2005 BCSECCOM 612

H & R Enterprises Inc.

and

Michael Lee Mitton, David Scott Heredia and Jerome Rosen

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

Hearing

Panel	Adrienne Salvail-Lopez	Vice Chair
	Marc A. Foreman	Commissioner
	Robert J. Milbourne	Commissioner
Dates of Hearing	February 17 to 20 and 26, 2004	
Date of Decision	September 29, 2005	

Appearing

Fiona M. Anderson Lorne Herlin	For the Executive Director

Decision

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Introduction

¶ 1 This decision relates to a hearing under section 161 of the *Securities Act*, RSBC 1996, c.418. The hearing dealt with allegations in four notices of hearing issued by the Executive Director. Each notice involved an investment scheme orchestrated by Michael Lee Mitton. During the period covered by the notices, Mitton was subject to an order removing his statutory exemptions and prohibiting him from becoming or acting as a director or officer of any issuer.

¶ 2 The "short sales" notice of hearing was issued on December 27, 2001; it was amended and the final version issued on December 17, 2003. The short sales notice says that Mitton, either directly or through nominees, made undeclared short sales of shares of issuers listed on the Vancouver Stock Exchange (now the TSX Venture Exchange). The notice says that Mitton's scheme involved making an undeclared short sale of shares through a cash account at one dealer and covering the short position by subsequently purchasing the shares through another dealer. This would allow Mitton and his nominees to avoid the margin requirements imposed on short sales of shares. The notice says that Mitton and his nominees assured the dealers that cash and shares would be delivered to cover debits in the accounts, but most of the accounts had to be sold out by the dealers to cover the debits. The notice contains allegations against Mitton and Bradley Nixon Scharfe, who was a registered salesperson with Canaccord Capital Corporation. Before the hearing, the Executive Director and Scharfe entered into a settlement, containing an agreed statement of facts. The settlement is in evidence in this hearing. The short sales notice alleges that Mitton:

- acted as an unregistered adviser;
- made undeclared short sales; and
- perpetrated a fraud on persons in British Columbia.

¶ 3 The "bond trading" notice of hearing was issued on January 31, 2002. It says that Mitton used nominees to purchase Government of Canada bonds through dealers, without the ability or intention of paying for the bonds. The bond trading notice alleges that Mitton:

- perpetrated a fraud on persons in BC.

¶ 4 The "share purchase" notice of hearing was issued on March 28, 2002; it was amended and the final version issued on January 28, 2004. The notice says that Mitton, either directly or through nominees, purchased shares through accounts at dealers that he had no intention of paying for and did not pay for. The notice also says that Mitton advised the nominees on the share purchases. The original notice contained allegations against Mitton, Scharfe and George Ronald Stephens. Before the hearing, the Executive Director entered into settlements, each containing an agreed statement of facts, with Scharfe and Stephens. The Scharfe settlement is in evidence. Stephens testified at the hearing. The share purchase notice alleges that Mitton:

- acted as an unregistered adviser; and
- perpetrated a fraud on persons in BC.

¶ 5 The "H & R" notice of hearing was issued on October 17, 1997. H & R Enterprises Inc. was the sole respondent and the notice was accompanied by a temporary order that all persons cease trading in the securities of H & R until October 30, 1997. The Commission extended the temporary order several times and, on February 20, 1998, extended it until a hearing is held and a decision is rendered.

¶ 6 The Executive Director amended the H & R notice of hearing and issued the final version on December 17, 2003. The notice says that several individual respondents, including Mitton, manipulated the price for the shares of H & R. Before the hearing, the Executive Director removed two respondents – Leslie Ann Gmur and Katherine Nicole Burden (formerly Hanna) – and entered into settlements, each containing an agreed statement of facts, with five respondents – Scharfe, Charles Wiebe, Elizabeth Anne Moxon, Jacob Jackie Alter and Richard Harris. Those settlements, other than Weibe's, are in evidence. Wiebe testified at the hearing. The remaining respondents are Mitton, David Scott Heredia, Jerome Rosen and H & R.

¶ 7 The H & R notice alleges that Mitton:

- traded without registration;
- distributed shares without a prospectus; and
- participated in transactions that he knew or ought to have known would contribute to a misleading appearance of trading activity or an artificial price for the shares of H & R.

¶ 8 The H & R notice alleges that Heredia and Rosen participated in transactions they knew or ought to have known would contribute to a misleading appearance of trading activity or an artificial price for the shares of H & R. The notice submits that it would be in the public interest to prohibit Heredia and Rosen from operating in BC's capital markets because they were involved in the H & R manipulation, they participated in Mitton's breach of his December 1988 order and, in the case of Heredia, he has been sanctioned by two securities regulatory authorities in the United States.

¶ 9 The H & R notice alleges that H & R distributed shares without a prospectus. The notice submits that it would be in the public interest to cease trading in H & R's shares because H & R issued false and misleading news releases.

¶ 10 The four notices of hearing submit that it would be in the public interest to prohibit Mitton from operating in BC's capital markets because:

- he breached his December 1988 order;
- he was convicted in BC in December 2000 of six counts of securities fraud; and
- he was involved in the short sales, bond trading and H & R schemes.

¶ 11 The hearing was held on February 17 to 20 and 26, 2004. We heard testimony from Wiebe, Stephens, Edward Rempel, William Park (Assistant Director of Enforcement at the US National Association of Securities Dealers) and Alan Costin (from Commission staff). None of the respondents appeared.

Background

Mitton

¶ 12 By the time Michael Lee Mitton first became involved with the Commission in 1988, he had 90 criminal convictions in Ontario and Quebec, all of which related to fraud, forgery or false pretence.

¶ 13 On December 19, 1988, the Superintendent of Brokers (now the Executive Director) issued an order removing Mitton's statutory exemptions, and prohibiting him from becoming or acting as a director or officer of any issuer, until November 1, 2008. The order was based on an agreement and undertaking signed by Mitton on November 14, 1988, in which Mitton consented to the order and admitted that he had, in respect of various issuers listed on the VSE:

- made trades through accounts owned or controlled by him that did not result in a change of beneficial ownership and "may have resulted in a misleading appearance of active public trading" in the shares of three issuers;
  (a)
- acquired beneficial ownership of over 20% of the shares of two issuers, through trades in accounts owned or controlled by him or accounts of persons acting in concert with him, but did not make any of the disclosure required of an insider and control person;
  (b)
- while in a special relationship with an issuer, traded shares of the issuer with knowledge of material facts that had not been generally disclosed;
  (c)
- while in special relationships with two issuers, informed others of material facts about those issuers that had not been generally disclosed; and
  (d)
- performed the functions of a director and officer for seven issuers while disqualified from doing so under corporate legislation.

¶ 14 In 1989, Mitton was convicted of seven counts of securities fraud in Quebec. He had purchased shares through accounts at dealers in Montreal, but did not pay for the shares.

¶ 15 On January 27, 1993, Mitton was indicted in the US for securities fraud. The indictment alleged that Mitton purchased shares of a VSE listed issuer through four dealers in the US, which he purported to pay for with worthless cheques totalling US$1,640,996. The issuer was one of those referred to in Mitton's agreement and undertaking of November 14, 1988. The indictment remains outstanding.

¶ 16 The events giving rise to the four notices of hearing began in December 1995. At that time, Mitton had 97 criminal convictions and an outstanding US indictment for securities fraud. He was banned from trading in BC, and from acting as a director or officer of any issuer, until 2008. Mitton has never been registered under the Act.

The short sales scheme

¶ 17 In December 1995, Mitton approached several Abbotsford businessmen with a proposed investment scheme. One of these businessman was Fred Rempel. Fred Rempel raised the proposal with his property manager, Charles Wiebe. Wiebe described Mitton's proposed scheme:

A Mr. Fred Rempel mentioned to me that Mr. Mitton had approached him about a trading idea and scheme which he was interested in perhaps pursuing, and asked if I would be interested in looking at it with him and working on it for him.
Q Can you describe that scheme?
A It was described as buying and selling stocks which were either undervalued or overvalued in price, selling if they were overvalued in price and buying them back in, and buying them if they were undervalued in price and selling them as they went up.

¶ 18 Fred Rempel and Wiebe met with Mitton that December and agreed to participate in Mitton's scheme. Neither of them had any trading experience. Wiebe described the financial arrangements:

A … Mr. Fred Rempel had given Mr. Mitton money -- loaned money to Mike in the past from what I had understood, Mike Mitton, and from what I understood, Mr. Rempel – or Mr. Mitton was giving him advice to buy these stocks, but it was not expecting compensation back for it.
Q But would he have to pay for the loan back if it was successful, was it in lieu of paying back the loan?
A I would say that was implied, yes.

Wiebe believed that the loan was in the order of $20,000 to $50,000.

¶ 19 Around this time, Mitton also approached Edward Rempel – a distant cousin of Fred Rempel – with the proposed scheme. Edward Rempel had been introduced to Mitton by Barry Holmes, who was a lawyer and Edward Rempel's son-in-law. Edward Rempel had been a director of, and held shares in, his brother-in-law's VSE listed company but had little trading experience. Edward Rempel described his conversations with Mitton at that time:

A … [Mitton] said that he would be setting up a company for Fred Rempel, and he would – he would be – he said he and Barry Holmes would be a partner in this, and the idea was to sell stock to – on the Vancouver and Alberta Stock Exchanges, something that would be really like over a dollar a share, and he said most stocks would come down, so there would be a difference in the selling and buying price, and that would be the profit. He said that he had been involved in a company prior to this where the stocks – most of the stocks went down, so he lost quite a bit of money.

…

Q Did Mr. Mitton describe how he would pick the shares that you would use for a short-selling system?

A He said that they would be probably like highly traded and over a dollar a share.

Q And did he describe the process of how you would acquire these shares?

A Yeah. He suggested that we open up brokerage accounts and you would sell stock to one broker and buy it at the other firm.

Q At two different firms?

A Yeah, that's right.

Q Okay. And did he explain to you why it was necessary to do that at two different firms?

A Yeah. He suggested that it would be better to have – to sell it in one firm and it wouldn't be a good idea to buy it in the same firm if they didn't have the stock.

Q And did he indicate to you whether or not you would tell the firm where you were selling this stock, that you did not in fact own the stock?

A I can't remember him saying anything about that, but I remember that I was just going to come to the broker and tell him to sell a certain amount of stock, and that he would.

Q Was the idea that when you went back to buy the stock that the price of the stock would have decreased?

A Yes.

Q Did he ever explain to you what would happen if the price actually increased in value?

A Well, he suggested that he would sell at a higher price, then it would be in a sense averaging up, and eventually the stock would go down.

…

Q Did Mr. Mitton ever have discussions with you regarding sharing the potential profits in the short-selling system?

A Yes. He said that he and Barry would have two-thirds of the profits and Fred would have one-third.

Q What about in relation to yourself?

A He said that I would have 50 percent of the profits and he and Barry Holmes would split the other 50 percent.

¶ 20 Ultimately, four groups participated in Mitton's short sales scheme.

¶ 21 The first group was Fred Rempel and Wiebe. On Mitton's instructions, Fred Rempel opened accounts for Valley Ridge Investment Group Ltd., a company he

owned. He gave Wiebe trading authority over the accounts. Fred Rempel also gave Wiebe an office in a building he owned on Emerson Street in Abbotsford and paid Wiebe $2,500 to $3,000 per month to look after the trading in the accounts. These accounts were the:

- Valley Ridge account at Scotia McLeod;
- Valley Ridge account at Midland Walwyn Capital Inc.;
- Valley Ridge account at Canaccord; and
- Valley Ridge account at RBC Dominion Securities.

¶ 22 On Mitton's instructions, Wiebe also opened an account for Valley Ridge at Golden Capital Securities Ltd. Shortly after Wiebe opened the account on February 26, 1996, he signed a blank "Appointment of Attorney for Account" form, at Mitton's request. After Wiebe returned the form to Mitton, it was completed and the name "Mike Matt" inserted as attorney, with complete authority over the account. Wiebe did not know who completed the form. "Mike Matt" was a name used by Mitton. Wiebe placed no orders in the account. He learned several years later that all trades in the account had been made by Mitton directly with the dealer before Weibe had even signed the account opening documents.

¶ 23 The second group was that of Edward Rempel. He already had accounts in his name at Canaccord and Pacific International Securities Inc. and his son, Bruce Rempel, had an account at Golden Capital. Edward Rempel opened additional accounts in the names of Sandy Key Automotive Ltd., a company he owned, and Lakeside Concrete Ltd., a company in which he held shares. Consequently, Edward Rempel participated in Mitton's scheme through the following accounts:

- Edward Rempel account at Canaccord;
- Edward Rempel account at Pacific International;
- Bruce Rempel account at Golden Capital (through Edward Rempel's instructions to his son);
- Sandy Key account at Canaccord;
- Sandy Key account at Scotia McLeod; and
- Lakeside Concrete account at Midland Walwyn.

¶ 24 The third group was two brothers – David Jones Vernon and Leslie Bruce Vernon. They were friends and business acquaintances of Fred Rempel and Wiebe. They opened the following accounts:

- 509326 British Columbia Ltd. account at Canaccord;
- 506655 British Columbia Ltd. account at Canaccord; and

- 506655 BC account at C. M. Oliver & Company Limited.

¶ 25 The Vernon brothers were president and secretary of the two companies. Wiebe provided a guarantee on the first two accounts and had trading authority over the third.

¶ 26 The fourth group was that of Alfred Kaminski. He was chair of the Share Foundation, a foundation that Mitton had established, ostensibly to raise money for charities. Kaminski set up the following accounts:

- Alfred Kaminski account at Canaccord; and
- B. B. & H. F. Investment Corporation Ltd. account at Golden Capital.

¶ 27 Kaminski was the president of BB & HF. The directors were Kaminski, Barry Holmes and Janet Mitton (Mitton's wife). "Mike Matt" had trading authority over the BB & HF account.

¶ 28 Wiebe described how the trades were made:

> Q And how did you decide what to buy, what to sell?
> A Strictly through what Mike Mitton had called in to us.
> Q The idea was Mr. Mitton told you each day you to trade?
> A That's correct.
> Q Did he call you each day or every couple of days?
> A I was to be by the phone by six o'clock in the morning, and not leave it until about one-thirty in the afternoon and he would call in buys and sells on different accounts.
> Q On different accounts or different accounts in the name of Valley Ridge?
> A That's correct, different accounts in the name of Valley Ridge.

¶ 29 The Vernon brothers came into Wiebe's office at 6:00 or 6:30 in the morning as well. David Vernon took the calls from Mitton and received the instructions for his and his brother's accounts. Mitton also made all the decisions for the Edward Rempel accounts in relation to the short sales scheme.

¶ 30 Wiebe testified regarding the short sales in particular:

> Q And at the time did you know whether you owned the stock, like if he called you and said sell Indomin for example, would you in your mind know whether you already owned Indomin?
> A In most cases we would not own the stock.

Q If he tells you to sell usually it was to sell short?
A Yes.
Q And when he was telling you to buy, did you know whether that was --
A Sometimes it was buy back in a stock is that had already been sold.
Q And sometimes it was just to buy long because he thought it would go up?
A That's correct.

¶ 31 Once shares had been bought to cover a short sale in another account, they had to be transferred into that account. The holder of the account that had bought the shares would order the transfer by completing a Delivery Against Payment form or DAP. Wiebe would always complete these DAP forms on Mitton's instructions or simply sign blank forms that were completed by someone else on Mitton's instructions. Edward Rempel always did the latter.

¶ 32 At the end of each day, Mitton tabulated the day's activities. Wiebe described how this was done:

A … Mr. Mitton had asked that we get a written summary of the trades activity with each brokerage house at the end of the day so that he could enter it into his bookkeeping system, and so we would -- I would forward to him that information.
Q Okay. So you did – you did ask Scotia McLeod, Midland Walwyn and the other accounts we're going to look at, you did ask those brokers to send you sort of a recap at the of the day?
A Yes, exactly what was sold and what was bought.

¶ 33 Mitton monitored the daily trading by the Edward Rempel and Vernon brothers accounts as well.

¶ 34 In addition to reviewing daily trading reports from the accounts, Mitton monitored market trading in the shares. In late January or early February 1996, Mitton moved into an office in the same building as Fred Rempel and Wiebe, on Emerson Street in Abbotsford. Mitton had four or five stock trading monitors in that office, which he used to track trading on the VSE, the Toronto Stock Exchange and the Montreal Exchange and, possibly, in the US as well.

¶ 35 At about the same time that Mitton moved into the Abbotsford office, some of the dealers holding the Valley Ridge accounts were raising concerns with Fred Rempel and Wiebe. Wiebe discussed these concerns with Mitton:

Q And what did he say?
A He was always passing along information to send back to them [the dealers] as to how everything was being settled and looked after, and but to encourage the trading to continue.

¶ 36 Finally, in early February, Fred Rempel told Wiebe to stop all trading in the Valley Ridge accounts. Wiebe understood that Fred Rempel was tired of getting calls from dealers about the trading in the accounts. Wiebe stopped placing orders in the accounts. Despite this, during February there were 13 undeclared short sales in the Golden Capital account and seven undeclared short sales in the Canaccord account. Wiebe subsequently learned that Mitton had given the instructions for the short sales in the Golden Capital account. He believed that Mitton did the same in respect of the Canaccord account.

¶ 37 Between December 14, 1995, and February 19, 1996, there were 191 undeclared short sales in the accounts of the four groups. No margin was ever deposited for the sales. In each case, the short sale was settled through the subsequent purchase of the shares. If the share price had dropped, Mitton would arrange for the shares to be purchased in another account and transferred into the short account. If the share price had risen, Mitton and his group would not purchase the shares; the dealer would have to buy the shares to cover the short position. Commission staff were unable to determine if any dealers suffered a loss on any accounts.

The bond trading scheme

¶ 38 As Mitton's short sales scheme was winding down, his bond trading scheme got underway. Indeed, some of the 191 undeclared short sales referred to above played an integral role in the bond trading scheme.

¶ 39 Edward Rempel described the inception of the scheme:

A … Mike Mitton suggested to me that he would like to trade bonds, he said that it would be quite safe because he would call it a straddle, just where you buy and sell and it would lessen the risk. So he set up a meeting at my house with Ben Oxholm [of Golden Capital], and so at the meeting it was attended by Barry Holmes, Mike Mitton and myself and Ben Oxholm and Fred Rempel. And it was called to discuss bond trading, the meeting was called to discuss bond trading.

…

Q And at the meeting itself, what was Mr. Mitton's level of participation at the meeting.
A Well, he was – he was discussing this with Ben Oxholm, and the rest of us didn't get involved much in the conversation.

Q And at the conclusion of the meeting you decided to participate in the bond trading?
A Yes.
…
Q What was – was Mr. Mitton – did he present himself as a person who would be in charge of making decisions regarding the bond trading?
A Yes.

¶ 40 Goldon Capital eventually sued Mitton and others to recover the losses it incurred in connection with the bond trading scheme. The trial was held in 2001 and 2002, and the reasons for judgment issued on October 22, 2002: *Golden Capital Sec. Ltd. v. Holmes et al* 2002 BCSC 1468. In his reasons, Edwards J. summarized Oxholm's testimony about this initial meeting:

> [122] Ben Oxholm testified he was led to believe that Michael Mitton (whose true identity he did not then know) was acting as trader for a group of 17 or 18 substantial investors, including Edward Rempel, who Ben Oxholm knew by reputation was a millionaire Abbotsford businessman and that the group was interested in trading in bonds, Ben Oxholm's specialty. Ben Oxholm further testified that he was led to believe that putting up the necessary margin for trades would be "no problem" for the group.
>
> [123] Ben Oxholm based these beliefs in part on what he was told at a meeting he had with Edward Rempel, Alfred Rempel, Michael Mitton and Barry Holmes at Edward Rempel's impressive Abbotsford condominium on February 12, 1996. …

¶ 41 The next day, Oxholm began to prepare account opening forms for Lakeside Concrete, BB & HF and Valley Ridge. Before he could complete the forms, Oxholm received a call from Mitton. Edwards J. summarized what happened next:

> [125] Ben Oxholm was persuaded by Michael Mitton to buy substantial positions in Canada bonds before account opening forms had been completed for Lakeside, BB & HF and Valley Ridge. Michael Mitton persuaded Ben Oxholm that margin would be provided by short sales in those accounts and began to order undeclared short sales, which gave the appearance of credits in the accounts which could stand as margin. The undeclared short sales ultimately amounted to over $1 million, of which over $310,000 were "covered" by DAP from North Shore's [North Shore Aggregates Ltd. was a company controlled by Holmes] Midland Walwyn account by Barry Holmes.

[126] The bond purchases and short sales of shares all took place within six days between February 13 and 19, 1996, which included a weekend. During that short time, the price of the bonds took an unanticipated precipitous decline. Golden Capital was required to pay for them on their respective settlement dates at the higher trade date purchase prices. What briefly appeared to be credits in the accounts, which could have stood as margin to protect Golden Capital on the bond purchases, were not in fact credits because the undeclared short sales were "covered" by DAP. That meant the shares necessary to cover the undeclared short sales had to be paid for by Golden Capital, leaving no credits to act as margin on the bond trades.

…

[190] When it became apparent to Golden Capital that the bond purchases would not be covered by margin from the short sales of shares in the BB & HF and Valley Ridge accounts, the bonds were sold at a loss. Unfortunately, the sales coincided with a fall in bond prices almost as bad as the worst Ben Oxholm had seen in ten years. …

[191] Ben Oxholm testified about his decision to sell the bonds:

> Well, I have a machine that shows when the accounts are under margined or how much margin they have. There wasn't any margin to carry this. I was aware that the stocks were being DAP'd in, but it was just wasn't working. So, I said, "You know, we're going to have to sell this bond."
>
> Q Who did you say that to?
>
> A To Michael Matt when he called me. He said, "What are the bonds doing, " and I said, "They're going down." And I said, "You should really cut your losses right here." "No", he said, "I don't want to do it." And that was on the Monday I believe.
>
> Q Monday was the 19th?
>
> A Yeah, the 19th. Because the bonds were in, the bond market was in turmoil. And he said, no, he didn't want to sell them and he said, "The margin, it will all be coming in." I think I gave him one day and then sold it on the 20th. It wasn't as bad but I couldn't carry the previous one that I had sold over the weekend. But one day it seemed fair to see if it

> would, if I could get additional margin, but it wasn't showing up. It was totally under margined. So he got sold out. He wasn't happy about it, but that's the way it is.
>
> …
>
> [195] The ultimate results of all the bond and share trades which were ordered by Michael Mitton between February 9 and 16, 1996, and subsequent bond sales and share buy ins were net losses of $177,989 in the Lakeside account, $715,202 in the BB & HF account and $38,733 in the Valley Ridge account, for a total of $931,924.
>
> [196] All trades ordered by Michael Mitton took place before the account opening documentation for these three accounts was completed, so Ben Oxholm and Golden Capital had undertaken all these trades without signed documents disclosing who the directors of BB & HF, Valley Ridge and Lakeside were, without written authorization for Michael Mitton to trade on behalf of those companies, without credit checks and without personal guarantees.
>
> …
>
> [205] There is no doubt that Michael Mitton committed fraud to obtain credit when he misrepresented to Ben Oxholm that margin for the bond purchases on behalf of Lakeside and BB & HF would be provided through the undeclared short sales of shares he instructed Ben Oxholm to make on behalf of BB & HF and Valley Ridge. The fact Ben Oxholm, in hindsight, acted unwisely is no defence. A person may believe and rely on lies told to him with intent to deceive. The law will not preclude recovery for being duped. …

¶ 42 Mitton orchestrated the purchase of Government of Canada bonds in the Lakeside and BB & HF accounts at Golden Capital. Both accounts were left with a debit balance. Edward Rempel paid the debit in the Lakeside account. Edwards J. found Mitton, Holmes, Fred Rempel, Wiebe, Valley Ridge, BB & HF and North Shore jointly and severally liable to Golden Capital for the losses in the BB & HF ($715,202) and Valley Ridge ($38,733) accounts.

The share purchase scheme

¶ 43 In December 1995, Mitton had hired George Ronald Stephens as a sales manager for the Share Foundation. Stephens had left grade 12 to join the navy and, since 1966, had been involved in sales. He had little trading experience.

¶ 44 In early 1996, the Share Foundation office moved into the Emerson Street office in Abbotsford. Mitton, Wiebe and Stephens worked there. Kaminski and Holmes would visit the office from time to time.

¶ 45 Stephens understood that, at that time, Wiebe was trading shares for Mitton and on behalf of a group of Abbotsford businessmen. Stephens did not know the identity of these businessmen.

¶ 46 In February or March, Mitton asked Stephens if he would take over Wiebe's role. Stephens testified about a discussion he had with Mitton and Holmes about Mitton's request:

> Q … Were you aware that Mr. Mitton had a trading ban?
> A Yes, I was.
> Q Okay. And did you -- did you have any discussions with Mr. Holmes regarding the trading ban?
> A Yes. When Mitton came to me and said that he wanted to do what Charles was doing, Barry Holmes was there, and Barry said you know that Mike can't trade, but he can advise this group of Abbotsford business people.
> Q So based on what Mr. Holmes said, you felt it was legal, if you will, for you to --
> A That's right.
> Q -- participate in the trading?
> A That's right.

¶ 47 Mitton instructed Stephens to open accounts at several dealers, in the name of a company rather than his own. As Stephens explained it:

> A Well, Mitton sent me over to Barry Holmes' office to -- his was just a numbered company off the shelf that he had, and then we started off with a numbered company and then changed it to Mill Creek Capital.

Stephens was the president of Mill Creek but did not own any shares in the company. The corporate records in evidence show Holmes as Mill Creek's sole shareholder.

¶ 48 Between April and June, Stephens opened accounts for Mill Creek at several dealers, including:

- Midland Walwyn;
- Coleman & Company, in Arizona; and
- RBC Dominion, in Alberta.

Stephens understood that these accounts were for the benefit of Mitton and his group of Abbotsford businessmen.

¶ 49 Stephens essentially took over the tasks that had been performed earlier in the year by Wiebe. Acting on Mitton's instructions, Stephens arranged for daily trading reports on the Midland Walwyn account, which he gave to Mitton. Stephens used a computer to follow trading in certain shares identified by Mitton. Stephens received calls from Mitton at 6:30 in the morning; Mitton wanted to know what was going on in the market. Stephens traded the Mill Creek accounts exclusively on Mitton's instructions. Stephens signed letters, cheques and share transfer documentation prepared on Mitton's instructions.

¶ 50 Stephens was also involved in the management of the Kaminski account at Canaccord:

> Q You mentioned the Kaminski account at Canaccord. Did you have -- what deals did you have in relation to that account?
> A Mitton would phone me every morning at six-thirty and instructed me to phone Brad Scharfe at Canaccord and have him fax the reports every day.
> Q Did you only deal with Mr. Scharfe or somebody else?
> A He had two assistants, one woman and one fellow.
> Q And did you have -- did he ask you to convey any information to Kaminski in regards to the Kaminski account at Canaccord?
> A Sometimes he would tell me to phone Kaminski and tell him to sell such and such, or to tell Kaminski to go down to Canaccord and pick up a cheque at one o'clock.
> Q Did he ask you to prepare any documents in relation to the Kaminski account at Canaccord?
> A He asked me to do up a bunch of IMMs [a form requesting an Inter Member Movement – a method of transferring shares from one account to another, similar to a DAP] and have Kaminski sign them regarding the Canaccord account.

¶ 51 Stephens also described the history behind a trust agreement signed by Kaminski on April 13, 1996, in which Kaminski stated that Mill Creek was the beneficial owner of the Canaccord account in his name:

Q Have you seen this document [the trust agreement] before?
A Yes.
Q Can you explain how it came to be?
A Well, Holmes and Mitton were in the office, and one day I said to -- because I got the status report every day from the Kaminski account and the trading that I was doing on the account that I had, I was always concerned about it, and I knew that if money was needed it came from the Kaminski account, so I said to Holmes and Mitton what happens if Al Kaminski drops dead because he was older than me, he wasn't in good health, and it was like the lights went out, and they both realized and, hey, if he did drop dead this account would be gone and his family would get that account. And so Barry did this agreement up in one day and I had it signed either that day or the next day, I can't remember.
Q Barry being Barry Holmes?
A Barry Holmes, yeah.
Q And you thought that the Kaminski account would assist in covering any of the trades that were made in the Mill Creek accounts?
A That's right.

¶ 52 In fact, there were significant debits to be covered in most of the Mill Creek accounts, as well as in other accounts with which Mitton was involved. To make it appear that these debits would be covered, Mitton instructed Stephens and Kaminski to transfer shares between accounts and to issue cheques to dealers, none of which were honoured. Most were returned due to insufficient funds; Mitton ordered a stop payment on others; one was written on a non-existent bank account.

¶ 53 On December 21, 2000, Mitton pleaded guilty in BC to six counts of fraud in connection with his share purchase scheme. Counts 1 and 2 involved the Mill Creek and Harris McLean Financial Group Ltd. accounts at Midland Walwyn (Harris McLean was an investment firm in the Cayman Islands that Mitton dealt with; Richard Harris was a principal of the firm). Count 3 involved the Mill Creek account at Coleman. Count 4 involved the Mill Creek account at RBC Dominion. Count 5 involved an account in the name of Collegiate Investments Limited at Standard Bank Stockbrokers (Isle of Man) Limited, another account for which Mitton had given all the trading instructions. Count 6 involved the Share Foundation.

¶ 54 Count one is representative of the five counts involving dealers. It alleges that Mitton, "by deceit, falsehood or other fraudulent means did defraud Midland Walwyn Capital Inc. … ("the Brokerage Firm") … by causing an account ("the

Account") in the name of Mill Creek Capital Corp. ("the Account Holder") to be established at the Abbotsford branch at the Brokerage Firm and by directing the affairs of the Account Holder so as to cause trades of securities to be made in the Account, knowing that the Account Holder lacked the ability or good faith intention to pay amounts arising and owing from such trades …" Count 2 made the same allegation in respect of the Harris McLean account at Midland Walwyn's Abbotsford office.

¶ 55 Midland Walwyn sold out the shares in the two accounts and was able to cover the debits. The other three dealers defrauded by Mitton were not so fortunate; despite selling out the accounts, each lost a significant amount.

¶ 56 On December 27, 2000, Mitton was sentenced to four years imprisonment. He was also ordered to pay restitution of $2,255,875 to the three dealers and to the salesmen he had dealt with at Coleman and RBC Dominion, each of whom had had to personally cover part of his firm's loss.

The H & R scheme

H & R Enterprises

¶ 57 The last of Mitton's four investment schemes began later in 1996. Mitton asked Wiebe to become president and general manager of a company called Capital Hill Ventures Ltd., which operated vending machines in the Lower Mainland. Wiebe agreed. In December 1996 or January 1997, Mitton and Wiebe moved their office from Emerson Street to Paramount Crescent in Abbotsford. That January, Mitton approached Weibe with a proposal respecting Capital Hill. Wiebe described Mitton's proposal:

> A Mr. Mitton felt that it needed capital, to be able to have Capital Hill Ventures grow, and was going to purchase or obtain a shell company in the States for NASDAQ, from NASDAQ I guess, and asked me if I would go down to Las Vegas, meet a person down there by the name of Peter Berney, to, to have a company picked up, selected, and, and then start trading with it, so.
> Q And you did that? You went to Las Vegas?
> A I did go to Las Vegas and did do that.

¶ 58 The shell company was H & R Enterprises Inc. H & R was incorporated in the US. It had no operating business and no assets. H & R's directors were not involved in the company's affairs. It was not a reporting issuer in BC. Its shares were quoted on the National Association of Securities Dealers Over-the-Counter Bulletin Board in the US.

¶ 59 The OTC BB is a quotation medium rather than a stock exchange. Market makers in an issuer's shares publish their bids (the price at which they are prepared to buy the shares) and asks (the price at which they are prepared to sell the shares). The trades are usually executed by phone; broker dealers call one another to buy or sell.

¶ 60 Wiebe characterized himself as the "middle person" in the negotiation with Berney. Eventually, Mitton spoke directly to Berney and they struck a deal for the purchase of 3,728,000 of the 4 million outstanding H & R shares. Wiebe put the share certificates in an envelope, brought them back and gave them to Mitton.

Market makers and promoters

¶ 61 Once Mitton had the shares of H & R in hand, he set up an extensive network of market makers and promoters. H & R had three market makers for its shares.

¶ 62 The first was J. Alexander Securities Inc. J. Alexander was registered as a broker dealer in the US, with four offices in California and one in Florida. Mitton dealt with Jerome Rosen. Rosen was a trader in the Florida office and one of J. Alexander's top revenue producers. Rosen was first registered in the US in 1975 and worked at nine firms before joining J. Alexander in 1995. He has never been registered under the Act.

¶ 63 Rosen had a disciplinary history. In 1980, he settled with the US Securities and Exchange Commission in a matter involving the distribution of unregistered securities during 1976 and 1977; Rosen was suspended from associating with any broker or dealer for 14 days and placed under supervision for two years. In 1985, Rosen settled with the NASD in connection with a scheme involving the purchase of mutual funds at prices substantially below their redemption value; he was censured, suspended from associating with any NASD member for 30 days and fined $30,000. In 1992, Rosen settled with the NASD in a case alleging that he fraudulently marked up principal retail sales by between 20% and 45% over market price during a public offering of securities; Rosen was censured and fined $5,000.

¶ 64 Once Rosen was involved with H & R, he set up two accounts in the name of OTCBB Holdings Ltd. One account was at McDermid St. Lawrence Securities Ltd. The other was at Harris McLean; Harris McLean then opened an account at Georgia Pacific Securities Corporation on behalf of OTCBB Holdings. The account documentation at McDermid indicated that the president of OTCBB Holdings was Juliana Frisselli. Frisselli is Rosen's daughter and was around six years old in 1997. The McDermid documentation also included a letter in which Rosen stated that he had "power of attorney" for OTCBB Holdings.

¶ 65 The second market maker was Equitrade Securities Corporation. Equitrade was registered as a broker dealer in the US. The trader responsible for H & R shares was Tim Chamberlain in California.

¶ 66 The third was Saperston Financial, Inc.,which was also registered as a broker dealer in the US. Robert Prager, of the firm's Florida office, was responsible for trading H & R shares.

¶ 67 H & R had several promoters. Its lead promoter was Alexander Troy Consultants, Inc. of Florida. The president and chief executive officer of Alexander Troy was David Scott Heredia. He had been registered in the US as a securities salesman from 1993 to 1996. In 1996, the Commissioner of Securities in Georgia found that Heredia had committed, among other things, misrepresentation and fraud. The Commissioner revoked Heredia's registration in Georgia and barred him from associating with any dealers or advisers registered in Georgia. The NASD and the SEC also disciplined Heredia in respect of these activities. In 1998, the NASD barred Heredia from associating with any NASD member in any capacity. In 2000, the SEC barred him from associating with any broker or dealer and from participating in any offering of penny stock. Heredia has never been registered under the Act.

¶ 68 Alexander Troy and H & R signed a "Consultant Agreement" on July 4, 1997. Alexander Troy agreed to "provide consulting services in connection with the Corporation's [H & R's] "public relations" dealings with NASD broker/dealers and the investing public." The agreement set out several specific services to be provided, including to "aid and advise the Corporation in establishing a means of securing nationwide interest in the Corporation's securities" and to "aid and consult the Corporation in the preparation and dissemination of press releases and news announcements." H & R agreed to pay the following compensation for these services:

- 1,744,000 free trading shares of H & R; and
- "*Performance Bonus on an Added Value Basis*
  Options are as follows if bid price is maintained for 3 consecutive days:
  $1.00 bid Consultant option for 50,000 common shares @$0.05
  $1.50 bid Consultant option for 50,000 common shares @$0.05
  $2.00 bid Consultant option for 50,000 common shares @$0.05
  $2.50 bid Consultant option for 50,000 common shares @$0.05"

¶ 69 H & R had at least eight other promoters. They were located in Vancouver, Toronto, Florida and other cities in North America.

¶ 70 Mitton's next step was to get the H & R shares into the hands of these promoters. Mitton gave 3,052,000 shares to Richard Harris, who deposited them into inventory at Harris McLean. On Mitton's instructions, Harris then transferred the shares to the promoters. These transfers included 1,744,000 shares to Alexander Troy, as per the Consultant Agreement. Harris also transferred 180,000 shares to Rosen's OTCBB Holdings account at McDermid. Rosen received the shares in exchange for making a market in H & R shares. Later, on September 24, Rosen received an additional 70,000 shares from a company controlled by Heredia and his associates.

News releases

¶ 71 With his market makers and promoters in place, Mitton turned his attention to H & R's public disclosure. Between February and August 1997, H & R issued several news releases, including the following.

¶ 72 On April 21, H & R announced that Harris McLean would act as broker for a private placement of 2 million shares and warrants for US$1 million. The private placement never took place.

¶ 73 On June 2, H & R announced that it had purchased all the outstanding shares of Capital Hill for $475,000 cash. The news release said that Capital Hill had over 400 vending and arcade game machines in BC and annual net revenue of approximately $2.2 million. There is no evidence that H & R paid $475,000 cash for Capital Hill shares; H & R had no assets of any kind at the time. As well, Wiebe confirmed that, in mid 1997, Capital Hill had only 150 to 200 vending and arcade game machines in circulation and negative net revenue.

¶ 74 On June 11, H & R announced the launch of a cross-Canada chain of cigar stores, with the first store opening in Vancouver in June. No cigar stores were ever opened.

¶ 75 On July 24, H & R announced that it had purchased all the real estate assets of a golf course development called Quail Ridge. The news release said that the assets had a net market value of $60 million and should generate annual after-tax earnings of $10 million. In fact, H & R had agreed to acquire certain interests in Quail Ridge, but no real estate assets.

¶ 76 On August 8, H & R announced that it had acquired all the outstanding shares of Cool-Ex International Inc. The news release said that H & R would have exclusive North American distribution rights for a patent refrigerant approved by the Environmental Protection Agency and Environment Canada. On August 13, H & R announced that the refrigerant had been tested on cars with a 100% success rate and projected the potential annual revenue for the product at $128 million for cars

and $160 million for commercial vehicles. In fact, Cool-Ex was a non-exclusive distributor of certain refrigerants produced by another company, but none of these products had EPA or Environment Canada approval.

¶ 77 Wiebe knew when news releases were coming out, but was not involved in their preparation:

> Q How did you know they were coming out?
> A Mr. Mitton would state that we have another press release and he would be watching the market very closely every time a press release was -- had come out.

Nominee accounts

¶ 78 In addition to his stable of market makers and promoters, Mitton had several nominees, including four people who worked in the H & R office on Paramount Crescent – Wiebe, Elizabeth Anne Moxon, Leslie Gmur and Katherine Nicole Hanna.

¶ 79 Wiebe set up five accounts to trade H & R shares, including accounts in the name of:

- Wiebe at Equitrade;
- Key West Realty Ltd. at Wolverton Securities Ltd.;
- Inland Ranch Company Ltd. at Midland Walwyn;
- 1194710 Ontario Ltd. at Midland Walwyn; and
- 512617 BC Ltd. at Midland Walwyn.

¶ 80 Moxon had no trading experience. She set up four accounts in her name, at Wolverton, Midland Walwyn, Canaccord and Dominick & Dominick.

¶ 81 Gmur also had no trading experience. She set up two accounts in her name, at Wolverton and Canaccord.

¶ 82 Hanna set up an account in her name at Wolverton.

¶ 83 Weibe testified that he, Moxon, Gmur and Hanna understood that they were setting up these accounts (the “nominee accounts”) for the benefit of H & R:

> Q And you understood that the accounts were to raise money for H & R itself?
> A That is correct.
> Q And who gave the instructions on those accounts?

A Mr. Mitton.
Q And those instructions included buying and selling shares?
A That is correct.
Q And did it include withdrawing money from the accounts?
A Yes, it did.
Q And if that was done, what was done with the money?
A We would receive instructions from Mr. Mitton and either the checks issued would be written to Mr. Mitton or to other accounts that he named.

¶ 84 Harris McLean also acted as a nominee for Mitton. Harris McLean set up the following accounts:

- an account in the name of Harris McLean at Quaker Securities Inc. in Pennsylvania;
- three accounts in the name of Harris McLean and one account in the name of Ana Jiminez (Harris' mother) at Georgia Pacific;
- an account in the name of Harris McLean and an account in the name of Paradigm Investments Ltd. at Dominick & Dominick;
- an account in the name of Harris McLean at Canaccord; and
- an account in the name of Harris McLean at Pacific International.

¶ 85 Harris confirmed in his agreed statement of facts that he allowed Harris McLean to act as a nominee for Mitton and that all the trading of H & R shares in these accounts was done on the instructions of, and for the benefit of, Mitton.

¶ 86 That had been Weibe's understanding as well:

Q And was your understanding that Mr. Mitton was giving directions -- trading instructions directly to Harris McLean?
A He was certainly dealing directly with everyone involved, yes.
Q Everyone involved, what do you mean by that?
A Whether it would be the market makers, promoters, any trades that were being done, Mr. Mitton was, was in contact with them.

Private placements

¶ 87 During July, August and September 1997, H & R issued 2,975,000 shares to promoters and Mitton nominees in three private placements.

¶ 88 On July 29, H & R issued 500,000 shares at US$.01 per share to Berney and two of H & R's promoters.

¶ 89 On August 11, H & R issued 475,000 shares to H & R's lawyer in Las Vegas, Weibe, Key West, Gmur and Hanna. The lawyer received 20,000 shares; the others received 113,750 shares each. None of the BC placees paid for their shares.

¶ 90 On September 15, H & R issued 2 million shares to Key West, Inland Ranch, 1194710 Ontario, 512617 BC, Moxon, Gmur and Hanna. 512617 BC received 200,000 shares; the others received 300,000 shares each. None of the placees paid for their shares.

¶ 91 Weibe and his companies, Moxon, Gmur and Hanna put the shares they received into the nominee accounts.

¶ 92 H & R did not file a prospectus or rely on an exemption from the prospectus requirement for any of these share issuances.

Trading in H & R shares

¶ 93 From January to June 1997, the trading in H & R shares was flat, hovering at or close to 0. There were days when there was some activity, but only one day during those six months when daily volume even approached 1 million shares.

¶ 94 The price during that period was similarly unremarkable. There were a few trades between US$5.00 and US$2.00 in the first three months of the year, but the price settled down around the US$1.00 mark by the end of March and declined gradually to around US$.50 by the end of June.

¶ 95 Everything changed suddenly in mid-July. On Friday, July 18, the price doubled from the previous day to US$1.09, on a volume of almost 1 million shares. By the following Wednesday, July 23, the price closed at slightly over US$2.00 on a volume of over 1.4 million shares. The price jumped to US$2.40 on July 24, the day the Quail Ridge news release was released. By July 29, the date of the 500,000 share private placement, the share price had fallen off somewhat to US$2.25.

¶ 96 The August 8 and 13 news releases announcing the Cool-Ex deal had little effect on the market. On August 11, the date of the 475,000 share private placement to Mitton's nominees, the share price closed at US$2.31 on a volume of around 2.28 million shares. Aside from a spike on August 25 to US$3.15, the price hovered around US$2.25 throughout the remainder of the month, with volumes generally well under 1 million shares.

¶ 97 These prices and volumes continued during the first half of September. On September 15, for example, the day of the 2 million share private placement to Mitton's nominees, H & R shares closed at US$2.12 on a volume of around

100,000 shares. Then, on Friday, September 19, trading volume more than doubled from the day before, to 1.13 million shares.

¶ 98 On Monday, September 22, the price closed at US$2.71 on a volume of 1.5 million shares. On Tuesday, September 23, the price closed at US$3.53 on a volume of 5.8 million shares. Wednesday, September 24 saw a volume of 12.4 million shares, while the price closed at US$6.09.

¶ 99 During those three days, one of J. Alexander, Equitrade or Saperston was involved in 64% of the trades. They frequently traded between themselves, as well as with other American or Canadian dealers. J. Alexander and Saperston, in particular, bought heavily. To attract sellers, they had to keep increasing their bids. During those three days, the "inside bid" for H & R shares increased 175%; the inside bid is the highest of the bids quoted by all the market makers in the shares. J. Alexander was responsible for 41% of the increases in the inside bid during this time, while Saperston was responsible for 51%.

¶ 100 H & R's share price actually reached its peak on September 25; at one point that day, H & R's shares traded at US$6.68. By the end of that day, however, the price had fallen to US$3.78, on a volume of around 6.2 million shares. By the end of the next day, Friday, September 26, the price was US$2.03 and volume had dropped to 2.5 million shares.

¶ 101 Volume remained strong during the early part of the following week, at over 1 million shares per day, but the price continued to drop. On Friday, October 3, the price closed at US$1.43 on a volume of around 600,000 shares. Both price and volume continued to decline throughout October. On October 31, H & R shares closed at US$.52, on a volume of 73,200 shares.

¶ 102 All three of H & R's market makers took their instructions from Mitton, Heredia or both. Apparently, there was some delineation of responsibility between the two of them when it came to directing the traders at J. Alexander, Equitrade and Saperston. William Park, who testified regarding the NASD's investigation in this matter, described the arrangement:

> … from the testimony that we obtained, Mr. Prager, who was with Saperston, he dealt, from what we could tell, directly with Mr. Heredia, and Mr. Chamberlain I believe dealt with either Mr. Heredia and Mr. Mitton, and I believe Mr. Rosen testified that he dealt with Mr. Mitton. However, we do see phone records between Mr. Rosen or J. Alexander Securities and Mr. Heredia as well.

The aftermath

¶ 103 Mitton's nominees were able to sell a large number of H & R shares at the inflated price. Wiebe and his companies, Moxon, Gmur and Hanna received over $6 million from the nominee accounts. All this money was paid to, or at the direction of, Mitton.

¶ 104 Heredia made a profit of over $1.1 million in an account that Alexander Troy had at Equitrade.

¶ 105 Rosen made a profit of over $750,000 in his two OTCBB Holdings accounts. He made additional profits from making a market in H & R shares.

¶ 106 Saperston went out of business due to the losses it sustained trading H & R shares. The shares it was left holding cost US$8,833,647. After deducting sales proceeds and recoveries from settlements, Saperston's net loss was US$2,791,332.

¶ 107 On August 27, 2001, the NASD issued a complaint against J. Alexander, James Alexander, Rosen, Chamberlain and Prager in respect of H & R. The complaint made a variety of allegations against Rosen including:

- market manipulation, or aiding and abetting market manipulation;
- engaging in wash trades;
- engaging in transactions in accounts without proper notification;
- failing to testify truthfully; and
- attempting to destroy requested books and records.

¶ 108 In September 2002, Rosen filed for bankruptcy. This automatically stays the NASD proceeding against Rosen until the Bankruptcy Court either lifts the stay or completes the bankruptcy proceedings. The stay was still in place at the time of the NASD hearing in September and October 2002. The hearing panel concluded that Prager had been unaware of Mitton's scheme and therefore was not liable for market manipulation. They did find Prager liable for failing to investigate red flags that may have indicated trading violations and fined him US$5,000. They found J. Alexander and Alexander, its president, liable for failing to establish and maintain an adequate supervisory system. They fined the firm US$200,000, ordered it to hire a consultant to recommend and implement new supervisory procedures in its Florida office, ordered it to suspend its market making activities for 60 days or until the implementation of the new supervisory procedures, and assessed costs. The panel fined Alexander US$200,000, suspended him for two years in all capacities, required him to requalify as a principal, and assessed costs. Chamberlain settled before the hearing and was barred from associating with any NASD member in any capacity.

¶ 109 Finally, in January 2004, Heredia and Rosen pleaded guilty in the US to a charge of conspiracy to commit securities fraud and wire fraud, and to a charge of fraud in the purchase and sale of H & R securities. Heredia admitted that he paid off brokers, that he received shares and that he directed buying and selling in H & R shares to try to show volume to increase the price. Rosen admitted that he received shares and that he assisted in pushing up the price by showing volume. We have no evidence respecting the sanctions that were imposed on Heredia and Rosen.

Findings

Mitton

¶ 110 The current Act came into force on April 21, 1997. From 1995 until that date, the applicable legislation was the *Securities Act*, SBC 1985, c. 83 (the "former Act").

¶ 111 The four notices of hearing allege that Mitton:

- acted as an adviser without being registered, contrary to section 20 of the former Act (short sales and share purchase notices);
- while placing orders for the sale of securities either directly or through his nominees, failed to declare that neither he nor his nominees owned the securities, contrary to section 41 of the former Act (short sales notice);
- participated in schemes that he knew or ought reasonably to have known perpetrated a fraud on persons in BC, contrary to section 41.1 of the former Act (short sales, bond trading and share purchase notices);
- traded without being registered through Wiebe, Moxon, Gmur and Hanna in the nominee accounts, contrary to section 20 of the former Act and section 34 of the Act (H & R notice);
- traded the shares of H & R without a prospectus or a prospectus exemption under circumstances where the trades were deemed distributions pursuant to section 140 of the *Securities Rules*, BC Reg 479/95, contrary to section 42 of the former Act and section 61 of the Act (H & R notice); and
- participated in transactions that he knew or ought to have known would contribute to a misleading appearance of trading activity or artificial price for the shares of H & R, contrary to section 41.1 of the former Act and section 57 of the Act (H & R notice).

Unregistered advising

¶ 112 Commission staff allege that Mitton acted as an adviser without being registered, contrary to section 20 of the former Act (short sales and share purchase notices).

¶ 113 Section 20(1)(c) of the former Act stated:

> 20(1) A person must not
> …
>
> (c) act as an adviser unless the person is registered in accordance with the regulations as
> (i) an adviser, or
> (ii) an advising employee, partner, director or officer of a registered adviser and is acting on behalf of that adviser.

¶ 114 An "adviser" was defined in section 1(1) of the former Act:

> "adviser" means a person engaging in, or holding himself out as engaging in, the business of advising another with respect to investment in or the purchase or sale of securities or exchange contracts;

¶ 115 Section 8(a) of the Rules states:

> 8. A person registered as an adviser must be classified in one or more of the following categories:
>
> (a) *portfolio manager:* a person that manages or holds itself out as managing the investment portfolio, consisting of securities, exchange contracts or both, of one or more clients through discretionary authority granted by the clients;

¶ 116 The Commission considered the definition of "adviser" in *Re Robert Anthony Donas*, [1995] BCSC Weekly Summary 14. The Commission stated at page 45 that:

> … the nature of the information given or offered by a person is the key factor in determining whether that person is advising with respect to investment in or the purchase or sale of securities. A person who does nothing more than provide factual information about an issuer and its business activities is not advising in securities. A person who recommends an investment in an issuer or the purchase or sale of an issuer's securities, or who distributes or offers an opinion on the investment merits of an issuer or an issuer's securities, is advising in securities. If a person advising in securities is distributing or offering the advice in a manner that reflects a business purpose, the person is required to be registered under the Act.

¶ 117 Mitton recommended the purchase and sale of securities to the four groups who participated in his short sales scheme. Mitton told Wiebe, Edward Rempel and the Vernon brothers which securities to buy and which to sell. Mitton, under the name "Mike Matt", had trading authority over the Valley Ridge and BB & HF accounts at Golden Capital. Wiebe, Fred Rempel and Edward Rempel had little or no trading experience; they followed Mitton's recommendations without question.

¶ 118 Mitton provided his advice in a manner that reflected a business purpose.

- Mitton solicited participation in his short sales scheme. He approached Fred Rempel and Edward Rempel.

- Mitton was paid by the participants for his advice. He had profit sharing arrangements with Fred Rempel and Edward Rempel.

- The short sales scheme involved significant trading. There were four groups of participants. Participants were told to set up not one, but several accounts. In all, 16 accounts were involved in the scheme. These accounts made 191 undeclared short sales over a ten week period. There was so much going on in the accounts that Fred Rempel paid Weibe a monthly salary of $2,500 to $3,000 to manage his trading for him.

- Mitton directed all aspects of the participants' trading activity. He told them what to buy and sell, when and how to transfer shares from one account to another, and what to tell the dealers if they raised concerns.

- Mitton ran the short sales scheme like a business. Wiebe was required to be by the phone from 6:00 to 1:30 every day to receive instructions; the Vernon brothers came to Wiebe's office for instructions as well. Mitton received written trading summaries from each dealer at the end of each day. He would then enter that information into his bookkeeping system. Mitton would also monitor trading in the markets; he had four or five trading monitors in his office.

¶ 119 The share purchase scheme appears to have been a continuation of the short sales scheme, albeit with a different focus. That is certainly how Stephens saw the situation – he understood that Wiebe had been trading for Mitton on behalf of a group of Abbotsford businessmen and that he, Stephens, would be taking over Wiebe's role. Holmes specifically told Stephens that "Mike can't trade, but he can advise this group of Abbotsford business people." We are satisfied that the

company set up to do the trading, Mill Creek, was owned at least in part by persons other than Mitton.

¶ 120 Stephens set up the Mill Creek accounts on Mitton's instructions. The accounts were managed in the same fashion as those involved in the short sales scheme. Stephens bought and sold shares in the accounts exclusively on Mitton's instructions. He signed letters, cheques and share transfer documentation that had been prepared on Mitton's instructions. He arranged for Mitton to receive daily trading reports and was by his phone by 6:30 in the morning to receive Mitton's calls. He used a computer to monitor trading in certain shares identified by Mitton. He conveyed instructions from Mitton for Kaminski's Canaccord account. Like Wiebe, Fred Rempel and Edward Rempel, Stephens had little trading experience. He did exactly what Mitton told him to do.

¶ 121 We find that Mitton was engaging in, and holding himself out as engaging in, the business of advising others with respect to the purchase and sale of securities and therefore should have been registered as an adviser. Mitton had trading authority over only two accounts but, for practical purposes, might as well have had it over the other accounts as well. The holders of those accounts completely abrogated their authority over the accounts and left all decisions in his hands. Mitton therefore should have been registered in the category of portfolio manager.

¶ 122 We find that Mitton acted as an adviser without being registered, contrary to section 20(1)(c) of the former Act.

Undeclared short sales

¶ 123 Commission staff allege that, while placing orders for the sale of securities either directly or through his nominees, Mitton failed to declare that neither he nor his nominees owned the securities, contrary to section 41 of the former Act (short sales notice).

¶ 124 Section 41(1) of the former Act stated:

> 41.(1) A person who places an order for the sale of a security through a registered dealer acting on his behalf and who
>
> (a) does not own the security, or
> (b) if he is acting as agent knows his principal does not own the security,
>
> shall, at the time of placing the order to sell, declare to the registered dealer that he or his principal, as the case may be, does not own the security, and that fact shall be disclosed by the dealer in the written confirmation of sale.

¶ 125 During February 1996, there were 13 undeclared short sales in the Valley Ridge account at Golden Capital and seven undeclared short sales in the Valley Ridge account at Canaccord. Wiebe did not place the orders for these sales. He subsequently learned that Mitton had placed the orders for the short sales in the Golden Capital account. Wiebe believed, and we agree, that Mitton did the same in respect of the short sales in the Canaccord account.

¶ 126 Therefore, we find that Mitton placed orders for the sales of securities through registered dealers, acting as agent, when he knew that his principal did not own the securities, without declaring to the registered dealers that his principal did not own the securities, contrary to section 41(1) of the former Act.

Fraud

¶ 127 Commission staff allege that Mitton participated in schemes that he knew or ought reasonably to have known perpetrated a fraud on persons in BC, contrary to section 41.1 of the former Act (the short sales, bond trading and share purchase notices).

¶ 128 Section 41.1(b) of the former Act stated:

> 41.1 No person, directly or indirectly, shall engage in or participate in a transaction or scheme relating to a trade in or acquisition of a security or a trade in an exchange contract if the person knows or ought reasonably to know that the transaction or scheme
> …
>
> (b) perpetrates a fraud on any person in the Province,

¶ 129 Section 41.1(b) of the former Act is, in substance, identical to section 57(b) of the Act. The British Columbia Court of Appeal considered section 57(b) in *Anderson v. British Columbia Securities Commission*, 2004 BCCA 7. At page 16 of that decision, Southin J. set out both the standard of proof and the test we must apply when we consider an alleged contravention of that section:

> Fraud is a very serious allegation which carries a stigma and requires a high standard of proof. While proof in a civil or regulatory case does not have to meet the criminal law standard of proof beyond a reasonable doubt, it does require evidence that is clear and convincing proof of the elements of fraud, including the mental element.

¶ 130 Southin J. identified the elements of fraud as those set out by the Supreme Court of Canada in *R v. Théroux*, [1993] 2 SCR 5. At page 20 of that decision,

McLachlin J. (as she then was) set out the elements necessary to establish the actus reus and mens rea of fraud:

> These doctrinal observations suggest that the actus reus of the offence of fraud will be established by proof of:
>
> 1. the prohibited act, be it an act of deceit, a falsehood or some other fraudulent means; and
>
> 2. deprivation caused by the prohibited act, which may consist in actual loss or the placing of the victim's pecuniary interests at risk.
>
> Correspondingly, the mens rea of fraud is established by proof of:
>
> 1. subjective knowledge of the prohibited act; and
>
> 2. subjective knowledge that the prohibited act could have as a consequence the deprivation of another (which deprivation may consist in knowledge that the victim's pecuniary interests are put at risk).
>
> Where the conduct and knowledge required by these definitions are established, the accused is guilty whether he actually intended the prohibited consequence or was reckless as to whether it would occur.

¶ 131 The fraud allegations in the three notices essentially relate to the same conduct, the same "prohibited act" – Mitton, directly or through nominees, would undertake a transaction in an account for which he did not intend to pay unless he was able to undertake an offsetting transaction at a profit. In the short sales scheme, Mitton intended to cover an undeclared short sale only if he was able to subsequently purchase the shares at a lower price. In the bond trading scheme, he intended to pay for a bond he purchased only if he could sell it for a higher price before the settlement date. In the share purchase scheme, he intended to pay for shares he purchased only if he could sell those or some other shares at a profit. If the scheme went awry and there was no profitable offsetting transaction to be made, Mitton simply refused to pay for the original transaction and left the dealer to cover the transaction and bear the loss.

¶ 132 Mitton's conduct was clearly deceitful. Neither he nor his nominees told the various dealers that they would pay for their transactions only if they were able to undertake a profitable offsetting transaction. Indeed, Mitton instructed his nominees to take steps to prevent the dealers from discovering this for as long as possible. For example, he told Edward Rempel to sell short at one dealer and buy

the shares to cover the short sale at another dealer. As well, when pressed by certain dealers for payment, Mitton stalled for time. He told Oxholm that margin would soon be coming in to cover the bond purchases in the Golden Capital accounts. He arranged for dealers involved in the share purchase scheme to be given cheques that were subsequently dishonoured.

¶ 133 It is just as clear that Mitton's conduct placed the dealers' pecuniary interests at risk. If Mitton and his nominees did not pay for a transaction, it would be up to the dealer to do so. In some cases, the dealer was able to sell out the account and cover the debit. In at least one case, the dealer was not so fortunate. In the short sales scheme, seven dealers were placed at risk, but we do not know if any suffered actual loss. In the bond trading scheme, Golden Capital suffered an actual loss of $753,935. In the share purchase scheme, the only BC dealer involved in the criminal case was Midland Walwyn. It was placed at risk but managed to avoid actual loss by selling out the shares in its two accounts.

¶ 134 Consequently, we are convinced that the actus reus of fraud has been established.

¶ 135 Mitton certainly knew of his own deceitful conduct. We are convinced that Mitton also knew that his deceitful conduct would put at risk the pecuniary interests of the dealers involved in his three schemes. Indeed, we can infer Mitton's subjective knowledge of this risk. As McLachlin J. stated at page 21 of *Théroux*:

> … In certain cases, the inference of subjective knowledge of the risk may be drawn from the facts as the accused believed them to be. The accused may introduce evidence negating that inference, such as evidence that his deceit was part of an innocent prank, or evidence of circumstances which led him to believe that no one would act on his lie or deceitful or dishonest act. But in cases like the present one, where the accused tells a lie knowing others will act on it and thereby puts their property at risk, the inference of subjective knowledge that the property of another would be put at risk is clear.

Mitton carried out his schemes knowing that the dealers involved would act, thereby putting their pecuniary interests at risk.

¶ 136 Consequently, we are of the view that the evidence clearly and convincingly establishes both the actus reus and the mens rea of Mitton's fraud.

¶ 137 Further, Mitton pleaded guilty to six counts of fraud in connection with his share purchase scheme. Two counts involved accounts at Midland Walwyn in BC.

¶ 138 We find that Mitton, directly and indirectly, participated in three schemes relating to trades in or acquisitions of securities when he knew that the schemes perpetrated a fraud on persons in BC, contrary to section 41.1(b) of the former Act.

Unregistered trading

¶ 139 Commission staff allege that Mitton traded without being registered through Wiebe, Moxon, Gmur and Hanna in the nominee accounts, contrary to section 20 of the former Act and section 34 of the Act (H & R notice).

¶ 140 All of the activities referred to occurred after the current Act came into force. Therefore, we will refer only to that Act.

¶ 141 Section 34(1)(a) of the Act states:

> 34 (1) A person must not
>
> (a) trade in a security or exchange contract unless the person is registered in accordance with the regulations as
> (i) a dealer, or
> (ii) a salesperson, partner, director or officer of a registered dealer and is acting on behalf of that dealer,

¶ 142 "Trade" is defined in section 1(1) of the Act:

> "trade" includes
>
> (a) a disposition of a security for valuable consideration whether the terms of payment be on margin, installment or otherwise, but does not include a purchase of a security or a transfer, pledge, mortgage or other encumbrance of a security for the purpose of giving collateral for a debt,

¶ 143 The nominee accounts were in the names of Wiebe and his companies, Moxon, Gmur and Hanna. Wiebe testified that the four of them understood that they were setting up these accounts for the benefit of H & R. Even if they had believed that at the outset, they should have realized very quickly that it was not H & R that was benefiting from the accounts, but Mitton. All of the money withdrawn from the accounts was paid to him, or at his direction.

¶ 144 Consequently, we are of the view that Mitton was the beneficial owner of the nominee accounts. Through Wiebe, Moxon, Gmur and Hanna, Mitton disposed of shares in the accounts and was therefore trading. Mitton was not registered to trade in securities. He could not rely on an exemption from the trading registration

requirement because his exemptions had been removed in his December 1988 order.

¶ 145 Therefore, we find that Mitton traded in securities without being registered, contrary to section 34(1)(a) of the Act.

Distribution without a prospectus

¶ 146 Commission staff allege that Mitton traded the shares of H & R without a prospectus or a prospectus exemption under circumstances where the trades were deemed distributions pursuant to section 140 of the Rules, contrary to section 42 of the former Act and section 61 of the Act (H & R notice).

¶ 147 Again, all of the activities referred to occurred after the current Act came into force. Therefore, we will refer only to that Act.

¶ 148 Section 61(1) of the Act states:

> 61 (1) Unless exempted under this Act or the regulations, a person must not distribute a security unless
>
> (a) a preliminary prospectus and a prospectus respecting the security have been filed with the executive director, and
>
> (b) the executive director has issued receipts for the preliminary prospectus and prospectus.

¶ 149 "Distribution" is defined in section 1(1) of the Act:

> "distribution" means, if used in relation to trading in securities,
>
> (a) a trade in a security of an issuer that has not been previously issued,
> …
>
> (e) a trade deemed to be a distribution
> (i) in an order made under section 76 by the commission or the executive director, or
> (ii) in the regulations,

¶ 150 Section 140 of the Rules stated:

> 140(1) This section applies only to securities of an issuer that was not a reporting issuer at the date of issue of the securities.

> (2) Subject to subsection (3) and to sections 141 and 143 [none of which apply], a trade in a security is deemed to be a distribution unless
>
> (a) the issuer of the securities is a reporting issuer, and

¶ 151 H & R was not a reporting issuer when it issued the 2,455,000 shares to Mitton's nominees – Wiebe and his companies, Moxon, Gmur and Hanna – in the August and September 1997 private placements.

¶ 152 The placees deposited those shares in the nominee accounts. We have determined that Mitton was the beneficial owner of the nominee accounts and that he traded those shares from the nominee accounts through Wiebe, Moxon, Gmur and Hanna. As H & R was not a reporting issuer at the time of those trades, they were deemed to be distributions under section 140(2) of the Rules. No person filed a prospectus in respect of those shares. Nor could Mitton rely on an exemption from the prospectus requirement because his exemptions had been removed in his December 1988 order.

¶ 153 Therefore, we find that Mitton distributed securities without a prospectus, contrary to section 61(1) of the Act.

Misleading appearance of trading activity

¶ 154 Commission staff allege that Mitton participated in transactions that he knew or ought to have known would contribute to a misleading appearance of trading activity or artificial price for the shares of H & R, contrary to section 41.1 of the former Act and section 57 of the Act (H & R notice).

¶ 155 Section 41.1(a) of the former Act and the section 57(a) of the Act that was in force at the time are, in substance, identical. Section 57(a) stated:

> 57. A person must not, directly or indirectly, engage in or participate in a transaction or scheme relating to a trade in or acquisition of a security or a trade in an exchange contract if the person knows, or ought reasonably to know, that the transaction or scheme
>
> (a) creates or results in a misleading appearance of trading activity in, or an artificial price for, any security listed, or exchange contract traded, on an exchange in British Columbia,

¶ 156 The shares of H & R were quoted only on the OTC BB, which is not an exchange in BC. Therefore, we make no findings against Mitton under section 57(a) of the Act.

Heredia and Rosen

¶ 157 Commission staff allege that Heredia and Rosen each participated in transactions that he knew or ought to have known would contribute to a misleading appearance of trading activity or artificial price for the shares of H & R, contrary to section 57 of the Act.

Section 57(a) of the Act applied only to securities listed on an exchange in BC. The shares of H & R were quoted only on the OTC BB. Therefore, we make no findings against Heredia or Rosen under section 57(a) of the Act.

H & R

¶ 158 Commission staff allege that H & R distributed its shares in BC without a prospectus or a prospectus exemption, contrary to section 42 of the former Act and section 61 of the Act.

¶ 159 Again, all of the activities referred to occurred after the current Act came into force. Therefore, we will refer only to that Act.

¶ 160 Section 61(1) of the Act states:

> 61 (1) Unless exempted under this Act or the regulations, a person must not distribute a security unless
>
> (a) a preliminary prospectus and a prospectus respecting the security have been filed with the executive director, and
>
> (b) the executive director has issued receipts for the preliminary prospectus and prospectus.

¶ 161 "Distribution" is defined in section 1(1) of the Act:

> "distribution" means, if used in relation to trading in securities,
>
> (a) a trade in a security of an issuer that has not been previously issued,

¶ 162 H & R issued 2,975,000 shares in three private placements, on July 29, August 11 and September 15, 1997. H & R was a US company quoted on the OTC BB and was not a reporting issuer here. Nevertheless, we are of the view that H & R had to comply with section 61(1) of the Act when it issued these shares. It is clear that Mitton was the directing mind of H & R – everyone involved with the company turned to him for instructions – and Mitton was located here in BC. As well, 2,455,000 of the shares were issued to persons in BC.

¶ 163 H & R neither filed a prospectus nor relied on an exemption from the prospectus requirement when it issued the shares.

¶ 164 Therefore, we find that H & R distributed securities without a prospectus, contrary to section 61(1) of the Act.

Public Interest and Orders

Mitton

¶ 165 Commission staff submit that it would be in the public interest to prohibit Mitton from operating in the capital markets of BC because of:

- his breach of his December 1988 order;
- his activities related to his December 2000 criminal conviction; and
- his involvement in the short sales, bond trading and H & R schemes.

¶ 166 On December 19, 1988, the Superintendent of Brokers issued an order removing Mitton's statutory exemptions (including the exemption that would allow him to trade through a registrant), and prohibiting him from becoming or acting as a director or officer of any issuer, until November 1, 2008. The order was based on a myriad of admissions by Mitton of conduct involving several VSE listed issuers. The conduct included trading that "may have resulted in a misleading appearance of active public trading", failure to make the disclosure required of insiders and control persons, insider trading, tipping, and acting as a director and officer while disqualified from doing so under corporate legislation.

¶ 167 We found that Mitton distributed shares without a prospectus, and traded in the nominee accounts, in connection with the H & R scheme; both were clearly in breach of his December 1988 order. That trading generated over $6 million, all of which was paid to, or at the direction of, Mitton.

¶ 168 On December 16, 2000, Mitton pleaded guilty in BC to six counts of fraud in connection with his share purchase scheme. He admitted to causing trades to be made in five accounts knowing that the holders of the accounts lacked the ability or good faith intention to pay amounts arising from the trades. Mitton was sentenced to four years imprisonment and ordered to pay restitution of $2,255,875. In connection with his share purchase scheme, we found that Mitton:

- acted as an adviser without being registered, contrary to section 20(1)(c) of the former Act; and

- directly and indirectly, participated in a scheme relating to trades in or acquisitions of securities when he knew that the scheme perpetrated a fraud on persons in BC, contrary to section 41.1(b) of the former Act.

¶ 169 Mitton's short sales scheme involved four groups of people and 16 accounts. It resulted in 191 undeclared short sales over a ten week period. We do not know if any dealers suffered a loss on any of the accounts. We found that Mitton:

- acted as an adviser without being registered, contrary to section 20(1)(c) of the former Act;
- placed orders for the sale of securities through registered dealers, acting as agent, when he knew that his principal did not own the securities, without declaring to the registered dealer that his principal did not own the securities, contrary to section 41(1) of the former Act; and
- directly and indirectly, participated in a scheme relating to trades in or acquisitions of securities when he knew that the scheme perpetrated a fraud on persons in BC, contrary to section 41.1(b) of the former Act.

¶ 170 In Mitton's bond trading scheme, he orchestrated the purchase of Government of Canada bonds in two accounts at Golden Capital. Both accounts were left with a debit balance. The debit balance in one account was paid by the account holder. The debit balance in the other account was not paid. Nor was the debit balance in another account at the firm, in which Mitton had sold short shares in an effort to create the appearance of margin for the bond purchases. Golden Capital brought a civil action to recover the amounts owing on the two accounts and received judgment in the amount of $753,935. In connection with the bond trading scheme, we found that Mitton:

- directly and indirectly, participated in a scheme relating to trades in or acquisitions of securities when he knew that the scheme perpetrated a fraud on persons in BC, contrary to section 41.1(b) of the former Act.

¶ 171 In connection with the H & R scheme, we were not able to find that Mitton had contravened section 57(a) of the Act. At that time, section 57(a) was drafted very narrowly to apply only to securities traded on an exchange in BC. However, even though H & R was quoted on the OTC BB, Mitton ran the scheme from BC. We are of the view that having a person in BC orchestrate a scheme of this nature is clearly contrary to the public interest.

¶ 172 Mitton's H & R scheme was a textbook market manipulation. In early 1997, Mitton acquired almost all the outstanding shares of H & R, a shell company quoted on the OTC BB. He set up an extensive network of market makers and

promoters across North America, and gave them the H & R shares. In the spring, H & R began issuing promotional news releases. One announced a significant private placement that never took place. Others announced the launch or acquisition of highly profitable business ventures that never materialized. We know that Mitton watched the market very closely every time a news release was issued and we are satisfied that he was the person responsible for issuing them.

¶ 173 Between July 29 and September 15, H & R issued 2,975,000 shares to promoters and Mitton's group of nominees – Wiebe and his companies, Moxon, Gmur and Hanna. None of the shares issued to the nominees were paid for. Once again, we are satisfied that it was Mitton who arranged for the issuance of those shares. Wiebe, Moxon, Gmur and Hanna deposited the 2,455,000 shares they received into the nominee accounts.

¶ 174 Once Mitton had the newly issued shares in the nominee accounts, the manipulation kicked into high gear. H & R's share price and trading volume had been gradually increasing over the summer – from US$.50 in late June on very low volume to slightly over US$2.00 by mid-September on volumes under 1 million shares. Then, in the week of September 22 to 26, the market for H & R shares exploded. Both trading volume and price rose dramatically. On Wednesday, September 24, H & R shares closed at US$6.09 on a volume of 12.4 million shares. Over the three day period between September 22 and 24, the inside bid increased by 175%. Two of H & R's market makers – J. Alexander and Saperston – were responsible for 92% of the increases in the inside bid during that period.

¶ 175 By the end of that week, however, the collapse had begun. The price had dropped to US$2.03, though volume was still relatively strong, at 2.5 million shares. By the end of October, it was over. Both price and volume had fallen back to their pre-manipulation levels.

¶ 176 Mitton had controlled it all. He acquired the shell company. He issued promotional news releases. He set up a network of market makers, promoters and nominees and funneled shares into their hands. He directed the trading not only in the nominee accounts, but among the market makers as well. As Wiebe observed: "Whether it would be the market makers, promoters, any trades that were being done, Mike Mitton was, was in contact with them." Mitton's attention to detail paid off – the nominee accounts sold a large number of shares at the inflated price and over $6 million was paid out of those accounts to Mitton or at his direction.

¶ 177 In connection with the H & R scheme, we found that Mitton:

- traded in securities without being registered, contrary to section 34(1)(a) of the Act; and
- distributed securities without a prospectus, contrary to section 61(1) of the Act.

¶ 178 The responsibility of the Commission is to regulate trading in securities in the public interest for the purpose of ensuring there is a fair and efficient securities market that warrants the confidence of investors. The integrity of the securities market and the confidence of investors can be damaged by persons who contravene the Act and engage in abusive trading activity. … *Re Holoboff*, [1993] 29 BCSC Weekly Summary 7 at page 11

¶ 179 Through his four investment schemes, Mitton engaged in two very serious kinds of abusive trading activity.

¶ 180 The first was that in the short sales, bond trading and share purchase schemes. Mitton, either directly or through his nominees, undertook transactions in accounts at a number of dealers for which he did not intend to pay unless he was able to undertake an offsetting transaction at a profit. In many cases, there was no profitable offsetting transaction to be made, and the dealers were left with significant debits in the accounts. As the Commission observed in *Re Pinchin*, [1996] 41 BCSC Weekly Summary 7, at page 33:

> It is clearly contrary to the public interest for a person to build up a large debit position in an account which he or she is unable to settle. It puts the liquidity of the dealer at risk and results in market activity that is essentially fictitious, thus undermining public confidence in both the market intermediary and the market itself.

¶ 181 We would go further. It is not necessary that a debit position actually be created. We are of the view that perpetrating a scheme or, in this case, three schemes that could foreseeably result in such debits is itself fraudulent and contrary to the public interest.

¶ 182 The second kind of abusive trading activity arose in the H & R scheme – the manipulation of the market for H & R shares. In *Pinchin*, the Commission considered similar activity and its effect on our capital markets:

> … As the United States Securities and Exchange Commission observed in its decision *In the Matter of Thornton and Company*, 28 S.E.C. 4 (1948) 208 at page 218:

> Investors reading reports of stock exchange transactions on ticker tapes and in newspapers ordinarily assume that the reports reflect legitimate transactions. If the transactions instead reflect fictitious activity, such investors are deceived as to the market in the security. They are falsely led to believe that bona fide transactions have occurred at a certain price and they may be induced by the volume or price changes to purchase or sell the securities as the case may be.

¶ 183 We do not know how many investors were induced by the volume or price changes in H & R shares during the week of September 22 to purchase the shares at the inflated price, or how much they lost as a result. We do know that dealers, as well as investors, were duped by this fictitious activity and suffered losses. One dealer's losses were so high that it was forced out of business.

¶ 184 Mitton has a long and egregious history of fraudulent and abusive trading. He has 103 criminal convictions in Canada and an outstanding indictment for securities fraud in the US. In 1988, the Superintendent of Brokers issued an order prohibiting Mitton from participating in the capital markets for 20 years, an order that Mitton brazenly ignored. We consider it to be in the public interest to remove Mitton permanently from the capital markets, and from involvement with issuers, and to impose on him the maximum administrative penalty. We order:

1. under section 161(1)(b) of the Act that Mitton cease trading in, and be prohibited from purchasing, any securities or exchange contracts permanently;

2. under section 161(1)(c) of the Act that all of the exemptions described in the Act do not apply to Mitton permanently;

3. under section 161(1)(d)(i) of the Act that Mitton resign any position that he holds as a director or officer of any issuer;

4. under section 161(1)(d)(ii) of the Act that Mitton is prohibited from becoming or acting as a director or officer of any issuer permanently;

5. under section 161(1)(d)(iii) of the Act that Mitton is prohibited from engaging in investor relations activities permanently; and

6. under section 162 of the Act that Mitton pay an administrative penalty of $250,000.

Heredia

¶ 185 Commission staff submit that it would be in the public interest to prohibit Heredia from operating in the capital markets of BC because of:

- his involvement with H & R;
- his breach of, or participation with Mitton in the breach of, Mitton's December 1988 order; and
- the orders against him in the US.

¶ 186 Heredia played a significant role in the manipulation of the market for H & R shares. In essence, Heredia was Mitton's second in command.

¶ 187 Heredia's firm, Alexander Troy, had a contract with H & R to provide "public relations" with US broker dealers and the investing public. Under that contract, Alexander Troy would receive a "performance bonus" if the bid price for H & R shares reached a certain level: the higher the level, the higher the bonus. Alexander Troy also received 1,744,000 H & R shares.

¶ 188 Heredia assisted Mitton to direct the trading by the market makers. Prager, at Saperston, dealt exclusively with Heredia. Chamberlain, at Equitrade, and Rosen, at J. Alexander, dealt with both Heredia and Mitton.

¶ 189 Heredia's involvement in the H & R manipulation proved to be profitable for him. He received net proceeds of more than $1.1 million from the Alexander Troy account at Equitrade.

¶ 190 In January 2004, Heredia pleaded guilty in the US to a charge of conspiracy to commit securities fraud and wire fraud and to a charge of fraud in the purchase and sale of H & R securities. He admitted that he paid off brokers, that he received shares and that he directed buying and selling in H & R shares to try to show volume to increase the price.

¶ 191 Heredia is subject to disciplinary orders issued by the SEC, the NASD and the state of Georgia that, among other things, prohibit him from associating with any broker or dealer or with any NASD member in any capacity.

¶ 192 We have already described the threat to our markets, and to investor confidence in those markets, posed by the type of abusive trading activity involved in the H & R manipulation. Heredia played a significant role in that activity. Therefore, we consider it to be in the public interest to permanently deny Heredia access to our capital markets and prohibit him from involvement with issuers. We order:

1. under section 161(1)(b) of the Act that Heredia cease trading in, and be prohibited from purchasing, any securities or exchange contracts permanently;

2. under section 161(1)(c) of the Act that all of the exemptions described in the Act do not apply to Heredia permanently;

3. under section 161(1)(d)(i) of the Act that Heredia resign any position that he holds as a director or officer of any issuer;

4. under section 161(1)(d)(ii) of the Act that Heredia is prohibited from becoming or acting as a director or officer of any issuer permanently; and

5. under section 161(1)(d)(iii) of the Act that Heredia is prohibited from engaging in investor relations activities permanently.

Rosen

¶ 193 Commission staff submit that it would be in the public interest to prohibit Rosen from operating in the capital markets of BC because of:

- his involvement with H & R; and
- his breach of, or participation with Mitton in the breach of, Mitton's December 1988 order.

¶ 194 J. Alexander was one of the market makers for H & R shares. Rosen was the trader responsible for H & R. He took his trading instructions from Mitton and Heredia. They told him how many shares to buy or sell, when to do it, and with which dealer. Rosen proved to be very effective in carrying out their instructions. In the three day period between September 22 and 24, there was an increase of 175% in the inside bid for H & R shares. J. Alexander was responsible for 41% of the increases in the inside bid during that time. During the same three day period, one of J. Alexander, Saperston or Equitrade was involved in 64% of the trades in H & R shares.

¶ 195 Rosen made a profit of over $750,000 trading H & R shares in his two OTCBB Holdings accounts. He made additional profits from making a market in H & R shares.

¶ 196 In August 2001, the NASD issued a complaint against Rosen in connection with his involvement in the H & R manipulation. That proceeding has been stayed due to Rosen's bankruptcy.

¶ 197 In January 2004, Rosen pleaded guilty in the US to a charge of conspiracy to commit securities fraud and wire fraud and to a charge of fraud in the purchase and sale of H & R securities. He admitted that he received shares and that he assisted in pushing up the price by showing volume.

¶ 198 Rosen has been disciplined on other occasions by the SEC and the NASD.

¶ 199 Rosen's abusive trading activity was central to the success of Mitton's manipulation of the market for H & R shares. We cannot permit Rosen to ever carry out such activity in BC. Accordingly, we consider it to be in the public interest to permanently deny Rosen access to our capital markets and prohibit him from involvement with issuers. We order:

1. under section 161(1)(b) of the Act that Rosen cease trading in, and be prohibited from purchasing, any securities or exchange contracts permanently;

2. under section 161(1)(c) of the Act that all of the exemptions described in the Act do not apply to Rosen permanently;

3. under section 161(1)(d)(i) of the Act that Rosen resign any position that he holds as a director or officer of any issuer;

4. under section 161(1)(d)(ii) of the Act that Rosen is prohibited from becoming or acting as a director or officer of any issuer permanently; and

5. under section 161(1)(d)(iii) of the Act that Rosen is prohibited from engaging in investor relations activities permanently.

H & R

¶ 200 Commission staff submit that it would be in the public interest to cease trading in H & R's shares because H & R issued false and misleading news releases. Rather than raising this as a matter of public interest, we would have expected Commission staff to allege that H & R made misrepresentations , contrary to section 50 of the Act. However, we do not need to consider H & R's actions in respect of the news releases.

¶ 201 H & R was a shell company by January 1997; it had no assets and no business. Mitton used H & R as the vehicle for his market manipulation. H & R's distribution of almost 3 million shares to Mitton's promoters and nominees was an integral part of that manipulation. We found that H & R's distribution of those shares without a prospectus was contrary to section 61(1) of the Act.

¶ 202 H & R's shares have been subject to a cease trade order since October 17, 1997. Commission staff submit that we should make that order permanent. They seek no other sanctions against H & R.

¶ 203 We consider it to be in the public interest to prevent any further trading in BC in the securities of H & R. Therefore, we order under section 161(1)(b) of the Act that all persons cease trading in, and be prohibited from purchasing, any securities of H & R.

Costs

¶ 204 We will consider written submissions before ordering costs in this matter. We direct Commission staff to send their submissions to the Secretary to the Commission and to the respondents at their last known addresses by October 21, 2005. If the respondents wish to make submissions, we direct them to send their submissions to the Secretary to the Commission and to Commission staff by November 14, 2005.

¶ 205 September 29, 2005

¶ 206 **For the Commission**

Adrienne Salvail-Lopez
Vice Chair

Marc A. Foreman
Commissioner

Robert J. Milbourne
Commissioner