Canadian Securities Law News

June 2022
Number 341

LexisNexis

CONFIDENTIALITY OF COMPELLED TESTIMONY IS AFFIRMED BY THE ONTARIO SECURITIES COMMISSION

— Adam D.H. Chisholm and William Burke (Student-at-Law). © McMillan LLP. Reproduced with permission.

Compelled testimony provided to the Ontario Securities Commission attracts certain statutory protections. One of these protections is that the information is confidential. Disclosure of such information is subject to certain requirements under the *Securities Act*.[1]

This regime begs the question as to what happens if Commission Staff disclose compelled information without complying with the Act. Those circumstances led to the motion considered in the Commission decision in *Sharpe (Re)*.[2] Counsel for one of the individual respondents sought an order revoking the investigation order underpinning Commission Staff's examination. The Commission agreed that Commission Staff improperly disclosed information gathered during its investigation, but held that revocation of the investigation order was not an available remedy.

Background

Commission Staff obtained an order under section 11 of the Act to conduct an investigation into Bridging Finance Inc. During the investigation, Commission Staff summoned Bridging's CEO to attend and submit to an examination. This is a common process in securities investigations.

What is less common is what followed. Without an order of the Commission or notice to the CEO, Commission Staff filed the contents of the compelled examination with the Ontario Superior Court of Justice as evidence in support of an application to appoint a receiver over the assets of Bridging.

After obtaining the order, the receiver disclosed the compelled evidence on a website that was linked to by the Commission, effectively revealing the sworn and confidential testimony to the public.

The Commission's disclosure of compelled testimony was not permitted

The Act contains a statutory scheme for collection and use of compelled testimony. Individuals can be summoned and compelled to testify under section 13. Information gained from that testimony cannot be disclosed by any person or company due to section

---

[1] RSO 1990, c S.5 [Act].

[2] 2022 ONSEC 3 [*Sharpe (Re)*].

16 of the Act, which only makes the testimony available "for the exclusive use of the Commission".

Section 17 of the Act allows disclosure in three situations: when the Commission makes an order, when a court with jurisdiction over a prosecution under the *Provincial Offences Act* makes an order or when an investigator (Commission Staff) makes disclosure in connection with an existing or contemplated proceeding before the Commission.

Even when disclosure is permitted under section 17, notice must be given to the individual who provided the evidence and the order must be in the public's interest. Further, the disclosure must only be ordered to the extent it is required for the Commission to carry out its mandate.[3]

In *Sharpe (Re)*, no section 17 order was obtained. The Commission rejected Commission Staff's argument that the Commission was permitted by the Act to freely decide how to use the testimony. The Commission noted that the powers of the Commission Tribunal and Commission Staff are distinct – only the Commission Tribunal possesses the power to make a disclosure order. Commission Staff cannot rely on its executive function to skip this step.[4] Further, bypassing the Commission Tribunal took away a necessary opportunity for the Commission to review and limit the extent of disclosure made by Commission Staff.[5]

In assessing Commission Staff's ability to disclose compelled testimony, the Commission considered the balance between the "extraordinary" power of Commission Staff to compel testimony and its consequential obligation to maintain the privacy of individuals providing this testimony.[6]

Finding that disclosure was not available to the Commission Staff, the Commission turned its attention to whether its actions were consistent with the CEO's expectations and whether the disclosure was only to the extent necessary. For both issues, the answer was no. The reasonable expectation of a compelled witness was that Commission Staff would act only as it is required to under the Act.[7] Further, there was no valid excuse for Commission Staff's failure to obtain a sealing order to limit disclosure in the court proceeding.[8]

Revoking an investigation order is not an available remedy for the improper disclosure

Despite the CEO's right to the privacy of his testimony being infringed, the Commission did not go as far as revoking the underlying investigation order. The Commission rejected the CEO's argument that the disclosure was a fact that, if known, would have changed the decision to issue the investigation order, as the decision to issue the investigation order and the later decision to disclose the testimony were both made by Commission Staff.[9] There was also not a sufficient connection between the investigation order and the inappropriate disclosure to support crafting a remedy of this nature, as revoking the investigation order would have no effect on restraining the already public disclosure of the testimony and would not be in the public's interest.[10]

The Commission held that revocation of the section 11 investigation order would not in any way reverse the public disclosure of the compelled evidence; nor would revocation offer any other relief, other than perhaps greater vindication or similar satisfaction. It could also involve punishment. These were insufficient reasons to invoke the Commission's rarely-used authority to revoke the order.[11]

---

[3] *Deloitte & Touche LLP v Ontario (Securities Commission)*, 2003 SCC 61.

[4] *Sharpe (Re)* at para 65.

[5] *Sharpe (Re)* at para 68.

[6] *Sharpe (Re)* at para 50.

[7] *Sharpe (Re)* at para 115.

[8] *Sharpe (Re)* at para 129.

[9] *Sharpe (Re)* at para 142.

[10] *Sharpe (Re)* at paras 150, 164.

[11] *Sharpe (Re)* at para 150.

The Commission did not entirely close the door to revoking an investigation order in future cases, concluding that situations could arise that would justify departing from established precedent to apply this remedy.[12] Specifically, section 144 of the Act permits revocation of a section 11 order.[13] It is clear this will be done rarely.[14]

Conclusion

This decision is important for both Commission Staff and parties under investigation for securities offences, as it reaffirms the statutory protections available for compelled evidence.

The power of Commission Staff to compel testimony during an investigation is, as recognized by the Commission in *Sharpe (Re)*, "extraordinary".[15] To balance this, the Act contains provisions intended to ensure that testimony remains confidential outside of specific exceptions. Here, the Commission recognized that Commission Staff overstepped their statutory abilities by freely disclosing testimony, providing an important caution about Commission Staff's use of compelled testimony in future cases.

It remains to be seen what remedy may flow from Commission Staff's disclosure in *Sharpe (Re)*. Certainly the decision may be raised by counsel about any subsequent attempted use of the testimony – perhaps in a civil context, for pending or future claims against the respondents named in the Commission proceeding. That may not be an insignificant use. Many counsel whose clients are examined by Commission Staff through compulsion will claim protections related to the uses of the information given.

But what of matters before the Commission itself? The Bridging case continues to work its way through the Commission and it will be interesting to see what role, if any, this wrongful disclosure may play in adjudication of the merits of the allegations.

Adam Chisholm is an experienced capital markets and intellectual property litigation lawyer at McMillan LLP who frequently appears in front of the Capital Markets Tribunal (formerly the Ontario Securities Commission).

William Burke is a student-at-law with McMillan LLP, with a strong background in technology and advocacy. He will applying his skills when he returns as an associate in McMillan's Capital Markets group this fall.

CSA SEEKS COMMENTS ON "ACCESS EQUALS DELIVERY" MODEL FOR PROSPECTUSES, FINANCIAL STATEMENTS AND MD&A

— Bruce Hibbard, John Piasta, Andrew Disipio, and Jason Wang. © Bennett Jones LLP. Reproduced with permission.

The Canadian Securities Administrators (CSA) have published for comment proposed amendments to implement an "access equals delivery" model (AED model) to generally permit electronic delivery of prospectuses, financial statements and related management discussion and analysis (MD&A) for non-investment fund reporting issuers. These proposed amendments are subject to a 90-day comment period ending on July 6, 2022.

Canadian securities legislation currently requires reporting issuers to physically deliver various documents to investors, including but not limited to, prospectuses, financial statements, MD&A and proxy-related materials. Although electronic delivery is already permitted in some respects, and despite the prior introduction of a notice-and-access regime for proxy-related materials relating to shareholders' meetings, many issuers continue to incur significant costs for printing and mailing the documents required to be delivered under securities laws.

---

[12] *Sharpe (Re)* at para 162.

[13] *Sharpe (Re)* at para 136.

[14] The Commission cited another example of a request to revoke an investigation order, *X Corp.*, 2004 ONSEC 19. As in *Sharpe (Re)*, the remedy was not granted.

[15] *Sharpe (Re)* at para 50.

Summary of the Proposed AED Model

The CSA's proposed amendments would implement an AED model for prospectuses, annual financial statements, interim financial reports and related MD&A for non-investment fund reporting issuers. The objective of "access equals delivery" is to modernize the way documents are made available to investors while reducing costs to issuers associated with printing and mailing. The proposed AED model contemplates the following:

- in all jurisdictions in Canada except British Columbia, providing public electronic access to a document and alerting investors that the document is available will constitute delivery for prospectuses under applicable securities legislation;
- in British Columbia, an exemption from the requirement under securities legislation to send a prospectus will permit access instead of delivery is intended to achieve the same outcome as implementing the model in other jurisdictions;
- for annual financial statements, interim financial reports and related MD&A, providing public electronic access to the documents and alerting investors that the documents are available, via news release, will constitute delivery for the documents; and
- in all cases, delivery of a document will occur, or the conditions in the BC exemption will be met, when:
  - the document is filed on the System for Electronic Document Analysis and Retrieval (SEDAR) and, where applicable, a news release is disseminated on the same day and filed on SEDAR indicating that the document is available electronically and that a paper or an electronic copy can be obtained upon request.

The proposed AED model would not limit an investor's ability to request documents via paper copy or an issuer's ability to deliver financial statements and related MD&A based on an investor's standing instructions.

At this time, the CSA is not proposing the AED model for the delivery of documents that require immediate shareholder action and participation, such as proxy-related materials for shareholders' meetings and take-over bid and issuer bid circulars.

Purpose of the Proposed AED Model

The purpose of the proposed AED model is to modernize the way documents are made available to investors while reducing costs for issuers associated with printing and mailing such documents. The proposed AED model is intended to provide a timely, cost-efficient and environmentally-friendly method to communicate information to investors. The CSA believes that the proposed AED model will reduce the regulatory burden on issuers without compromising investor protection, while recognizing that information technology is an important and useful tool to facilitate communication with investors.

The proposed AED model is intended to be beneficial for both reporting issuers and investors alike as it facilitates the communication of information by enabling issuers to reach investors in a faster and more effective manner, as opposed to mailing documents. SEDAR is a widely-utilized platform, free of charge, that allows investors to access and search for information with ease and convenience.

Interplay of the AED Model with Corporate Law Requirements

Issuers should be aware that even if the proposed AED Model is adopted by the CSA, other corporate laws and regulations will continue to apply, some of which will continue to contain specific delivery requirements, including those set forth in the *Business Corporations Act* (Alberta) (ABCA) and the *Canada Business Corporations Act* (CBCA). Similarly, the proposed AED model would not limit an investor's ability to request documents via paper copy or an issuer's ability to deliver financial statements and related MD&A via paper copy.

For example, section 159 of the CBCA requires issuers existing under the CBCA to send annual financial statements to each registered shareholder, unless such shareholder has previously requested not to receive such materials. Notwithstanding this requirement, section 156 of the CBCA additionally allows for applications to be made to exempt an issuer from such delivery requirement. As such, issuers incorporated under the CBCA who wish to rely upon the proposed AED model and cease delivery of physical financial statements may wish to consider making such an application.

A similar delivery requirement exists, for example, for issuers existing under the ABCA. Under the ABCA, however, there is no general equivalent to section 156 of the CBCA to allow for applications to exempt an issuer from such delivery requirement.

Impact on Public Offerings

The proposed AED model applies to all types of prospectuses, except rights offerings by way of prospectus and medium-term note programs and other continuous distributions under a shelf prospectus. The proposed AED model would also not apply to prospectus offerings of investment fund securities.

Under the proposed AED model, access to the final prospectus or any amendment is deemed to have been provided if the issuer has filed the document on SEDAR and been issued a receipt, and the issuer has issued and filed a news release on SEDAR announcing that the document is available and accessible on SEDAR and containing certain additional specified disclosure.

Under the proposed AED model, the right to withdraw from an agreement to purchase securities may be exercised within two business days after the later of: (i) the date that access to the final prospectus or any amendment has been provided; and (ii) the date that the purchaser has entered into the agreement to purchase the securities. In order to rely upon the proposed AED model in connection with a prospectus offering, the prospectus would need to contain an additional cross-reference on the front page of the prospectus to alert investors to the section explaining how this withdrawal period is calculated is also required.

The proposed AED model will additionally have an impact on road shows, underwriting agreements and marketing materials as new disclosure requirements relating to any such marketing materials and road shows are required by the proposal.

Practical Applications and General Commentary

Certain investor advocates have long resisted a shift to "access equals delivery", citing concerns over shareholder disenfranchisement and a reduction shareholder engagement. However, the proposed AED model, if adopted, would bring Canada in line with the current rules and practices of other major securities markets, such as the United States and recognizes the continuing evolution towards consumption of information electronically. Notably, from an issuer's perspective, the proposed AED model would reduce costs and regulatory burdens, even though physical printing and delivery of some materials will likely still be required in order to comply with the issuer's applicable corporate statutory requirements. From an investor's and market participant's perspective, the proposed AED model provides timely and efficient access to information through SEDAR.

If the proposed AED model is implemented, issuers and their financial advisors and underwriters would be well-advised to consider what changes may be required, or beneficial, for their standard shareholder communications, road show and underwriting practices.

For further details, please see the CSA notice for the proposed amendments.

Bruce Hibbard practises corporate and securities law, with a particular emphasis on M&A, public and private capital markets offerings, investment funds and corporate/commercial issues. He acts for a diverse group of clients, including both public and private entities, mutual funds, hedge funds, private equity funds, venture capital funds, investment banks and exempt market dealers.

John Piasta's practice focuses on public and private M&A transactions, capital markets transactions, including cross-border financings, and governance and securities law compliance matters for public and private entities.

Andrew Disipio practices securities and corporate law with a focus on M&A and capital markets transactions. He represents a broad range of clients, including issuers and investment dealers, in connection with public and private financings, takeover bids, plans of arrangement and restructurings.

Jason Wang has a corporate and securities law practice with a focus on M&A, corporate finance and capital market transactions. His experience includes acting for issuers and underwriters in securities offerings, companies in M&A transactions including plans of arrangement and advising clients on corporate governance and continuous disclosure requirements.

CANADIAN SECURITIES ADMINISTRATORS

CSA Staff Notice 25-303

CSA Staff Notice 25-303 *2021 CSA Annual Activities Report on the Oversight of Self-Regulatory Organizations and Investor Protection Funds*, dated April 28, 2022, was issued. For more information, please see CSA Staff Notice 25-303, which will be reproduced in Volume 1 of the *Canadian Securities Law Reporter* at ¶2533.

Companion Policy 41-101CP

Companion Policy 41-101CP *General Prospectus Requirements* was amended on April 14, 2022. For more information, please see National Instrument 41-101CP, which will be reproduced in Volume 1A of the *Canadian Securities Law Reporter* at ¶4101d.

Companion Policy 51-102CP

Companion Policy 51-102CP *Continuous Disclosure Obligations* was amended on April 14, 2022. For more information, please see Companion Policy 51-102CP, which will be reproduced in Volume 1B of the *Canadian Securities Law Reporter* at ¶5102i.

PROVINCIAL UPDATES

Alberta

Blanket Order 13-503

Blanket Order 13-503 *Temporary Exemption from Requirements to Manually Sign Documents* was amended on April 26, 2022. For more information, please see Blanket Order 13-503, which will be reproduced in Volume 2 of the *Canadian Securities Law Reporter* at ¶174-100a.

Ontario

Securities Act

The *Securities Act* was amended by S.O. 2021, c. 8, Sched. 9, effective April 29, 2022. For more information, please see the *Securities Act*, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶450-001.

Securities Commission Act, 2021

The *Securities Commission Act, 2021*, S.O. 2021, c. 8, Sched. 9, was proclaimed in force effective April 29, 2022. For more information, please see the *Securities Commission Act, 2021*, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶467-001.

Transitional Matters Regulation

The *Transitional Matters Regulation* (under the *Securities Commission Act, 2021*), O. Reg. 43/22, dated April 29, 2022, was issued. For more information, please see the *Transitional Matters Regulation, 2021*, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶468-001.

OSC Rule 11-501

OSC Rule 11-501 *Electronic Delivery of Documents to the Ontario Securities Commission* was amended on April 29, 2022. For more information, please see OSC Rule 11-501, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶479-801.

OSC Policy 11-601

OSC Policy 11-601 *The Securities Advisory Committee to the OSC* was amended on April 29, 2022. For more information, please see OSC Policy 11-601, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶480-671.

OSC Staff Notice 11-722

OSC Staff Notice 11-722 *Recommendations of the Committee on Staff Communications* was withdrawn on April 29, 2022. For more information, please see OSC Staff Notice 11-722, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶490-122.

OSC Staff Notice 11-795

OSC Staff Notice 11-795 *Notice of Withdrawal of Ontario Securities Commission Staff Notices*, dated April 28, 2022, was issued. For more information, please see OSC Staff Notice 11-795, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶490-129an.

OSC Rule 14-501

OSC Rule 14-501 *Definitions* was amended on April 29, 2022. For more information, please see OSC Rule 14-501, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶480-021.

OSC Policy 15-601

OSC Policy 15-601 *Whistleblower Program* was amended on April 29, 2022. For more information, please see OSC Policy 15-601, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶480-731.

OSC Staff Notice 15-701

OSC Staff Notice 15-701 *Meetings with a Commissioner Regarding a Prospectus or an Application for Exemption or Registration* was withdrawn on April 29, 2022. For more information, please see OSC Staff Notice 15-701, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶490-151.

OSC Policy 51-601

OSC Policy 51-601 *Reporting Issuer Defaults* was amended on April 29, 2022. For more information, please see OSC Policy 51-601, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶480-822.

Companion Policy 91-507CP

Companion Policy 91-507CP *Trade Repositories and Derivatives Data Reporting* was amended on April 29, 2022. For more information, please see Companion Policy 51-601, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶480-857.

RECENT CASES

Sanctions and Costs

British Columbia Securities Commission, February 22, 2022

Arian Resources Corp. ("Arian") was a reporting issuer in British Columbia in the mineral exploration business, and its shares were listed on the TSX Venture Exchange. During the relevant period, Zahir "Zip" Sadrudin Dhanani ("Dhanani") and Robert James Naso ("Naso", together with Dhanani and Arian, the "Respondents") were directors of Arian, and CEO and CFO, respectively. In a decision dated October 5, 2021, a Panel of the British Columbia Securities Commission (the "Commission") found that the Respondents breached the British Columbia *Securities Act*, RSBC 1996, c. 418 (the "Act"), by failing to disclose material changes contrary to section 85 of the Act and making misleading statements in its public filings contrary to subsection 168.1(1) of the Act. In brief, the Respondents: mischaracterized payments to a promotor that failed to perform services and did not return the funds, and payment to Dhanani's mother; failed to accurately report on the status of Arian's primary project, in particular that it was in jeopardy; and failed to accurately report on executive compensation. It was also found that Dhanani and Naso authorized Arian's contraventions and thereby contravened the same provisions of the Act pursuant to 168.2 of the Act (the "Liability Decision"; see 2021 CSLR ¶900-901). The Executive Director of the Commission sought various sanctions, including that: Dhanani and Naso be permanently banned from participating in the market; Arian be permanently prohibited from trading or purchasing securities; and Dhanani and Naso pay administrating penalties of $200,000 each.

Various sanctions were ordered. The Panel began its analysis by noting that, from *Re Eron Mortgage Corporation et al.*, [2000] 7 BCSC Weekly Summary, the non-exhaustive factors to consider when making public interest orders included: the seriousness of the respondent's conduct; the respondent's enrichment and harm suffered by the market and investors; the respondent's past conduct; mitigating and aggravating factors; the respondent's fitness to be a registrant, director, officer, or advisor to issuers; the need for specific and general deterrence; and orders made in similar circumstances. Key findings by the Panel included that: the conduct at issue was serious, as the loss of the funds to the promotor and inability to secure Arian's only material asset were crucial pieces of information to an investor that were not provided until well after they occurred, thus depriving them of information that would permit them to make informed decisions; Arian caused risks of financial loss to investors and damaged the integrity of the market; Dhanani and Naso established they were unfit to act as directors and presented risks to the market if they were to participate; aggravating factors included that Dhanani and Naso were aware of their obligations for timely and accurate disclosure but repeatedly failed to fulfil their responsibilities; and there was a need for specific and general deterrence. The Panel reviewed two other cases where issuers made inaccurate or untimely disclosures (see *Re Mountainstar Gold Inc.*, 2019 CSLR ¶900-782, and *Re Ironside*, 2007 CSLR ¶900-232), and, in both cases, the directors were subject to permanent market participation bans and required to pay administrative penalties. The Panel concluded that, based on its findings and the prior decisions, it was in the public interest to permanently prohibit Dhanani and Naso from participating in the market in any capacity, and to order them to pay administrative penalties of $200,000 each. Arian was also permanently prohibited from trading in or acquiring securities.

Arian Resources Corp. (Re), 2022 CSLR ¶900-921

Fraud

Ontario Securities Commission, March 28, 2022

Solar Income Fund Inc. ("SIF Inc.") was a small private company in the business of developing and managing solar power generation installations. Allan Grossman ("Grossman") and Paul Ghezzi were SIF Inc.'s founders. SIF Inc. had established various funds, including SIF Solar Energy Income & Growth Fund ("SIF #1") and Solar Income and Growth Fund #2 (SIF #2"), which paid SIF Inc. to provide consulting, development, and management services. The two funds raised money from the public by selling fund units through exempt market dealers based on offering memoranda and amendments. Decision making for SIF Inc. was done through a management committee which was composed of senior personnel. Only the management committee members could authorize movements of funds through SIF Inc.-related accounts, and they all had access to the bank accounts of the entities that SIF Inc. managed. In June 2014, Charles Mazzacato ("Mazzacato") became a director of SIF Inc. and then became President in summer 2015; he was a SIF Inc. shareholder and on the management committee until November 2017. Kenneth Kadonoff ("Kadonoff"; together with Mazzacato, Grossman, and SIF Inc., the "Respondents") was a lawyer who began working with SIF Inc. in 2010 and later became an indirect shareholder. Kadonoff was part of the management committee until his formal resignation as a director and officer in August 2015. SIF #1's offering memorandum (the "Memorandum") was originally issued on March 6, 2013, and it stated, among other things, that SIF #1 "was established to invest in Subsidiaries which will in turn invest in the acquisition, development, financing and operation of solar energy power installations... and other ancillary or incidental business activities". Staff of the Ontario Securities Commission (the "Commission") provided evidence that, during the summer of 2015 to May 2016: SIF #1 transferred funds to SIF #2, and this was the majority of all external funds received by SIF #2;

and SIF #2 paid at least $223,224.04 to investors as distributions and paid $11,640 for dealer fees. Commission Staff alleged that the Respondents breached: subsection 44(2) of the Ontario *Securities Act*, RSO 1990, c. S.5, (the "Act"), which prohibits false or misleading representations that an investor would consider in deciding whether to maintain or enter into a trading or advising relationship with the person or company that made the representation; and subsection 126.1(1)(*b*) of the Act, which prohibits fraudulent conduct related to securities. The Respondents took the position that the loan from SIF #1 to SIF #2 was authorized, and if the Commission found otherwise, the Respondents had relied on legal advice.

The Respondents were found to have engaged in fraud. The Panel began by dismissing the allegation of a breach of subsection 44(2) of the Act, finding, among other things, that: read in context, the relationship envisioned by subsection 44(2) was between registrants and investors; the SIF #1 unitholders were not in a trading relationship with SIF Inc., as SIF Inc. merely provided information and administrative work, and it was exempt market dealers who interacted with the unitholders; and to apply subsection 44(2) in this case would depart from caselaw and was not warranted on policy grounds, as it could create liability for every issuer involved in a single trade with an investor when other remedies were available. Turning to the allegation of fraud, the Panel began by noting that: to establish fraud under subsection 126.1(1)(*b*) of the Act, Staff must establish that the respondent directly or indirectly engaged in conduct relating to securities and knew or reasonably ought to have known the conduct perpetuated a fraud; the elements of fraud to be established were the wrongful act (i.e., an act of deceit, falsehood, or some other fraudulent means) and the risk of or actual deprivation caused by that act, and subjective knowledge of the wrongful act and the risk of deprivation; a corporation's "knowledge" can be established where the directing minds "knew or ought reasonably to have known that the corporation perpetrated a fraud"; "other fraudulent means" included unauthorized diversions of funds, and caselaw had established the principle that "the use of funds that is inconsistent with what was promised to investors and that is without notice to them is dishonest"; and, where the allegation was of a dishonest act, Staff did not need to demonstrate that the respondent regarded the act as dishonest, as it was proven where the respondent knowingly undertook the act, as was subjective awareness of the risk of deprivation. It was not disputed that the impugned conduct involved securities or that SIF #2 used funds to pay the distributions and dealer fees. The first issue was whether the payments were authorized, and the Panel found, among other things, that in reviewing the language of the offering memorandum and testimony, SIF #1 was not permitted to make loans, and if the Panel was wrong on that interpretation, it was not authorized to make loans for the payment of distributions or dealer fees but only for financing solar power installations. Having found an unauthorized diversion, the Panel then found that the diversion created a risk of prejudice to the investors' funds, as they "unwittingly took on risks they did not bargain for", and it was irrelevant whether the risks would turn out to be neutral, beneficial, or detrimental. Turning to the *mens rea* element, the Panel reviewed the evidence and found that, as he authorized the transfer of funds for unauthorized purposes, Grossman was subjectively aware of the fraudulent act. As Grossman was a directing mind of SIF Inc., the company was deemed to have also had subjective knowledge. In the cases of Mazzacato and Kadonoff, the Panel found that, given their positions as former presidents, they likely were or at least should have been aware of the fraudulent acts and were reckless in that regard. Having found the Respondents had knowledge of the unauthorized act, it followed that the Respondents had subjective awareness of the risk of prejudice to the investors' funds. Finally, the Panel considered whether the defence of reasonable reliance on legal advice was available to the Respondents. Among other things, the Respondents had to establish that they made sufficient enquiries and relied on the advice, with reliance demonstrated by showing "that the advice was sufficiently clear, specific and connected to the impugned act, by addressing the question raised by that impugned act" (see *Re CTC Crown Technologies* (1998), 8 ASCS 1940). In finding that the defence was unavailable, the Panel noted, among other things that: the evidence was that the Respondents' counsel gave advice based on their reading of the trust documents, not the offering memorandum; the question of whether loans were permitted to pay distributions and dealer fees was never directly asked of the counsel; and all of the individual Respondents received communications from counsel but none of them formed an independent view or asked questions. Sanctions would be determined at a later date.

Solar Income Fund Inc. (Re), 2022 CSLR ¶900-922

Jurisdiction

Québec Court of Appeal, February 23, 2022

Volkswagen Aktiengesellschaft ("VW" or the "Respondent") was a German corporation with no domicile in Québec; its shares only traded on the Over-the-Counter ("OTC") markets and the Frankfurt Stock Exchange. Lawrence Chandler (the

"Appellant") had purchased VW's sponsored unlisted American Depositary Receipts ("ADR") listed on the OTC. On September 18, 2015, VW admitted to cheating on American emissions tests, and the Appellant commenced a class action lawsuit again VW on behalf of Québec residents who purchased VW securities (including the ADRs, shares, and credit notes, which were issued by a VW subsidiary) between March 12, 2009 (the date of VW's 2008 Annual report that allegedly did not disclose the cheating) and September 18, 2015 (when the cheating was disclosed to the public) and held all or some of their VW securities until after that date. The proposed action was made pursuant to Article 1457 of the *Civil Code of Québec*, CQLR, c. CCQ-1991 (the "CCQ"). The Appellant claimed the class members suffered monetary damage when the value of their VW securities dropped after the disclosure of the intentional misrepresentations about VW's vehicles' emissions standards. Similar actions had also been commenced in the United States and Germany. The Respondent applied to the Québec Superior Court (the "QSC") for a declinatory exception arguing that the Québec courts did not have jurisdiction over the proceedings, as none of the connecting factors creating jurisdiction enumerated in Article 3148 of the CCQ were established. The Respondent also argued that Québec was the *forum non conveniens* and the German or United States courts were in a better position to resolve the matter. The QSC judge allowed the application (see 2020 CSLR ¶900-830). The QSC judge applied the principles in *Club Resorts Ltd. v. Van Breda*, 2012 SCC 17, reviewed the connecting factors in Article 3148 of the CCQ, and found, among other things, that: the Respondent had not attorned to Québec's jurisdiction when it did not raise jurisdiction at the authorization stage of the proceedings; the connecting factors to establish jurisdiction were not met, as the Respondent had no establishment in Québec, nor did it carry on activity in Québec with all of its key activities taking place in Germany, and the alleged economic injury occurred where the investors purchased and sold the ADRs which was in the United States and Germany; and section 236.1 of the Québec *Securities Act*, CQLR, c. V-1.1 (the "QSA") did not apply to grant jurisdiction, as the matter did not relate to the distribution of securities. The Court also found that if it had jurisdiction, it would not have concluded that Québec was *forum non conveniens*. The Appellant appealed to the Québec Court of Appeal (the "Court") alleging that the QSC judge erred in law.

The appeal was dismissed. The issues before the Court were whether the QSC judge erred concluding that: (1) VW did not attorn to the jurisdiction of Québec; (2) no injury was suffered in Québec; (3) the fault was not committed in Québec; (4) there was no jurisdiction established under section 236.1 of the QSA; and (5) Québec was not *forum non conveniens*. On the first issue, the Appellant had argued that the Respondent had attorned to Québec's jurisdiction when it waived its right to raise the issue of jurisdiction at the authorization stage of the proceedings. The Court found the QSC judge correctly applied the principle in *Infineon Technologies AG v. Option consommateurs,* 2013 SCC 59 ("*Infineon*"), which was that "the determination of jurisdiction at the authorization stage is not *res judicata* and that the issue of territorial jurisdiction can be raised again on the merits". Further, the Respondent had expressly stated it would contest jurisdiction once the originating application was issued. On the second issue, the Court found, among other things, that the QSC judge was correct in her application of *Infineon*, which provided that the site of the economic injury was where it was "substantially suffered" and not merely recorded. In this case, the substantial damage was where the securities were purchased (in Germany and the United States) and merely recorded in Québec; the contracts for the purchases of those securities were entered into abroad, through non-Canadian brokers. The QSC judge was also correct in finding that the fact that the notes were issued in Québec was not enough to establish jurisdiction over all the transactions. On the third issue, the Court again determined there were no reviewable errors made by the QSC judge, finding, among other things, that the mere fact that the Respondent's prospectus was available in Québec was insufficient to conclude a fault was committed there. The prospectus was prepared in Germany and there was no evidence it was specifically sent to Québec investors. On the fourth issue, the Court noted that section 236.1 of the QSA grants jurisdiction to the Québec courts where Québec investors acquire securities through a distribution. The Court found that the QSC judge was correct in finding the section did not apply, as the matter did not relate to the distribution of securities, with the notes having been issued by VW's subsidiary, and VW did not distribute the shares or ADRs in Québec. Having confirmed there was no jurisdiction for Québec courts to hear the matter, the Court did not need to address the issue of *forum non conveniens*.

Chandler v. Volkswagen Aktiengesellschaft, 2022 CSLR ¶900-923

Sanctions and Costs

British Columbia Securities Commission, March 21, 2022

Robert Waters (the "Applicant") was a registered investment advisor in British Columbia whose registration ceased in September 1998. In a decision dated June 5, 2014, a Panel of the British Columbia Securities Commission (the

"Commission") found the Applicant had contravened subsections 34(*a*) and 61(1) of the British Columbia *Securities Act*, RSBC 1996, c. 418 (the "Act"), by trading and distributing securities of Berkeley Coffee & Tea, Inc. ("Berkeley") without being registered and without filing a prospectus (see 2014 BCSECCOM 215). In a sanctions decision dated September 2, 2014 (see 2014 BCSECCOM 369; the "Sanctions Decision"), the Panel found, among other things, that: the Applicant engaged in serious misconduct, as he deprived investors of the Act's protections and damaged the market's integrity; the Applicant's conduct fell short of that expected of a former registrant; Berkeley was misled about the Applicant's relationship with some of the investors he solicited and claimed prospectus exemptions for which Berkeley was ineligible; and the Applicant posed a risk to the market. Accordingly, the Panel ordered that the Applicant: resign any positions held as a director or officer; pay an administrative penalty of $20,000; and be prohibited from participating in the market, including acting as a promotor or engaging in investor relations activity until the later of September 4, 2020, full payment of the administrative penalty, or the completion of a course about capital raising in British Columbia. The Applicant subsequently completed the required course but had not yet repaid any amount of the penalty. The Applicant requested that the Sanctions Decision be varied to reduce the administrative penalty and allow him to do investor relations work. The Applicant argued that he had new and compelling evidence and changed circumstances.

The application was dismissed. The Panel began its analysis by noting, among other things, that: section 171 of the Act provides that the Commission can vary or revoke a decision if doing so would not be prejudicial to the public interest; section 9.10 of BC Policy 15-601 *Hearings* provides that a decision can be revoked or varied if there is new and compelling evidence that was not before the original decision maker or there was a significant change in circumstances since the decision was rendered; and, in *Re Deyrmenjian*, 2019 CSLR ¶900-777, the Commission held that it was key for the evidence to be compelling (i.e., the evidence would have led to a different result if available to the original adjudicator), otherwise a revocation or variation would be contrary to the public interest. The new and compelling evidence offered by the Applicant included that: in an offering that was similar and took place prior to Berkeley's, an investigation was undertaken by the Commission but attracted no proceedings, which was why the Applicant proceeded as he did and was of the view that the sanctions in Berkeley contradicted the "precedent" of the earlier case; the Applicant had contacted the Commission to ask if a prospectus was required for the Berkeley offering and was only advised to obtain legal advice; and the Applicant claimed he was unable to find employment and had little income since the Sanctions Decision was rendered. The Panel's key findings included that: the prior offering and contact with the Commission was not new evidence (as it was available during the liability hearing) nor was it compelling; the Commission's prior decision not to proceed with enforcement actions did not negate the need to ensure compliance in the Berkeley offering; the Applicant's position that he could proceed given the "precedent" contradicted his subsequent contact with the Commission to seek advice and again he failed to engage in the required due diligence; the evidence provided by the Applicant did not address the findings of lack of truthfulness in the Sanctions Decision; and the Applicant did not provide complete financial information to support his claim of impecuniosity or what actual attempts were made for gainful employment. Ultimately, in dismissing the Application, the Panel was influenced by the Applicant not having made any attempts to pay any portion of the administrative penalty and continuing to blame others for his misconduct, demonstrating that a variation of the order would be contrary to the public interest.

Waters (Re), 2022 CSLR ¶900-924

CANADIAN SECURITIES LAW NEWS

Published monthly as the newsletter complement to the *Canadian Securities Law Reporter* and the *Canadian Stock Exchanges Manual* by LexisNexis Canada Inc. For subscription information, contact your Account Manager or call 1-800-387-0899.

For LexisNexis Canada Inc.

Jaime Latner, LLB,
Content Development Associate
905-479-2665
jaime.latner@lexisnexis.ca

Customer Support
1-800-387-0899
service@lexisnexis.ca
Customer Service is available from 7 a.m. to 11 p.m. (ET) Monday to Friday, and from 9 a.m. to 11 p.m. (ET) on Weekends.

LexisNexis Canada Inc.
111 Gordon Baker Road
Suite 900
Toronto, Ontario
M2H 3R1