

2011 BCSECCOM 225

Kunekt Corporation and Mark Bruk

Securities Act, RSBC 1996, c. 418

Panel	Brent W. Aitken Don Rowlatt Shelley C. Williams	Vice Chair Commissioner Commissioner
Dates of hearing	April 8 and 11, 2011	
Date of Decision	April 11, 2011	
Date of Reasons	May 16, 2011	
Appearing		
Graham MacLennan	For the Executive Director	
Thomas Manson, Q.C.	For Kunekt Corporation and Mark Bruk	

Reasons for Ruling

I Introduction

- ¶ 1 On March 8, 2011 the Executive Director issued a temporary order against Kunekt Corporation and Mark Bruk and a notice of hearing under section 161(2) of the *Securities Act*, RSBC 1996, c. 418 (2011 BCSECCOM 109). The Commission ordered an extension of the temporary order until a hearing beginning on April 8, when it extended the temporary order until a hearing is held and a decision is rendered.
- ¶ 2 At the continuation of the hearing on April 11, Kunekt and Bruk applied to the Commission to have the temporary order revoked or, alternatively, varied to allow Kunekt to complete specified transactions. We denied the application (2011 BCSECCOM 178). These are our reasons.

II Background

A Kunekt and relevant events up to the hearing

- ¶ 3 Kunekt was formed in 2007. Bruk is its president and its sole director. Its only other officer of record is Arom Thaveeloue, its secretary. The shares of Kunekt

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are quoted on the Over-the-Counter Bulletin Board in the United States. They are not listed or quoted on any market in Canada. Kunekt has 62 million shares outstanding; Bruk owns 32 million (52%) of them.

- ¶ 4 As of January 31, 2011, Kunekt had no revenues and assets of \$360,000.
- ¶ 5 Bruk says that in late 2010, Kunekt entered the business of marketing mobile phones, smartphones, and tablets. Bruk says Kunekt now seeks to enter the business of designing and manufacturing those devices.
- ¶ 6 Bruk says Kunekt started negotiations in 2010 with Matt Li, with a view to acquiring control of companies in China that develop software for mobile devices, and that are involved in device design.
- ¶ 7 On December 2, 2010 Kunekt issued a news release disclosing trademark applications in the United States for mobile phones and smartphones and disclosing the company's change in focus to designing, building and marketing mobile phones, smartphones and tablets. On that day Kunekt also launched its website.
- ¶ 8 The negotiations led to agreements dated January 20, 2011 whereby Kunekt would issue shares to the shareholders of the Chinese software and design companies in exchange for the shares of those companies. We refer to these agreements as the pending transactions.
- ¶ 9 Kunekt has a wholly-owned subsidiary incorporated in Hong Kong. According to Bruk, Li is the *de facto* president of that company and "runs the Kunekt office" in Shenzhen, China. When the pending transactions close, Li will become a director of Kunekt, co-CEO, and its president.
- ¶ 10 Kunekt issued a news release on January 21, 2011 announcing the move of its head office to Hong Kong. It issued another news release on January 24, 2011 announcing the pending transactions.
- ¶ 11 Between January 24 and the date of the hearing, Kunekt issued another eight news releases disclosing:
 - on January 28, trademark applications in the United States for its smartphone, tablet, and mobile phone products;
 - on February 1, the company's formation of an advisory board, the intended opening of a sales office in Shenzhen, and the hiring of sales staff;
 - on February 9, the appointment of Li and another to Kunekt's advisory board;

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- on February 24, the opening of the Shenzhen sales office, the continued hiring of sales staff, and a new line of products;
 - on February 28, the appointment of two individuals to its advisory board;
 - on March 4, a \$1.8 million private placement;
 - on March 14, a clarification that no shares had yet been issued under the private placement (although Kunekt had received the proceeds); and
 - on April 8, matters relevant to this hearing, further details about the pending transactions, and an agreement between Kunekt and three Chinese manufacturers granting Kunekt the right to market their products under Kunekt brand names.
- ¶ 12 In January (beginning no later than January 24) and February 2011 promotional material about Kunekt appeared on the internet on several websites. This internet material included the following statements:
- “This Company Can Return You 5,192% Profits by June 1st, 2011 . . .
. . . Act now and you could watch \$5,000 blossom into \$264,600 or \$10,000 soar to a cool \$529,200 – all by Summertime of this year!
. . . is it any wonder why experts are already calling Kunekt “*The Apple of Emerging Markets*”?
. . .
Is Mark Bruk The Next Steve Jobs? . . . Well, the argument could easily be made that Kunekt President and Chairman, Mark Bruk is cut from the same cloth as the driving force behind Apple’s success.”
- ¶ 13 In a footnote to this dishonest touting, the internet material disclosed that an entity called Capital Financial Media “has received and managed a total production budget of \$2,500,000 for this online advertising effort” The disclosure also says that Capital Financial Media paid one of the touts \$3,000. If true, someone paid well for this promotion.
- ¶ 14 During the period that Kunekt was issuing its news releases and the internet material was appearing, the trading volume and price of the Kunekt shares increased significantly.
- ¶ 15 For all of 2010, up to December 2, Kunekt traded on only nine days, for a total volume of 124,900 shares at prices ranging from 5 cents to 50 cents.

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- ¶ 16 In December 2010, Kunekt traded on six days, for a total volume of 218,000 shares at prices ranging from 51 cents to 83 cents.
- ¶ 17 From January 3 through January 21, 2011, Kunekt traded on every trading day but two, for a total volume of 2.75 million shares at prices ranging from 83 cents to 99 cents.
- ¶ 18 On January 24, when the internet material appeared, total volume jumped to more than 1.5 million shares for the day, and the price increased to \$1.07 that day. From January 24 through the end of February, over 91 million Kunekt shares traded at prices ranging from \$1.07 to \$2.89.
- ¶ 19 Part of this volume was trading done through an account in the name of Steven Bruk, the respondent Bruk's brother. From February 16 to February 28, Steven Bruk sold nearly 1.9 million Kunekt shares for proceeds of over \$4 million.
- ¶ 20 Commission staff became aware of the internet material and the concurrent increase in the trading volume and price of the Kunekt shares.
- ¶ 21 On February 28 and March 3 Commission staff issued halt trade orders under section 89 of the Act.
- ¶ 22 On March 3 and 4 Commission staff issued production orders under section 141 against each of Kunekt and Bruk.
- ¶ 23 On March 8 the executive director issued the temporary order and notice of hearing, seeking the extension of the temporary order until
- Kunekt and Bruk complied with the production orders, and
 - Kunekt generally disclosed to the public the extent to which Kunekt and its directors, officers and insiders were involved in or had knowledge of the internet material.
- ¶ 24 On March 11 the Commission issued an investigation order under section 142.
- ¶ 25 By the time of the hearing, Kunekt and Bruk had complied with the production orders so that aspect of the order sought by the executive director was no longer relevant.
- B The hearing**
- ¶ 26 The hearing occurred on Friday, April 8 and Monday, April 11. April 8 was the expiry date of the temporary order. Since the hearing was in progress, we

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considered it necessary and in the public interest to extend the temporary order until a hearing is held and a decision rendered.

- ¶ 27 At the conclusion of the hearing we dismissed the respondents' application. We also said that the Commission will reconsider that decision if the respondents file sworn statements by specified persons, and by anyone else who is a director, officer or insider of Kunekt, to the effect that none of them had anything to do with the creation and dissemination of the internet material, and that they had no knowledge of it.

III Analysis

A The law

- ¶ 28 Because we extended the temporary order on April 8 until a hearing is held and a decision is rendered, the respondents, as a matter of procedure, applied on April 11 to have the temporary order revoked or varied. However, this we considered a matter of form rather than substance. We heard the matter on the basis of whether it was necessary and in the public interest to extend the temporary order.

- ¶ 29 Section 161(3) says:

“161(3) If the commission . . . considers it necessary and in the public interest, the commission . . . may . . . make an order extending a temporary order until a hearing is held and a decision rendered.”

- ¶ 30 In *Fairtide Capital Corp.* 2002 BCSECCOM 993 the Commission considered what is required for the Commission to conclude that it is necessary and in the public interest to extend a temporary order. The Commission said:

“29 In our view, there is no bright line test. The Commission considers evidence using its expertise and specialized understanding of the markets and the securities related activities it supervises, to determine what is in the public interest in any given circumstance. See: [*Pezim v. British Columbia (Superintendent of Brokers)*, [1994] 2 SCR 557].

30 The three Commission decisions referred to us by Commission staff are examples of applications where we determined that it was necessary and in the public interest to extend the temporary orders

31 In each of these cases, Commission staff produced

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evidence for the Commission to conclude that there was prima facie evidence of the misconduct alleged and that the extension order was necessary and in the public interest. . . .”

- ¶ 31 In *Hypo Alpe-Adria-Bank (Lichtenstein) AG* 2007 BCSECCOM 622, the Commission considered *Fairtide* in circumstances where the evidence required to meet that test is not available. The Commission said:

“16 In *Terry James Minnie and Raymond Patrick Shaw* 2004 BCSECCOM 677 the commission said this about the standard of proof required to establish that an extension of a temporary order is necessary and in the public interest:

As stated in *Fairtide*, there is no bright line test. The commission considers evidence using its expertise and specialized understanding of the markets . . . to determine what is in the public interest . . .

Staff must produce evidence for the commission to independently assess whether there is *prima facie* evidence of the misconduct alleged and whether, in the circumstances, the extension is necessary and in the public interest. The evidence must be more than staff’s opinion or belief . . .

. . .
. . . where there is *prima facie* evidence of egregious behaviour, our main aim must be to protect the public.”

17 This enunciation of the standard of proof for extending a temporary order is useful in cases like *Fairtide* and *Minnie*, where the circumstances involve a known respondent and clearly defined alleged misconduct.

18 However, there is another category of cases, involving conduct that appears could be in contravention of the Act or otherwise be contrary to the public interest by persons unknown and, because they are unknown, it is not possible to gather the information necessary to meet the *prima facie* evidence standard described in *Fairtide* and *Minnie*.

19 For that category of cases, *LOM (Holdings) Limited et al* 2005 BCSECCOM 144 is instructive. In that case, the commission noted that it could be in the public interest to

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issue a cease trade order absent evidence of inappropriate trading activity. The commission said, “There is also no evidence of any inappropriate trading activity. Even without such evidence, it could still be in the public interest to make a cease trade order.”

20 The commission has a broad public interest mandate to protect investors and maintain confidence in our capital markets . . .

21 In considering whether it is necessary and in the public interest to extend a temporary order, the commission must assess the risk to the capital markets. If that risk assessment is hampered because commission staff cannot obtain information on a timely basis about the trading of individuals whose identities are protected by foreign banking secrecy laws, the balance of interests must be tilted in favour of protecting our capital markets. . . .

- ¶ 32 The Commission found that there was evidence of suspicious trading through Hypo Bank’s account at a British Columbia dealer by unknown clients of the Bank, and extended the temporary order against the Bank until a hearing is held and a decision is rendered.
- ¶ 33 In *Sungro Minerals Inc.* 2009 BCSECCOM 585, the Commission considered the extension of a temporary order in circumstances where the price of the company’s shares had spiked dramatically over a three-week period in the absence of any disclosure by the company that would account for the increase.
- ¶ 34 The panel noted (at paragraph 33) that the increase in price was “highly suspicious and strongly suggests market manipulation is involved.” The panel found it necessary and in the public interest to extend the temporary order “while staff continues its investigation to determine the source and nature of the wrongdoing evidenced by the suspicious trading.”

B Application of the law

- ¶ 35 In our opinion, the executive director has provided *prima facie* evidence of wrongdoing. There was a significant increase in both the trading volume and the price of the Kunekt shares, concurrent with the dishonest touting over the internet. That makes the trading suspicious – it has the earmarks of a manipulation, conduct in contravention of the Act.

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- ¶ 36 What the executive director did not provide is *prima facie* evidence of the involvement of Kunekt, or anyone associated with Kunekt, in the touting activity over the internet.
- ¶ 37 The executive director does not have that evidence partly because the respondents did not provide complete answers to Commission staff investigators. Nor did they do so in the hearing. In these circumstances, the reasoning in *Hypo* and *Sungro* applies.
- ¶ 38 It is true that, unlike *Sungro*, Kunekt made disclosures during the period the trading volume and price of its shares increased. However, the nature of those disclosures could hardly account for the increase in trading volume and share price that occurred during the relevant period.
- ¶ 39 Kunekt had 62 million shares outstanding. Between January 24 and February 28, 91 million Kunekt shares – nearly three times its public float – traded between \$1.07 and \$2.89. Even at only \$2.00 per share, the implied market value of Kunekt was \$124 million – hardly a credible value for a company with a nascent business, no revenues, assets of \$360,000, and a few contracts (yet to be completed) for it to start operations.
- ¶ 40 Incredible as that is, it pales against the realm of fantasy invented by the touts, who claimed that within six months after January, Kunekt’s share price (then about, say, 90 cents) would multiply 50 times, implying a market value of about \$3 billion.
- ¶ 41 In these circumstances, the only reasonable conclusion to draw is that the internet touting was mainly responsible for the increase in the trading volume and price of the Kunekt shares after January 21, evidenced by the sudden increase in volume and share price on January 24, the earliest known date that the internet material appeared.
- ¶ 42 It is also true that, unlike *Hypo*, this case does not involve a bank secrecy jurisdiction, but the principle stated in *Hypo* remains: if there appears to be a risk to the capital markets that cannot be fully assessed because Commission staff cannot obtain the information they need to investigate the potential wrongdoing, the uncertainty will be resolved in favour of protecting the markets.
- ¶ 43 Commission staff investigators sought to interview Bruk as part of their investigation. He has yet to make himself available. In the meantime, Commission staff asked him and Kunekt to make unequivocal disclosure about the involvement of Kunekt and anyone connected with it in the internet touting.

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- ¶ 44 In the hearing this remained a significant area of concern for the executive director. Bruk swore a statutory declaration on April 11, the second day of the hearing. The statutory declaration addresses the subject matter of these concerns yet, to the extent the statutory declaration intends to put them to rest, it fails to do so.
- ¶ 45 The statutory declaration deals with six separate groups of the internet touts. Bruk deposes similar facts about each group. For the most part, the language used is identical for each group. Bruk deposes that:
- neither he nor Kunekt “had any business dealings” with any of the touts
 - he first became aware of the internet material when it was drawn to his attention by Commission staff
 - neither Kunekt “nor anyone on its behalf” paid any amounts to the touts
 - neither Kunekt “nor I had an involvement, direct or indirect, in the creation, financing (paid or prospective) or dissemination” of the internet material
 - Kunekt “has not sponsored, paid for, or otherwise supported any spam, email, or e-letter campaign promoting Kunekt or its securities”
 - “To the best of its knowledge, Kunekt knows of no link or association” between the principals of the proposed transactions described above “and any spam, email, or e-letter campaign promoting Kunekt or its securities”.
- ¶ 46 This evidence, at first glance, appears responsive to the executive director’s concerns about the involvement of Kunekt, or persons associated with Kunekt, in the internet touting of its stock. On closer examination, there are important questions left unanswered.
- ¶ 47 In one of the paragraphs, Bruk deposes that neither he nor Kunekt had any business dealings with four named touts. He then deposes that “neither Kunekt, nor anyone on its behalf paid \$3,000 or any amount” to only two of the four. Why this paragraph fails to deny payments to the other two touts is not explained.
- ¶ 48 Bruk deposes only that *he* was not aware of the internet material until it was drawn to his attention by Commission staff. That does address the knowledge of any other directors or officers of Kunekt.
- ¶ 49 Bruk deposes that neither Kunekt “nor anyone on its behalf” paid any money to the touts. This does not address the possibility that whoever paid them was doing so, not for Kunekt’s benefit, but for their own.
- ¶ 50 Bruk deposes that he is the sole director and that he and Thaveeloue are its only officers, but is silent on the subject of *de facto* directors and officers. In section

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1(1), the Act defines directors and officers to include those who perform a similar function or occupy a similar position.

- ¶ 51 Whether there are *de facto* directors or officers of Kunekt is not an academic inquiry. Nearly 1.9 million Kunekt shares for proceeds of over \$4 million were sold from an account in the name of Bruk's brother Steven during the period of suspicious trading. Li is clearly involved in the affairs of Kunekt and in the proposed transactions. He is the president of its Hong Kong subsidiary and runs its office in Shenzhen.
- ¶ 52 One is led to ask whether either or both of Steven Bruk and Li have an undisclosed role in Kunekt. Bruk deposes that Li has no signing authority for Kunekt and no authority to bind the company, but the absence of those formal arrangements would not be untypical of those acting solely as *de facto* officers or directors. Kunekt and Li have agreed that when the pending transactions close, Li will become a director of Kunekt, co-CEO, and its president.
- ¶ 53 In five of the six paragraphs about involvement in the creation, financing and dissemination of the internet material, Bruk deposes that neither he nor Kunekt had that involvement. In the sixth, Bruk deposes that neither Kunekt "nor its director/insider and officers" had any involvement. One is led to ask whether Bruk could not honestly deny the involvement of Kunekt's directors or officers (including *de facto* directors and officers) in the context of the other five paragraphs.
- ¶ 54 Bruk describes Li's role in his statutory declaration but is silent on his potential involvement in the creation, financing and dissemination of the internet material. (Bruk deposes that to the best of Kunekt's knowledge, none of those associated with the proposed transactions were associated with the dissemination of the internet material, but in doing so, he does not name Li directly.)
- ¶ 55 Bruk deposes that he is not aware of anyone other than himself owning more than 10% of Kunekt's shares, presumably to show that Kunekt has no insiders other than himself. However, he does not speak to Li's status as an insider. The definition of insider in section 1(1) of the Act includes "a director or an officer of a person that is . . . a subsidiary of an issuer". As *de facto* president of Kunekt's Hong Kong subsidiary, Li is an insider of Kunekt.
- ¶ 56 These discrepancies might be explained as mere sloppiness if it were not for the apparent care taken in the drafting of the statutory declaration to use consistent language to convey the same type of facts. That leads us to conclude that where the language in the statutory declaration is inconsistent, the inconsistency is intentional.

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- ¶ 57 We have not overlooked the contents of a letter purportedly from Li bearing the date of April 7, 2011 addressed to counsel for the executive director. The letter says, among other things, that Li does not hold shares in Kunekt and did not trade in Kunekt shares between December 1, 2010 and March 8, 2011. The letter also says that Li had no involvement, direct or indirect, in the creation, financing (paid or prospective) for any internet websites promoting Kunekt, although is silent as to his knowledge of the internet material. From the perspective of conducting an investigation, the letter is hardly conclusive of the facts it states.
- ¶ 58 We could, of course, be wrong. Maybe the discrepancies we have noted are the result of mere sloppiness. We are also mindful of the respondents' submissions that an extension of the temporary order would do Kunekt irreparable harm as it would prevent it from completing the pending transactions.
- ¶ 59 For that reason, although we decided not to revoke or vary the extended temporary order, we said the Commission will reconsider that decision if Kunekt and Bruk file sworn statements of each of Kunekt, Bruk, Thaveelouie, Li, and any other person who is a director, officer or insider of Kunekt. The sworn statements are to be to the effect that the deponent did not
- cause the internet material to be prepared or published,
 - cause any payment to be made in connection with the internet material,
 - have any other involvement in the preparation of the internet material, and
 - have any knowledge of the content of the internet material until informed of it by Commission staff.
- ¶ 60 This provides the opportunity for the respondents and their associates to deny unequivocally any involvement in the internet touting and for Kunekt and Bruk then to apply for a revocation of the temporary order or its variation to allow the pending transactions to proceed.
- ¶ 61 May 16, 2011
- ¶ 62 **For the Commission**

Brent W. Aitken
Vice Chair

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Don Rowlatt
Commissioner

Shelley C. Williams
Commissioner