

# 2003 BCSECCOM 847

## Amended Notice of Hearing

**Michael Lee Mitton and Bradley Nixon Scharfe  
(the Respondents)**

### **Section 161 of the *Securities Act*, RSBC 1996, c. 418**

- ¶ 1 TAKE NOTICE that a hearing will be held (the Hearing) to give the Respondents an opportunity to be heard before the British Columbia Securities Commission (the Commission) considers whether it is in the public interest to make the following orders:
- 1.1 pursuant to section 161(1)(c) of the *Securities Act*, R.S.B.C. 1996, c. 418 (the *Act*) that any or all of the exemptions described in sections 44 to 47, 74, 75, 98 or 99 of the *Act* do not apply to the Respondents;
  - 1.2 pursuant to section 161(1)(b) of the *Act* that Michael Lee Mitton (Mitton) cease trading in or be prohibited from purchasing any securities;
  - 1.3 pursuant to section 161(1)(d) of the *Act* that the Respondents resign any position they hold as directors or officers of any issuer and be prohibited from becoming or acting as directors or officers of any issuer;
  - 1.4 pursuant to section 161(1)(d) of the *Act* that the Respondents be prohibited from engaging in investor relations activities;
  - 1.5 pursuant to section 161(1)(f) of the *Act* that the registration of Bradley Nixon Scharfe (Scharfe) be suspended, cancelled or restricted or that conditions be imposed on his registration;
  - 1.6 pursuant to section 162 of the *Act* that the Respondents pay an administrative penalty;
  - 1.7 pursuant to section 174 of the *Act* that the Respondents pay the prescribed fees or charges for the costs of or related to the Hearing; and
  - 1.8 to make any other orders the Commission may deem appropriate in the circumstances.
- ¶ 2 AND TAKE NOTICE that the Commission will be asked to consider the following facts and allegations in making its determinations:

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### **The Respondents**

- 2.1 Mitton has never been registered under the *Act* in any capacity.
- 2.2 On November 14, 1988, Mitton entered into an Agreement and Undertaking (the Agreement) with the Superintendent of Brokers. In the Agreement, Mitton admitted to several breaches of the *Securities Act*, S.B.C. 1985, c. 83 (the *Former Act*), including: insider trading; market manipulation; and failure to meet continuous disclosure filing requirements.
- 2.3 On December 19, 1988, the Superintendent of Brokers issued an Order under sections 145 and 145.1 of the *Former Act* (the Order), which among other things, removed Mitton's exemptions under the *Former Act* and prohibited him from serving as an officer or director of any issuer from November 1, 1988 to October 31, 2008.
- 2.4 Mitton has been convicted by Canadian courts of numerous counts of fraud. Mitton's most recent convictions for fraud occurred in British Columbia on or about December 27, 2000, when he pled guilty to six counts of fraud in relation to frauds he perpetrated on brokerage firms and a charity.
- 2.5 Scharfe has been registered as an investment advisor from on or about December 1987 to the present.

### **Share Trading Scheme**

- 2.6 From on or about December 1995 to March 1996 (the Relevant Period), Mitton carried out a trading scheme (the Share Trading Scheme) involving the trading of shares of a number of companies listed on the former Vancouver Stock Exchange (the VSE).
- 2.7 The Share Trading Scheme involved making undeclared short sales of shares through cash accounts at one brokerage firm. The short position was to be covered through the subsequent purchase of shares of the same issuer at a lower price, through an account at another brokerage firm. The shares acquired from the second brokerage firm were then to be delivered against payment (DAP) to the first brokerage firm in order to settle the outstanding short position. Through the use of cash accounts, the margin requirements that would otherwise be required on short sales were avoided.

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- 2.8 Mitton used a group of nominees (the Nominee Group) to place the trades related to the Share Trading Scheme through a number of accounts at various brokerage firms.
- 2.9 The members of the Nominee Group for the most part relied upon Mitton's advice and instructions to carry out the Share Trading Scheme. In particular Mitton:
  - 2.9.1 informed them that the Share Trading Scheme would enable them to trade shares without cost to them by trading on a brokerage firm's capital;
  - 2.9.2 told them which brokers to approach to open accounts;
  - 2.9.3 assisted them in filling out the client account opening forms;
  - 2.9.4 advised them as to which shares to trade and what instructions to give the brokers for the trades;
  - 2.9.5 assisted them in preparing the documents required by the brokers to settle the trades; and
  - 2.9.6 informed them that if any of the brokers began to press for settlement or delivery of shares, the brokers should be informed that the shares were offshore and would take a period of time to deliver.
- 2.10 Mitton tracked the trading of the members of the Nominee Group. At Mitton's request, all or most of the members directed their respective brokers to provide a daily confirmation of trading in their accounts to Mitton.
- 2.11 Mitton and the members of the Nominee Group made assurances to the brokers that cash and shares would be delivered to cover debits in the various accounts, but most of the accounts had to be sold out by the brokers to cover the debits.
- 2.12 Mitton hid his involvement in the Share Trading Scheme from some by, among other things, using the members of the Nominee Group to place the trades and by employing one or more aliases.
- 2.13 Scharfe was one of the brokers used by Mitton and some of the members of the Nominee Group to place trades related to the Share Trading Scheme.

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- 2.14 On February 4, 1996, a meeting was held between Scharfe, Mitton and some of the members of the Nominee Group to discuss settlement problems with the accounts. During the course of this meeting, Scharfe agreed to deal directly with Mitton to ensure settlement of outstanding positions in some of the accounts held by members of the Nominee Group.
- 2.15 After the meeting, Scharfe continued to accept orders for short sales in one or more of the accounts of the Nominee Group.
- 2.16 Scharfe was disciplined by the Canadian Venture Exchange (the CDNX) as a result of his involvement with the Share Trading Scheme. In a Settlement Agreement with the CDNX dated March 26, 2001, Scharfe admitted the following facts:
  - 2.16.1 he was the investment advisor responsible for six cash accounts that operated a short selling scheme (the Associated Accounts);
  - 2.16.2 between December 5, 1995 and February 14, 1996, 116 undeclared short sales of shares involving 24 issuers were executed through the Associated Accounts;
  - 2.16.3 all trades in the Associated Accounts were executed through him;
  - 2.16.4 none of the transactions effected in the Associated Accounts settled within a reasonable period of time in accordance with industry practice for short accounts and he should have suspected that the clients were not selling from a long position;
  - 2.16.5 prior to March 15, 1996, he was aware that an individual was keeping track of the short position in the Associated Accounts;
  - 2.16.6 at a meeting on February 4, 1996, an owner of one of the Associated Accounts introduced him to this individual and he agreed to deal directly with this individual in arranging a timely delivery of shares to cover outstanding short positions in the Associated Accounts; and
  - 2.16.7 when this individual was unable to deliver the shares within the settlement period, the brokerage firm that employed Scharfe instructed him to close all but one of the Associated Accounts.
- 2.17 In relation to this conduct, Scharfe acknowledged, among other things, the following:

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- 2.17.1 he ought to have known that the short selling scheme implemented in the Associated Accounts violated the VSE's short sale rules; and
- 2.17.2 that he had a responsibility to detect unlawful trading schemes that might impugn the integrity of the capital markets and that he failed to use due diligence to learn the essential facts about the trading activity in the Associated Accounts.

### **Alleged Violations of the *Former Act***

2.18 During the Relevant Period, Mitton did the following:

- 2.18.1 acted as an advisor in British Columbia without an exemption from the registration requirements of the *Former Act*, and without being registered to advise, contrary to section 20 of the *Former Act*;
- 2.18.2 while placing orders for the sale of securities either directly or through the members of the Nominee Group, failed to declare that neither he nor his nominee owned the security in question, contrary to section 41 of the *Former Act*; and
- 2.18.3 participated in a scheme that he knew or ought reasonably to have known perpetrated a fraud on persons in British Columbia, contrary to section 41.1 of the *Former Act*.

2.19 It would be in the public interest, as set out in section 144 of the *Former Act*, to prohibit Mitton from operating in the capital markets of British Columbia because of the following:

- 2.19.1 his activities related to his December 27, 2000 criminal conviction;
- 2.19.2 his involvement in the Share Trading Scheme; and
- 2.19.3 his breach of the Order.

2.20 During the Relevant Period, Scharfe did the following:

- 2.20.1 failed to establish the identity and reputation of his clients as required by section 43 of the *Securities Regulations*, B.C. Reg. 270/86 (the *Securities Rules*) and the rules and by-laws of the VSE;

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2.20.2 breached the *Former Act* and the rules and by-laws of the VSE by placing orders or allowing clients to place orders for sales of securities in accounts over which he was the investment adviser without declaring that such sales were short sales; and

2.20.3 breached the *Securities Rules* and the rules and by-laws of the VSE by, among other things, allowing accounts to be operated as nominee accounts, accepting orders from a third party without written authorization to do so and accepting orders from Mitton when Mitton was prohibited from participating in the market.

2.21 It would be in the public interest, as set out in section 144 of the *Former Act*, to prohibit Scharfe from operating in the capital markets of British Columbia for the following reasons:

2.21.1 he knew or ought reasonably to have known that he was assisting Mitton and the members of the Nominee Group to carry out the Share Trading Scheme;

2.21.2 he knew or ought reasonably to have known that he was assisting Mitton in breaching the Order;

2.21.3 he failed to fulfil his gatekeeper responsibilities by not identifying and preventing improper trading schemes; and

2.21.4 he violated VSE By-Laws and Rules as set out above.

¶ 3 AND TAKE NOTICE that the Respondents may be represented by counsel at the Hearing and may make representations and lead evidence. The Respondents are requested to advise the Commission of their intention to attend the Hearing by contacting the Secretary of the Commission at P.O. Box 10142, Pacific Centre, 5<sup>th</sup> Floor, 701 West Georgia Street, Vancouver, British Columbia, V7Y 1L2 or by email at: commsec@bcsc.bc.ca.

¶ 4 AND TAKE NOTICE that the Respondents are required to attend at the 12<sup>th</sup> Floor, 701 West Georgia Street, Vancouver, British Columbia, on Tuesday, February 26, 2002, at 10:00 a.m., if they wish to be heard before the Commission fixes a date for the Hearing;

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- ¶ 5 AND TAKE NOTICE that the Commission may make determinations in this matter if the Respondents or their counsel do not appear at the Hearing.
- ¶ 6 December 17, 2003

Steve Wilson  
Executive Director