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Canadian Securities Administrators . . . 6

Provincial Updates 7

Recent Cases 7

ISSUERS' DISCLOSURE IN UNCERTAIN TIMES: CANADIAN SECURITIES REGULATORS' REVIEW OF PUBLIC DISCLOSURE

— *By Oleg Stratiev.*[1]

"It was the best of times, it was the worst of times," said Charles Dickens in "A Tale of Two Cities", accurately describing what it was like living and working through a pandemic, protests and unrest in 1859. Almost 200 years later, the quote could still be relevant to describe public issuers' experience navigating through Covid-19.

But, regardless of one's view of the last two years, it is undoubtfully the most uncertain of times. Whether accounting for Covid-19 affecting businesses and supply chains worldwide, the rising interest rates and currency fluctuations impacting the monetary systems, or the conflict in Ukraine, the issuers are preparing disclosure in evolving and uncertain times, resulting in increased estimation uncertainty and a risk that financial statements may materially change in the near term.

On November 3, 2022, the Canadian Securities Administration ("**CSA**") issued Staff Notice 51-364 (the "**Staff Notice**") to report the common deficiencies noted over the past two years concerning issuers' financial reporting and other disclosures. CSA examined the filings of 466 issuers and included a review of issuers' financial statements, management's discussion and analysis, and other documents.

Takeaways from the CSA's Staff Notice

The CSA was generally satisfied by the quality of disclosure provided by many issuers who have significantly bolstered and expanded the disclosure in their financial statements, annual reports and MD&As.

However, the Staff Notice underlined that certain deficiencies persisted over the last two years, namely:

- ***Financial Statements***: Issuers failed to properly recognize, measure, present, classify and disclose specific IFRS requirements, such as revenue recognition, disclosure of expected credit losses, business combinations *et al*.
- ***MD&As:*** Issuers improperly disclosed forward-looking information, discussions of operations, non-GAAP and other financial measures, and failed to update non-applicable disclosures.

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LexisNexis

- ***Other Regulatory Requirements:*** CSA noted that certain issuers engaged in “greenwashing" by including overly-promotional language in their disclosure about ESG matters, while others failed to provide sufficient disclosure in reverse takeover transactions or comply with regulatory matters concerning audit committee requirements.

The issues above are discussed in greater detail below. The “*Financial Statements Deficiencies*” section will be of most use to professionals in the accounting and financial industries, while the “*MD&A Deficiencies*” and “*Other Regulatory Disclosure Deficiencies*” will be most useful to external legal counsels and in-house legal departments.

Financial Statements Deficiencies

A. Variable Consideration

Variable consideration is defined broadly and takes many forms, such as price concessions, rebates or refunds. Consideration could also be “variable” if the amount an issuer will receive is contingent on a future event occurring or not occurring, even though the amount itself is fixed.

When analyzing the disclosure of variable consideration, the CSA invites issuers to consider whether the consideration promised in a contract includes a variable amount. If so, issuers are encouraged to further consider whether there are valid expectancies of some price concession, such as through customary business practices, published policies or specific statements an issuer has made, leading to a variable consideration component or contract.

If the consideration is considered variable, issuers should discuss whether the consideration is accurate or could, ultimately, be different. To do so, the CSA invites issuers to disclose information about the methods, inputs and assumptions used for determining the consideration, including the extent of possible variation from the expected amount. Finally, once said consideration is received, the CSA encourages issuers to update, at the end of the reporting period, the price previously provided.

Moreover, issuers could include estimated variable consideration, but only if it is highly probable that a significant reversal of cumulative revenue recognized will **not** occur.

B. Credit Risk

Throughout its review, the CSA noted that several issuers did not disclose sufficient information regarding the effect of their credit risk or the amount, timing and uncertainty regarding future cash flow.

To correct this deficiency, the CSA invites issuers to determine the specific disclosures that are relevant to the issuers’ businesses, namely:

- The issuers’ credit risk management practices and how they relate to the recognition and measurement of expected credit losses;
- The issuers’ method to assess whether there has been a significant increase in credit risk;
- Whether the significant increase in credit risk is instrument-specific or caused by a collection of instruments;
- Quantitative and qualitative information used to evaluate the amounts arising from expected credit losses; and
- The gross carrying amount of financial assets by credit risk rating grades.

Disclosure of the above elements should be sufficient to increase compliance with the disclosure requirements under IFRS 7.

C. Business Combinations

IFRS 3 *Business Combinations* outlines the accounting when an acquirer obtains control of a business (e.g. an acquisition or merger). Each business combination is accounted for using the “acquisition method”, which requires:

- Identifying the acquirer;
- Determining the acquisition date;

- Recognizing and measuring the identifiable assets acquired, the liabilities assumed and any non-controlling interest in the acquiree; and
- Recognizing and measuring goodwill or a gain from a bargain purchase.

The Staff Notice points out that some issuers do not disclose certain information related to the business combination which occurred during the reporting period. To correct said deficiencies, the CSA encourages issuers to provide sufficient information so the investors can adequately evaluate the nature and financial effect of the business combination. In particular, issuers should focus on disclosing the following information:

- Amounts of revenue and profit or loss of the acquiree since the acquisition date; and
- Revenue and profit or loss of the combined entity for the current reporting period, as though the acquisition had been at the beginning of the annual reporting period.

MD&A Deficiencies

A. Forward-Looking Information

Forward-looking information ("**FLI**") is disclosure about possible events, conditions or financial performance that is based on assumptions about future economic conditions and courses of action. Forward-looking information includes Future Oriented Financial Information[2] and Financial Outlooks.[3]

The CSA notes that issuers must not disclose FLI unless the issuer has a reasonable basis for the FLI. For instance, the CSA found several cases where backlog, order book or order intake estimates were not based on firm purchase orders, but the basis of the estimate has not been disclosed. As such, any disclosure regarding material FLI should include material factors or assumptions used to develop the FLI.

With respect to prospective financial performance based on assumptions about future economic conditions, the CSA found that certain issuers disclosed an overly optimistic financial outlook of revenue projections, which was not supported by reasonable assumptions. The disclosure of the financial outlook of revenue projections must be based on **reasonable** assumptions and comply with the requirements of Part 4B of the *National Instrument 51-102*.

For instance, one issuer reported $180,000 of gross revenue in 2021 and disclosed in a press release that its gross revenue for 2022 will be approximately $3 to $5 million. A 1,600% increase in gross revenue is an inappropriate optimistic revenue projection and, from a practical perspective, highly unlikely. Moreover, the issuer did not provide any supporting detail regarding how the company plans to achieve such a result.

Proper disclosure of such revenue projection would have included a discussion/analysis of the following elements:

- the capacity of any new manufacturing facility and whether the projected production levels are possible;
- the necessary inputs required to produce the products;
- existence of demand for the product and its sufficiency;
- required working capital; and
- capacity to deliver the product to customers.

In providing the information above, the issuers should have explained whether it has the necessary infrastructure and whether its current personnel has the training required to proceed with shipping, receiving, producing, administering and ensuring quality control of the products.

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[2] Future Oriented Financial Information is forward-looking information about prospective financial performance, financial position or cash flows that is based on assumptions of future economic conditions and courses of action and that is presented in the format of a historical statement of financial position, statement of comprehensive income or statement of cash flows.

[3] A financial outlook is future-oriented financial information not presented in a historical financial statement format. For example, EBITDA, earnings per share, revenue targets, operating ratios, projected spending or operating costs, and earnings guidance are all forward outlooks.

B. Updating Previously Disclosed Material FLI

Section 5.8 of *National Instrument 51-102* provides that issuers must update previously disclosed FLI in certain circumstances. Such updates are required in the MD&A to assist investors with understanding how an issuer is progressing towards achieving its disclosed targets and objectives, as well as how actual results differ materially from previously disclosed FLI.

For instance, in the previous example, the issuer projected annual revenue of $3 to $5 million. Suppose the issuer has only reported $800,000 in sales after its second fiscal quarter, and the business does not experience seasonality. In that case, it is most likely that the issuer will not achieve the financial projections and that an update of FLI is required.

Updating previously disclosed FLI can be done in two ways. First, the issuer could provide an updated FLI in its next MD&A. Second, the issuer could disclose the updated information in a news release before filing the MD&A. This second approach ensures the new information is communicated to the market promptly. Note, however, that the subsequent MD&A must refer to the news release to satisfy the requirement in *National Instrument 51-102,* as including the information in a news release **instead** of the MD&A is **not** permitted.

C. Venture Issuers and Early-Stage Issuers

The Staff Notice underlined that several venture issuers tended to announce significant projects but later failed to disclose sufficient information to enable investors to understand the project, its timing and costs.

Should the issuer announce a significant project, the following information ought to be included (or at least discussed):[4]

- Issuer's plan for the project and the status of the project relative to that plan (short and long-term);
- Concrete milestones in the plan and what specific events need to occur to meet each milestone; and
- Description of the expenditures made to date and how these relate to anticipated timing and costs of the project.

Moreover, throughout the reporting periods, the issuers are encouraged to provide updates on the project status in each MD&A, including any delays in the previously disclosed timeline and anticipated cost overruns.

Finally, the MD&A must also include discussions of events and circumstances that occurred during the reporting period and that are reasonably likely to cause actual results to differ materially from material forward-looking information previously disclosed.

Other Regulatory Disclosure Deficiencies

A. Environmental Social Governance—Greenwashing

Environmental Social Governance ("**ESG**") is probably one of the most popular and fastest-growing trends in the corporate world. Companies look to be more transparent about how they operate, what they produce and how they aim to achieve sustainability. The use of disclosures pertaining to ESG, thus, grew at a proportional pace.

The terms ESG are used to refer to a wide variety of factors: pollution and waste management, biodiversity, climate risks, carbon and other greenhouse gas emissions, energy efficiency, diversity and inclusion, human rights, indigenous reconciliation, labour standards, corporate governance, shareholder engagement, bribery and corruption, to name a few. The breadth of what is encompassed by ESG can make using it misleading if there is no more specific disclosure about the factors being considered and how they are being measured and evaluated.

The Staff Notices noted that an increased number of issuers are potentially engaging in a behaviour known as "greenwashing", that is, making misleading, unsubstantiated or otherwise incomplete claims about business operations or the sustainability of a product or service being offered. In other words, greenwashing aims to deceive the reader into believing that a company's product or service is environmentally friendly or has a more significant positive environmental impact than what is true.

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[4] For additional disclosure elements, please refer to Item 1.4(d) of Form 51-102F1 *Management's Discussion & Analysis*.

Whether it is disclosure in a press release, ESG report or any other voluntary document, the CSA encourages issuers to avoid misleading promotional language and stresses the importance of substantiating any claim with reasonable and available data.

For instance, in an identified example of greenwashing disclosure, the issuer stated that it "plans to be carbon neutral by 2023". In the opinion of the CSA, the issuer made an unsubstantiated claim because the 2023 carbon neutrality claim has not to been supported by any facts or corporate activities and, thus, is misleading. Moreover, such type of statement would typically constitute FLI, which requires the issuer to: (1) have a **reasonable** basis for the FLI, (2) identify the material risk factors that could cause the actual results to differ materially, (3) state the material factors or assumptions used to develop the FLI and (4) describe the policies for updating the information. In other words, doubly deficient disclosure.

In the same identified example, the issuer, identifying itself as a "global leader in environmental solutions", stated that it established relationships with "high-quality" partners, which will contribute to the issuer's increased performance and long-term value. Although a commendable effort, the disclosure fails to provide sufficient information about the potential partners, particularly the claims about the partner being "high-quality". Finally, as far as "global leaders" go, the issuer does not fit the description as it has generated only nominal revenue from its operating activities.[5]

The CSA makes similar remarks about the issuers' "Social" and "Governance" levels of disclosure: overly-promotional and unsubstantiated.

B. Business Acquisitions

The Staff Notice highlights that several issuers did not file a business acquisition report for a significant acquisition under which securities of the acquired business were exchanged for the issuer's securities.

The CSA considers acquiring the target's securities a business acquisition, regardless of how the consideration is paid or transferred. When doing so, the issuers are encouraged to determine whether the acquisition is a significant acquisition by performing the required significance tests and may re-calculate the significance of the acquisition using the option significance test, if applicable.[6]

Should the issuer seek relief from the requirement to file a business acquisition report or to include the target's financial statements, the issuer must apply for exemptive relief **before** the filing deadline for the business acquisition report **and before** the closing date of the transaction, if applicable.[7]

Concerning transactions that meet the definition of "restructuring transaction"[8], the CSA reminds issuers that instead of filing a business acquisition report, the issuers are required to file a material change report or an information circular, for which prospectus-level disclosure is required. Prospectus-level disclosure refers to prescribed financial statements for the issuer and each entity whose securities are being changed, exchanged, issued or distributed.

Upon the closing of the restructuring transaction, the issuer is then required to file a material change report to provide the disclosure required by Item 14.2 of *Form 51-102F5 Information Circular* for each entity resulting from the restructuring. The CSA also noted that issuers might satisfy the disclosure requirement by incorporating information by reference into another document, such as an information circular sent to the issuer's security holders, a prospectus or a takeover bid circular.

Finally, a restructuring transaction also includes a reverse takeover. Determining whether a transaction is a reverse takeover requires an analysis of facts and circumstances against the relevant guidance and involves **significant**

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[5] For further information about problematic promotional activities by issuers, please refer to CSA Staff Notice 51-356 dated November 29, 2018.

[6] Please refer to Section 8.3 of *National Instrument 51-102* and Sections 8.2 - 8.3 of *Companion Policy 51-102CP Continuous Disclosure Obligations*.

[7] Please refer to Sections 8.4, 8.8 and 8.9 of *Companion Policy 51-102CP Continuous Disclosure Obligations* and *National Policy 11-203 Process for Exemptive Relief Applications in Multiple Jurisdictions*.

[8] For the definition, please see Section 1.1 of the *National Instrument 51-102* and Section 1.4 of *Companion Policy 51-102CP Continuous Disclosure Obligations*.

judgement. Issuers should disclose in the financial statements any significant judgements involved for a transaction that occurred during the applicable reporting period.[9]

C. Inconsistencies and Outdated Information

The Staff Notice concluded that several issuers provided inconsistent disclosure between documents that ought to be filed under securities legislation. The CSA reminds issuers that information should be consistently disclosed in all public documents, including voluntary disclosures (i.e. presentations, sustainability reports and public surveys). For instance, if the issuer includes material information in a voluntary disclosure but later omits to include it in the continuous disclosure documents, the issuer technically fails to provide the disclosure required by securities laws. In short, disclosure should be factual and balanced, and the issuer must disclose unfavourable news just as promptly and completely as favourable news.

The CSA also noted that certain issuers fail to provide up-to-date information in their reporting documents. The CSA reiterates that disclosure in the MD&A must be current to avoid being misleading when filed. Explaining how the issuer is performing during a reporting period is relevant, whereas any information that is no longer relevant to current operations and period should be removed.

D. Audit Committees—Composition and Responsibilities

The Staff Notice's results indicate that some issuers do not have an appropriate audit committee composition and inappropriately rely on exemptions to appoint fewer than three (3) members to the audit committee.[10]

Moreover, it appears that some audit committee members may not fully understand their responsibilities as directors and audit committee members. These responsibilities include:

- Overseeing the work of the issuer's external auditor, reviewing the auditor's services, participating in resolving any disagreements between management and auditors; and
- Reviewing the issuers' financial statements, MD&A, and profit or loss press releases **before** the issuer publicly discloses this information.

Directors are reminded that an audit committee member has extensive responsibilities which should be carefully considered before accepting an appointment.

Conclusion

In conclusion, it appears that the majority of the issuers reviewed by the CSA were proactive in providing quality and detailed disclosures. There is always room for improvement, but considering the uncertain macroeconomic and political environment in which issuers currently operate, this might be easier said than done. Nevertheless, issuers are invited to consult the CSA Staff Notice in order to perfect and complete their continuous disclosure documents.

CANADIAN SECURITIES ADMINISTRATORS

CSA Multilateral Staff Notice 58-314

CSA Multilateral Staff Notice 58-314 *Review of Disclosure Regarding Women on Boards and in Executive Officer Positions* was added on October 27, 2022. For more information, please see CSA Multilateral Staff Notice 58-314, which will be reproduced in Volume 1A of the *Canadian Securities Law Reporter* at ¶5844.

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[9] For further information, please refer to paragraphs B13 - B18 of *IFRS 3 Business Combinations* and paragraph 122 of *IAS 1 Presentation of Financial Statements*.

[10] For said exemption, please refer to *National Instrument 52-110 Audit Committees*.

PROVINCIAL UPDATES

Ontario

OSC Rule 32-506 and Form 32-506F1

OSC Rule 32-506 *Exemptions for International Dealers, Advisers and Sub-Advisers* and Form 32-506F1 *Submission to Jurisdiction and Appointment of Agent for Service Ontario Securities Commission Rule 32-506 (Under the Commodity Futures Act) Exemptions for International Dealers, Advisers and Sub-Advisers* were added on October 14, 2022. For more information, please see OSC Rule 32-506 and Form 32-506F1, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶480-127 and ¶480-127a.

OSC Staff Notice 33-754

OSC Staff Notice 33-754 *Compliance and Registrant Regulation Branch Summary Report for Dealers, Advisers and Investment Fund Managers* was added on October 14, 2022. For more information, please see OSC Staff Notice 33-754, which will be reproduced in Volume 3A of the Canadian Securities Law Reporter at ¶490-387s.

Ontario Instrument 45-507

Ontario Instrument 45-507 *Self-Certified Investor Prospectus Exemption (Interim Class Order)* was added on October 25, 2022. For more information, please see Ontario Instrument 45-507, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶480-206a.

OSC Staff Notice 81-733

OSC Staff Notice 81-733 *Summary Report for Investment Fund and Structured Product Issuers* was added on October 19, 2022. For more information, please see OSC Staff Notice 81-733, which will be reproduced in Volume 3A of the *Canadian Securities Law Reporter* at ¶490-700i.

OSC Rule 91-502

OSC Rule 91-502 *Trades in Recognized Options* was amended on October 14, 2022. For more information, please see OSC Rule 91-502, which will be reproduced in Volume 3A of the Canadian *Securities Law Reporter* at ¶480-502.

RECENT CASES

Breach of Cease-Trade Order

Alberta Securities Commission, August 18, 2022

North America Frac Sand, Inc. (“NAFS”) was an American company which was also a designated issuer and required to file certain materials with the Alberta Securities Commission (the “Commission”). Lambert (Bert) Joseph Lavallee (“Lavallee”) and Brian Maurice Gibbs (“Gibbs”) both owned NAFS shares; Lavallee also had prior involvement with NAFS. David Malcolm Alexander (“Alexander”) was a director of NAFS during the material times. Canadian Sandtech Inc. (“CSI”) was founded by the Newton brothers, and held leases (the “Leases”) over properties in Saskatchewan from which they planned to extract frac sand. As CSI had financial difficulty and poor record keeping, the Newtons sought outside assistance to further the project. Brian Maurice Gibbs (“Gibbs”) was a chartered accountant and became involved with CSI in early 2015 and acted as an advisor to the Newtons. Lambert (Bert) Joseph Lavallee (“Lavallee”) became involved in May 2015 and provided funding to NAFS. In July 2015, a transaction (the “Transaction”) was underway, whereby NAFS would acquire the Leases through the acquisition of North America Frac Sand (CA) Ltd. (“NAFSCA”), a wholly owned subsidy of CSI created in June 2015, to which CSI would transfer the Leases. After the Transaction was complete, CSI and its shareholders would receive common shares of NAFS in exchange for the outstanding NAFSCA shares, and NAFS would thereby own the Leases. The Transaction was eventually completed. Other notable events included that in May 2016, a cease-trade order (“CTO”) was issued by the Alberta Securities Commission (the “Commission”) against NAFS for filing issues and was never revoked, and an engineering firm was retained to prepare a report on the viability of the leased

lands. Lavallee paid the bill for the engineer's report which was released in May 2017. Between December 2016 and September 2017, Lavallee sold over 4.5 million NAFS common shares, and purchased NAFS common shares in May and June 2017. Commission Staff made a number of allegations against the respondents, primarily related to the direction and control of NAFS, including that: Lavallee and Gibbs failed to file insider reports contrary to section 182 of the Alberta *Securities Act*, RSA 2000, c. S-4 (the "Act"); Lavallee, Gibbs, and Alexander filed reports with the Commission containing misleading statements or omissions contrary to subsection 222.1(2) of the Act; Lavallee engaged in insider trading contrary to subsection 147(3) of the Act and breached the CTO contrary to section 93.1 of the Act; and Lavallee concealed or withheld information from Commission Staff during their investigation contrary to subsection 93.4(1) of the Act.

Lavallee was found to have traded in breach of a cease trade order and concealed information during an investigation. The Panel began its analysis by noting that several of the allegations against the respondents depended on the contention that Lavallee and Gibbs were *de facto* officers of NAFS. On this issue, the Panel noted that it was well accepted that the assessment of whether an individual was a *de facto* officer was the same as the determination of whether one was a director, and "'requires a consideration of the entirety of the individual's involvement in the context of the company's activities' to determine whether he or she 'is an integral part of the mind and management of the company'" (*see Re Mandyland Inc*., 2012 ABASC 436). The Panel further noted the analysis was fact-specific, and some functions that could be considered to bring an individual into the *de facto* officer or director role included: responsibility for supervision, direction, operation of the company; signing authority over bank accounts; negotiation on behalf of the company; arranging public offerings; making significant business decisions; acting in positions with pay and responsibility similar to a director or officer; preparing corporate documents; giving instructions to outside firms; and being referenced as a director or officer (see *Re World Stock Exchange* (2000), 9 A.S.C.S. 658, and *Re Pinchin* (1996), 12 C.C.L.S. 24). The Panel noted that NAFS' key activities during the relevant period were not extensive and included: remaining in good standing; making required filings to regulators; closing the Transaction; engaging an engineer for a report on the viability of leased land; and having the CTO lifted. The Panel also found that Alexander was performing the duties of a director and was not a "figurehead" which was Staff's position. Regarding Lavallee, Staff argued that Lavallee's motive for concealing his control over NAFS was because of his regulatory history and he performed duties of a *de facto* officer including: funding NAFs; meeting with and directing the engineering firm; working on NAFS' website; hiring third parties; and communicating with the Commission. However, the Panel found, among other things, that: while Lavallee did pay NAFS expenses out of his own pocket, "Staff did not point … to any authority that paying invoices is a factor in determining whether a person is a *de facto* officer"; Lavallee did not direct the work of the engineer nor hire the third parties; and there was little evidence that Lavallee was integral to NAFS' management or held himself out as being so. The Panel's overall conclusion was that Lavallee was involved with various aspects of NAFS given his investment and interest in having NAFS succeed, but "involvement and interest do not equate to management", and what little there was to manage was handled by Alexander. Turning to Gibbs, Staff argued that he was "involved in all aspects of NAFS' operations" and his *de facto* officer duties included: providing input into various filings; dealing with the NAFS auditor; drafting NAFSCA documents; directing the engineer; drafting the Transaction documents; dealing with the Leases; marketing NAFs; and working on the NAFS' website. However, in reviewing the evidence, the Panel concluded, among other things, that: Gibbs' initial involvement with NAFS was due to his involvement with CSI and the Newton brothers; Alexander had greater involvement with the auditor than Gibbs; Alexander had final say over filings and rejected some of Gibbs' input; and Gibbs' did not have extensive involvement with the Leases. As with Lavallee, the Panel did not find on a balance of probabilities that Gibb's involvement with NAFS rose to the level of a *de facto* officer. Having determined that neither Gibbs nor Lavallee were *de facto* officers, the majority of the allegations premised on that basis were dismissed. The Panel did find that Lavallee had breached the CTO and concealed information from Staff during the investigation. Sanctions would be determined at a later date.

North America Frac Sand, Inc. (Re), 2022 CSLR ¶900-945

Reciprocal Orders

Ontario Capital Markets Tribunal, August 24, 2022

Ronald James Aitkens ("Aitkens") was the guiding mind of the Foundation Capital Group Trust (the "Trust"), which was established to raise funds for oil and gas exploration and development (the "Trust Project"). Aitkens also controlled 0865701

B.C. Ltd ("0865710") which acted as the trustee. Roy Juergen Beyer ("Beyer", together with Aitkens the "Respondents") primarily acted in a marketing capacity but was also a director and officer of various entities connected with the Trust. From January 2010 to February 2011, the Respondents raised approximately $33.6 million through offering memoranda ("OMs") for the Trust. Aitkens also controlled entities involved in the SV Project and the HV Project, which were to use investors' funds to purchase and develop lands in Calgary and British Columbia, respectively. From October 2007 to August 2012, $31.6 million was raised for the SV Project, and from February 2009 to October 2012, $16.1 million was raised for the HV Project. On February 15, 2018, a panel of the Alberta Securities Commission (the "ASC") found that: the Respondents, the Trust, 0865701, and an entity involved with the HV Project each breached subsection 92(4.1) of the Alberta *Securities Act*, RSA 2000, c. S-4 (the "ASA") by making materially misleading omissions in two of the OMs; and, Aitkens and two entities involved with the SV and HV Projects breached subsection 93(*b*) of the ASA by perpetuating a fraud when funds raised from investors were diverted to other entities and for purposes unrelated to the two Projects. On October 2, 2019, an ASC Panel imposed sanctions against the Respondents and the corporate entities. Specifically, Aitkens was permanently prohibited from participating in the Alberta capital market and ordered to pay an administrative penalty of $600,000 and costs. Beyer was banned from participating in the Alberta capital market for 10 years and ordered to pay an administrative penalty of $75,000 and costs (the "ASC Order"). Staff of the Ontario Securities Commission (the "Commission") requested an order imposing sanctions that substantially mirrored the non-financial sanctions imposed by the ASC against the Respondents, pursuant to subsections 127(1) and 127(10) of the Ontario *Securities Act*, RSO 1990, c S.5 (the "Act").

The order was granted. The issues before the Tribunal were: whether any of the circumstances under subsection 127(10) of the Act applied to the Respondents; and, if so, whether the Tribunal should exercise its public interest jurisdiction to make an order. The Tribunal began by finding that under paragraph 4 of subsection 127(10) of the Act, it could make an order against a person who "is subject to an order made by a securities regulatory authority, derivatives regulatory authority or financial regulatory authority, in any jurisdiction, that imposes sanctions, conditions, restrictions or requirements". In this case, the ASC was a securities regulatory authority and had ordered sanctions against the Respondents, with the result that the Tribunal could make an order against them if it determined it was in the public interest to do so. Staff argued, among other things, that it was in the public interest to make an order because: the misconduct at issue would likely have breached the Act; Ontario investors were defrauded and Aitkens had a history with an Ontario-based company; and the orders were prospective and would only impact the Respondents if they attempted to participate in the Ontario market. Beyer argued, among other things, that the application should be dismissed due to undue delay or the expiration of the applicable time limit. The Tribunal rejected Beyer's argument, finding the six-year limitation period to commence an action started when the ASC Order was made. The Tribunal also found that Beyer failed to discharge the onus to establish that the ASC Order should not be reciprocated, which required him to demonstrate that: there was no substantial connection between himself and Alberta; the ASC Order was obtained through fraud; or the ASC denied him natural justice. In the Tribunal's view, sanctions were needed to protect Ontario investors by deterring the Respondents or others from engaging in similar or other misconduct, and determined the requested order was appropriate.

Aitkens (Re), 2022 CSLR ¶900-946

Abuse of Process

British Columbia Court of Appeal, August 24, 2022

Scott Lower (the "Appellant") was an "approved person" registered with the Investment Industry Regulatory Organization of Canada ("IIROC"). IIROC's authority to regulate its members' activities flowed from a contractual obligation to comply with IIROC's bylaws, regulations, and rules. Beginning in 2006, the RCMP began investigating the Appellant for potentially engaging in matched trades and paying secret commissions. In July 2008, the RCMP notified IIROC about the investigation, and on September 18, 2008, the RCMP provided IIROC with a copy of a Information to Obtain a Production Order ("ITO") which set out detailed information about the potential criminal activity. On September 11, 2008, the Appellant was arrested by the RCMP but was ultimately never charged. On October 28, 2008, the Appellant resigned from his firm and from being an approved person. IIROC informed the Appellant that he was required to attend a compelled interview on November 12, 2008; the Appellant failed to appear which resulted in a discipline hearing that was held on August 11, 2009. On May 29, 2009, IIROC had provided the Appellant with a "Disclosure Index" which, among

other things, disclosed the ITO, but had no other information from IIROC's investigation and had redactions. Six days prior to the discipline hearing, IIROC counsel provided the Appellant with further documentation. At no point did the Appellant raise concerns about procedural fairness. In a decision dated September 1, 2009 (the "Discipline Decision"), an IIROC Panel found that the Appellant had breached IIROC Dealer Member Rule 19.5 which requires an approved person under investigation to attend an interview if required. The Appellant was subsequently banned from being registered in any capacity with IIROC, fined $50,000, and required to pay costs. Pursuant to IIROC Rule 33.1 and sections 28 and 165 of the British Columbia *Securities Act*, RSBC 1996, c. 418 (the "Act"), the Appellant could have requested a review of the Discipline Decision within 30 days of it being received but did not do so until six years later. On December 3, 2015, the British Columbia Securities Commission (the "Commission") ruled that the Appellant was out of time to request a review. On January 5, 2018, the Appellant commenced an action in the British Columbia Supreme Court (the "BCSC") seeking declarations that, among other things: the Discipline Decision was *ultra vires* and invalid; he was denied procedural fairness and natural justice during the investigation that resulted in the Discipline Decision; and, IIROC acted in bad faith and failed to act with integrity, transparency, and fairness during its investigation and disciplining. IIROC sought and received a summary dismissal of the Appellant's action on the basis that it was barred by the *Limitation Act*, SBC 2012, c. 13, the doctrine of laches, and it was an abuse of process and a collateral attack on the Discipline Decision (the "BCSC Decision"; see 2020 CSLR ¶900-814). On the finding of an abuse of process, the BCSC judge concluded, among other things, that the Appellant: was aware of potential procedural unfairness issues in 2009, prior to the discipline hearing; did not avail himself of statutory remedies; and had caused IIROC to incur expenses to defend the suit and deprived them of the ability to provide any remedies. The BCSC judge also held that "[s]eeking a declaration of invalidity of the Discipline Decision is a misuse of court procedure. It is manifestly unfair to IIROC and offends the principle of finality." The Appellant appealed to the British Columbia Court of Appeal (the "Court") on the basis that the BCSC judge erred in her factual findings and legal analysis.

The appeal was dismissed. The Court began its analysis by noting, among other things, that: judges exercise discretion that is entitled to deference when applying the abuse of process doctrine (see *Krist v. British Columbia*, 2017 BCCA 78); appellate intervention is warranted where the judge proceeded on a wrong principle or gave insufficient weight to relevant considerations, made a palpable and overriding error in assessing facts or in applying the law, or the discretion amounted to an injustice; the abuse of process was a flexible doctrine and used to prevent misuse of the court's procedures that would result in unfairness to a party to the litigation or "bring the administration of justice into disrepute" (see *Canam Enterprises Inc. v. Coles*, 51 O.R. (3d) 481); the doctrine's focus is on the integrity of the administration of justice and not the parties' interest; and excessive delay and finality may be factors to consider in applying the doctrine. The Court's key findings included that: the BCSC judge did not overlook material evidence that contradicted her finding that the Appellant was aware of procedural unfairness issues in 2009, but instead rejected it; the BCSC judge did not err in considering the Appellant's failure to pursue statutory remedies and finality in her analysis; and the BCSC judge did not err in considering IIROC's interests which were relevant given its public interest mandate. Ultimately, the Court was of the view that the Appellant was attempting to use the court's process to invalidate a decision that was made in the public interest – relief that could have been sought over a decade prior – and agreed with the BCSC judge that permitting the action would bring the administration of justice into disrepute. Having found there was no error in the abuse of process finding, the Court did not need to address the BCSC judge's findings on the doctrine of laches or time limit.

Lower v. IIROC, 2022 CSLR ¶900-947

Fraud

British Columbia Securities Commission, August 8, 2022

John Sand ("Sand"), Karol Achs ("Achs"), and Jolyon Charles Christopher Gulston ("Gulston", together with Sand and Achs, the "Respondents") were involved in the development of zinc air battery technology. Achs had obtained worldwide rights to the technology which were held through Marketwise Investments Inc. ("Marketwise"). Each of the Respondents had provided financing for the development of the battery directly or through companies they controlled. Starting in the fall of 2014, the Respondents began meeting with K and P who were told, among other things, that: the market for the new battery was enormous; there were already existing orders including from a company in Africa; and the investors' funds would be used to alter a building to accommodate the battery production line, laboratory, and storage, and to buy

manufacturing equipment. K and P were also shown documentation to support the purported purchase commitments. K and P provided a total of $600,000 to Marketwise. With no progress being made to the building, K and P demanded the return of their funds and only received $200,000. Investigation Staff of the British Columbia Securities Commission (the "Commission") determined that the remainder of the investors' funds went to, among other things: repay Sands' girlfriend; repay a relative of Achs'; repay loans made to Marketwise; and pay various of the Respondents' personal expenses. Approximately $100,000 was withdrawn in cash with no evidence of where it was spent. Gulston also contacted several potential investors and made claims including that: international companies had already placed orders for the batteries; and a manufacturing plant was already in existence and additional ones would be established. In a Notice of Hearing dated October 26, 2020, the Executive Director of the Commission alleged that the Respondents engaged in conduct which perpetuated a fraud, contrary to subsection 57(*b*) of the British Columbia *Securities Act*, RSBC 1996, c. 418 (the "Act") and Gulston made misrepresentations to potential investors contrary to subsection 50(1)(*d*) of the Act.

The Respondents were found to have breached the Act. The Panel began its analysis by noting, among things, that: to prove fraud, the Executive Director had to establish, on a balance of probabilities, the conduct involved securities, the *actus reus* (the prohibited act and deprivation or placing of the victim's pecuniary interests at risk), and *mens rea* (knowledge of the prohibited act and deprivation); to prove misrepresentations, the Executive Director had to establish that Gulston engaged in investor relations activities (communications that promoted or could promote the purchase of securities) and made false statements or omissions that were material to effect the purchase of securities; and materiality was determined through the market impact test (i.e., "would the fact ... reasonably be expected to significantly affect the market price or value of the securities?", also taking into consideration the issuer's industry and the market). On the allegation of fraud, the Panel's key findings included that: the investments were securities as defined by the Act as they were either investment contracts (from *Pacific Coast Coin Exchange v. Ontario Securities Commission*, [1978] 2 SCR 112, "an investment in a common enterprise from which the Investors expected to profit from the efforts of the respondents") or a profit sharing agreement; the deceitful acts included the Respondents' stating there were orders when there were none and stating the funds would be used for the manufacturing facility when they were diverted for other purposes, and the investors were deprived of their funds; and the Respondents knew they were deceiving the investors and depriving them of their funds as Sand and Achs had control over Marketwise's spending, and Gulston had insisted on payment of $100,000. The Panel also concluded that Gulston made misrepresentations contrary to the Act, with key findings including that: Gulston had communicated with potential investors and this constituted investor relations activities; Gulston made several misrepresentations about order status and manufacturing capabilities that he knew or should have known were false; and the misrepresentations were material as they would have had an impact on the market price of the security as a reasonable investor would be led to believe that the company had future prospects. Sanctions would be determined at a later date.

Sand (Re), 2022 CSLR ¶900-948

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