which came into force on January 1, 2019, as appears from (i) Appendix E of BMONBI's Trade Floor Supervision Procedures in 2019 (E-20, page 83 and E-26), (ii) the FQ3-2019 review on front running (July 24, 2019,E-20, page 179) and (iii) the FQ4-2019 review on front running (October 13, 2019, E-20, page 188), although the undated Appendix F compliance materials (E-27) frequently refer to the 2019 version of the Bourse Rules;

145. In paras. 31 to 37 of their Reply, Respondents deny any such breach of article 3.100 on the following grounds:

a) the Client was clearly aware and intended that Carelli and the agency traders were involved in the transactions and the execution of same, with the result that BMONBI's above-cited policy of logical separation of the agency and proprietary trading functions had no application to these trades;
b) the fact that the first line supervisor (Menon), who later left BMONBI to work for the Canadian Investment Regulatory Organization, did not appreciate that there could be circumstances where Carelli (based in Montreal) could communicate directly with the agency trading desk (based in Toronto) is neither relevant nor evidence of a supervisory failure on the part of BMONBI
c) at all times, BMONBI took its supervision responsibilities seriously so as to ensure its first line supervision and compliance programs provided a reasonable assurance of compliance with the Rules;
d) although BMONBI maintains that no violations took place in this case, it nevertheless took this opportunity to conduct additional training for its traders on order sequencing procures and it recalibrated the settings on the SMARTS system for the front running alert;
e) it is inappropriate and contrary to public interest to prosecute an Approved Participant for evaluating, improving and providing guidance regarding its compliance programs on an ongoing basis, which conduct does not constitute an admission that BMONBI's compliance and supervisory program was deficient at the relevant time.

146. Although the above-mentioned guidelines of the Bourse recognize that a reasonably designed supervisory system is a "best-efforts obligation", and the jurisprudence has ruled that such system need not be "perfect", the Committee finds that the number and impact of above-cited significant shortcomings and failings of BMONBI's supervisory system, while not the result of bad faith on its part, fall short of the requirements of article 3.100 of the Rules, for the following reasons:

a) BMONBI's two front running detection systems were deficient and not adequately adapted to detect the Impugned Transactions, although the numbers of contracts involved on both dates were greater than the 200 contract threshold recognized as relevant by BMONBI;
b) it is difficult to explain why BMONBI delayed recalibrating its SMARTS system for almost 7 months after first learning of its inadequacy, thereby demonstrating a lack of timely commitment to the degree of supervision required by the Rules;
c) the supervisory employee in charge of evaluating exception reports was either misinformed or inadequately trained as regards the possibility and regularity of

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interaction and collaboration between the trading desk employees and liquidity providers, which led to his failure to verify telephone call and chat logs regarding the Impugned Transactions;

d) said employee's work and operating assumptions were not adequately supervised or reviewed by his superiors or BMONBI's second line of defence regarding compliance;

e) each of the foregoing factors contributed to the above-described breaches of articles 7.3 and 7.6 of the Rules;

f) BMONBI's explanations in its Reply do not excuse or adequately justify these failings on its part.

147. BMONBI's argument that training courses subsequent to May 31, 2019 somehow mitigated the seriousness of these shortcomings is not relevant to the issue of guilt, although it may be relevant to determining the appropriate sanction.

148. In view of the Committee's above finding regarding count 4, the question (in count 6) as to whether article 6.115 was contravened is moot.

149. For these reasons, the Committee finds BMONBI guilty under counts 5 and 6 of failing to establish and maintain a surveillance system to supervise the activities of each of its employees and Approved Persons that is reasonably designed to achieve Compliance with the Rules, more specifically as it did not have a surveillance system in place reasonably designed to detect (i) the trading practice of front running by its Approved Persons and employees and (ii) violations of articles 6.114, 6.202, 6.205 and 7.3 of the Rules.

Count 7 – Failure to prevent Front Running

150. Count 7 alleges that BMONBI contravened article 3.101 of the Rules on March 19 and May 31, 2019 by failing to ensure that one of its employees and Approved Persons complied with article 7.6 of the Rules regarding front running.

151. Section 3.101 of the Rules reads as follows:

> **3.101 Approved Participant's Supervisory Responsibility**
>
> Each Approved Participant must ensure that all its employees, approved Persons and Designated Representative comply with the provisions of the Regulations of the Bourse.

152. Given our above findings that BMONBI is guilty of (i) front running pursuant to article 7.6 and (ii) failing to establish and maintain a proper supervisory, surveillance and compliance system reasonably designed to achieve compliance with the Rules pursuant to article 3.100, it follows that BMONBI must be found guilty of failing to ensure that its employees and Approved Persons complied with the Rules, as alleged in count 7.

D. CONCLUSIONS

153. In view of the foregoing, the Committee renders the following judgment regarding guilt in this matter:

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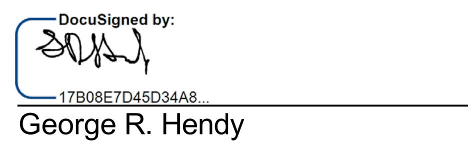
DECLARES Franco Carelli guilty under count 1;

DECLARES BMONBI guilty under counts 1, 2, 3, 5, 6 and 7;

ACQUITS BMONBI under count 4;

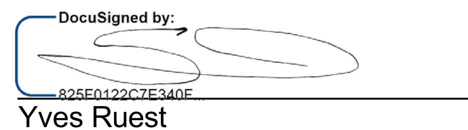
CONVOKES the parties, with the assistance of the Secretary, to a hearing regarding sanctions on a date to be set after consulting all involved.

Montreal, October 29, 2025



George R. Hendy

Élaine Cousineau Phénix



Yves Ruest