BRITISH COLUMBIA SECURITIES COMMISSION
Securities Act, RSBC 1996, c. 418

Citation: Re Johnston, 2021 BCSECCOM 79 Date: 20210219

In the Matter of Tim Johnston and a Decision of the TSX Venture Exchange Inc. dated May 11, 2020

Panel	Gordon Johnson	Vice Chair
	Judith Downes	Commissioner
	Marion Shaw	Commissioner

Hearing dates	October 16 and December 15, 2020
Submissions Completed	December 15, 2020
Decision date	February 19, 2021

Appearing

David Hausman Jonathan Wansbrough	For Tim Johnston
Teresa Tomchak	For the TSX Venture Exchange
Jennifer Whately Gordon Smith Nazma Lee	For the Executive Director

Decision and Reasons

I. Introduction

[1] On June 2, 2020, Tim Johnston applied under section 28(1) of the *Securities Act*, RSBC 1996, c. 418 (the Act) for a hearing and review of a decision dated May 11, 2020 (the Decision) of the TSX Venture Exchange Inc. (the Exchange). The Decision sets certain pre-conditions for any future application by Mr. Johnston to become a director or officer of an issuer listed on the Exchange.

[2] The Exchange opposed the application. Each of Mr. Johnston, the Exchange and the executive director, the latter on just two issues, provided written submissions on the application. We also heard oral submissions from all parties.

[3] One key issue raised in this application concerns the appropriate standard of review to be applied by the Commission on its review of a decision of the Exchange. Other key issues raised are whether the Exchange exceeded its jurisdiction, whether the Exchange has fettered its discretion, whether Mr. Johnston has established a defence based on his

reliance on legal advice and the adequacy of the reasons given by the Exchange for the Decision.

II. Background

A. Factual Background

[4] Mr. Johnston served as a director and the chief executive officer (CEO) of Desert Lion Energy Inc. (Desert Lion) during the period from February 23, 2018 to July 16, 2019. According to public filings, he also served as the President of Desert Lion during the period from February 23, 2018 to approximately May 2019.

[5] Mr. Johnston is a chartered professional engineer. He has particular experience in the global lithium business. In 2015, Mr. Johnston obtained a designation as a Chartered Financial Analyst.

[6] Desert Lion was an Exchange-listed issuer in the business of developing lithium assets in Namibia. By mid- to late-2018, Desert Lion was in significant financial distress and faced the prospect of imminent bankruptcy.

[7] On October 31, 2018, Desert Lion entered into an agreement (the Note Purchase Agreement) with AIP Asset Management and AIP Global Macro Fund L.P. (AIP), where Desert Lion would sell to AIP $5,000,000 principal amount of convertible notes for a purchase price of $4,000,000, reflecting an original issue discount of $1,000,000. While a purchase price that reflects a discount from the face value of notes may be permitted, the amount of the discount proposed in this case was highly material. The Note Purchase Agreement also contained an enterprise value covenant that could give rise to a default by Desert Lion (the Covenant). The Note Purchase Agreement was signed by Mr. Johnston on behalf of Desert Lion.

[8] On November 5, 2019, Desert Lion issued a news release announcing the proposed financing. The news release stated that Desert Lion was raising "gross proceeds of $5,000,000", but did not disclose the $1,000,000 discount. A cash closing fee of $150,000 to AIP was disclosed. There was no disclosure of any other fees or of the Covenant. Mr. Johnston is listed as the contact person for the news release and is quoted in the news release with reference to "AIP's commitment to invest a minimum of $5,000,000…".

[9] The rules and policies of the Exchange required that Desert Lion seek the Exchange's approval of the proposed financing by filing a Form 4B - Notice of Private Placement. The Form 4B requires specified information, including the total amount of the funds raised, the pricing terms, any default provisions for convertible securities, and any unusual or significant information regarding the transaction that has not otherwise been provided on the form.

[10] On November 7, 2019, Desert Lion filed an initial Form 4B disclosing that $5,000,000 was to be raised through the issuance of secured convertible notes (the Convertible Note). The Form 4B disclosed the $150,000 cash closing fee described in the news release and a further $200,000 facility fee not mentioned in the news release, but did not disclose either the $1,000,000 discount stipulated in the Note Purchase Agreement or the Covenant. The initial Form 4B was signed by Mr. Johnston as President and CEO of Desert Lion.

[11] Desert Lion's application was accompanied by the Note Purchase Agreement. When staff of the Exchange reviewed it, they learned that its terms included a $1,000,000 discount on the purchase price payable by AIP to Desert Lion. The Exchange informed Desert Lion that the discount would not be acceptable.

[12] Desert Lion subsequently advised the Exchange that it would issue a $4,000,000 Convertible Note and a $1,000,000 non-convertible note (the Non-Convertible Note), for aggregate gross proceeds of $5,000,000. Desert Lion filed a revised Form 4B, also dated November 7, 2018, which described the gross proceeds to be raised by Desert Lion from the Convertible Note as $4,000,000. As before, the Covenant was not disclosed.

[13] On November 29, 2018, the Exchange advised that it had conditionally approved the financing.

[14] On December 10, 2018, Desert Lion issued a news release announcing that "it has successfully closed the initial tranche of secured convertible promissory notes (the "Notes") for gross proceeds of $5,000,000." The news release disclosed the cash closing and facility fees totaling $350,000 described in the Form 4B, but no other fees were disclosed, and the news release did not disclose the discount or the Covenant. Mr. Johnston is listed as the contact person for the news release and is quoted in the news release, referring to "AIP's investment of $5,000,000…".

[15] On December 12, 2018, the Exchange sent an email to Desert Lion asking for the completed Form 4B for the $4,000,000 Convertible Note and the supporting documents for the $1,000,000 Non-Convertible Note. Mr. Johnston was copied on the email.

[16] On January 2, 2019, Desert Lion sent the Exchange an email with the final Form 4B dated December 20, 2018 for the Convertible Note, showing gross proceeds of $4,000,000. Again, the Form 4B did not disclose the Covenant. Mr. Johnston was copied on the email.

[17] On March 6, 2019, having received the requested supporting documentation, the Exchange advised Desert Lion that the Non-Convertible Note was approved.

[18] On March 22, 2019, Desert Lion filed its financial statements for the year ended December 31, 2018. The notes to the financial statements disclosed publicly, for the first time, the existence of the Covenant and that the Convertible Note was subject to a $1,000,000 original issue discount.

[19] In April 2019, having defaulted on the Covenant, Desert Lion filed an application for Exchange approval of the issuance of shares for debt. In the course of its consideration of the application, the Exchange learned that contrary to Desert Lion's prior disclosure and contrary to the Exchange's instructions, Desert Lion had in fact closed the aggregate $5,000,000 note financing with a $1,000,000 discount and had received gross proceeds of only $4,000,000, less various fees and expenses, which were themselves higher than had been disclosed either to the Exchange or publicly.

[20] After various further inquiries and responses between the Exchange and Desert Lion, the Exchange initiated a review of the Desert Lion senior management team to assess their suitability to act as directors or officers of a listed issuer. On June 7, 2019, the Exchange sent a letter to the directors and officers of Desert Lion asking for responses to a number of issues related to the financing.

[21] On June 21, 2019, in a letter signed on behalf of the company by Mr. Johnston, Desert Lion responded to the Exchange's letter. Key elements of its response are summarized below:

a) Regarding the concern that Desert Lion had proceeded to effect a $1,000,000 discount after being advised of the Exchange's objections, Desert Lion responded that it had understood the Exchange's primary concern to be with convertibility and did not appreciate that the discount was problematic. Desert Lion acknowledged that clearer communications by it "may have avoided the apparent misunderstanding…".

b) Regarding the lack of disclosure of the $1,000,000 discount in the November 5, 2018 news release, Desert Lion described it as an "oversight", emphasizing that its attention at the time had been on its dire financial situation.

c) Regarding the disclosure in the December 10, 2018 news release that it had received gross proceeds of $5,000,000 on closing, Desert Lion attributed the problem to confusion over the treatment of the discount.

d) Regarding Desert Lion's failure to identify the default provisions associated with the Covenant, which the Exchange considered to be both material and likely to be triggered very quickly (as proved to be the case), Desert Lion acknowledged that the terms should have been mentioned in the Form 4B but also referenced arguments for why it did not consider them material at the time.

e) Regarding certain financing expenses which were not initially disclosed, Desert Lion attributed the lack of disclosure to inadvertence, noting that full disclosure was made in its year-end financial statements.

[22] The Exchange subsequently commenced a further suitability review specific to Mr. Johnston. On October 11, 2019, after Mr. Johnston had ceased to be a director or officer of Desert Lion or any other Exchange-listed issuer, the Exchange sent Mr. Johnston a letter asking for his responses to a number of concerns.

[23] A reply on Mr. Johnston's behalf was delivered on October 24, 2019. Key elements of the reply are summarized as follows:

a) Regarding his obligation as President and CEO and as a director of Desert Lion to ensure compliance with the Exchange's requirements, Mr. Johnston emphasized that his attention had been focused on operational and technical matters. In that regard, he said that on August 22, 2018 his role within Desert Lion had changed such that he was no longer the President and CEO, but only the CEO.

b) Regarding the failure to disclose the $1,000,000 discount in the November 5, 2018 news release, Mr. Johnston acknowledged that "with the benefit of hindsight the disclosure should have been more fulsome". He added that given his changed role in Desert Lion, his focus at the time was on running the business and completing the necessary financing. He also emphasized, as he did in response to a number of the Exchange's concerns, that he "believed, at the time, based on the advice of counsel and [his] understanding of the Company's disclosure obligations, that the disclosure was appropriate".

c) Regarding the issues with the initial form 4B, Mr. Johnston questioned whether he had been the person who signed the document. He noted that he is not a lawyer and relied throughout on the legal expertise of internal counsel, who drafted the documents and interacted with the Exchange. Mr. Johnston stated that the lawyers involved "were trained at top tier Canadian law firms and thus I had no reason to believe I could not rely on their legal work".

d) Mr. Johnston blamed the "inherent complexity of convertible securities" for what he described as a misunderstanding between Desert Lion and the Exchange.

[24] Exchange staff took Mr. Johnston's responses and various other materials and prepared a summary and recommendation memorandum in contemplation of a decision to be made by the appropriate representative of the Exchange. On May 11, 2019, the Exchange sent the Decision to Mr. Johnston.

B. The Decision

[25] The Decision requires Mr. Johnston "to make a written application to and obtain prior written acceptance from the C&D Department of the Exchange for any proposed involvement as a Director or Officer of any Exchange listed issuer or perform functions for any Exchange listed issuer which are similar to those normally performed by an individual occupying the position of Director or Officer". The Decision also notes that the Exchange "will not consider an application regarding your involvement as a Director

or Officer unless the application is also made on your behalf by an Exchange listed issuer. That issuer will be required to provide the Exchange with satisfactory evidence that a copy of this letter has been received and reviewed by the Issuer".

[26] The Decision states that its determination is made pursuant to section 2.3(a) of Exchange Policy 3.1, certain agreed terms contained in the Personal Information Form (PIF) which Mr. Johnston submitted to the Exchange, and Section 4.1 of the Exchange's listing agreement with Desert Lion.

C. Powers of the Exchange

[27] The Exchange is a stock exchange recognized by the Commission under section 24 of the Act and pursuant to a recognition order that sets out terms and conditions the Exchange must fulfil, including a requirement to require listed issuers to comply with securities legislation and the rules and policies of the Exchange. Decisions taken by the Exchange are subject to review by the Commission.

[28] The Exchange is a private entity that applies its own rules and policies to issuers who contract to list on the Exchange and to those individuals who, by virtue of their involvement with listed issuers, agree to adhere to the terms of that contractual relationship. Those rules and policies, which were approved by the Commission, are set out in the Exchange's listings manual and committed to in the listing agreement signed by each listed issuer.

[29] Some of the provisions establishing the powers of the Exchange generally and the terms extending those powers to Mr. Johnston by contract are set out below.

[30] Policy 3.1 of the Exchange, dealing with directors, officers and corporate governance, includes the following provisions:

> **Exchange Policy 3.1**
> **Exchange Discretion**
> 2.1 The Exchange considers the Directors, Officers and other Insiders, as well as certain other people involved with an Issuer, to be important factors in determining whether to accept and/or maintain the listing of an Issuer. The Exchange will exercise discretion in considering all factors related to the Directors, Officers and other Insiders of an Issuer, as well as certain other people involved with the Issuer.
>
> 2.2 In exercising its discretion, the Exchange may review the conduct of Directors, Officers, other Insiders, Promoters, significant securityholders, Control Persons, employees, agents and consultants in order to satisfy itself that:
> (a) the business of the issuer is and will be conducted with integrity and in the best interests of its securityholders and the investing public; and
> (b) Exchange Requirements and the requirements of all other regulatory bodies having jurisdiction are and will be complied with.
> 2.3 In exercising the Exchange's discretion regarding individuals involved or proposed to be involved with an Issuer, the Exchange may:

(a) prohibit an individual from serving as a Director or Officer or being an Insider of an Issuer or impose restrictions on any Director, Officer or other Insider;

…

5.4 Each Director and Officer must exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

5.5 Director and Officers of an Issuer must ensure that the Issuer complies with the applicable Exchange Requirements, corporate and Securities Laws.

[31] Desert Lion's listing agreement with the Exchange contains the following provision:

4. **Directors, Officers and other Personnel**

4.1 The affairs of the Issuer shall at all times be managed or supervised by at least three directors, all of whom shall:

(a) be individuals qualified to act as directors under the Issuer's incorporating statute and Exchange Requirements;
(b) act honestly and in good faith and in the best interests of the Issuer;
(c) exercise the care, diligence and skill of a reasonably prudent person in the exercise of their duties as directors;
(d) not be personally indebted to or subject to an unsatisfied or incomplete term of a sanction of the Exchange or any securities regulatory body; and
(e) be otherwise acceptable to the Exchange.

Officers, employees, agents and consultants of the Issuer, and others engaged by or working on behalf of the Issuer, shall be subject to all other specified Exchange Requirements and, at the discretion of the Exchange, shall be subject to clauses 4.1(d) and 4.1(e) above.

[32] The Exchange also requires that every director and officer submit a Form 2A – Personal Information Form (PIF). The PIF dated October 15, 2017 that Mr. Johnston signed and delivered to the Exchange includes the following statutory declaration made by him:

(e) I hereby agree to (i) submit to the jurisdiction of each of the Exchanges and to the Investment Industry Regulatory Organization of Canada and any successor or assignee of any of them, and wherever applicable, the directors and committees thereof, and (ii) be bound by and comply with all applicable rules, policies, regulations, directions, decisions, orders and rulings of each of the Exchanges (collectively, the "Exchange requirements");

…

(g) I agree that any acceptance, approval or other right granted by the Exchanges may be revoked, terminated or suspended any time in accordance with the then applicable Exchange requirements. In the event of any such revocation, termination or suspension, I agree to immediately terminate my association or involvement with any Exchange issuer to the extent required by the Exchanges. I agree not to resume my association or involvement with any Exchange issuer, except with the prior written approval of the Exchanges;

III. Analysis

A. What Standard of Review Applies?

[33] Mr. Johnston brought this application under section 28(1) of the Act. That section reads as follows:

> **Review of action**
> **28** (1) The executive director or a person directly affected by a direction, decision, order or ruling made under a bylaw, rule or other regulatory instrument or policy of a clearing agency, exchange, quotation and trade reporting system, self-regulatory body or trade repository may apply by notice to the commission for a hearing and review of the matter under Part 19, and section 165 (3) to (9) applies.

[34] The first question that arises for decision by the panel concerns the appropriate standard to be applied by the Commission on its review of a decision of the Exchange: must the panel determine that the Exchange's decision is correct, or only that it is reasonable?

[35] BC Policy 15-601 sets out the principles and procedures established by the Commission to govern hearings held by it. For the purposes of that policy, the Exchange constitutes a "Recognized Entity". Section 7.9(a) of Policy 15-601 reads as follows:

> **7.9 Form and scope of reviews of a decision under sections 28 and 165**
> ***(a) Where the review of a Recognized Entity decision proceeds as an appeal*** –
> The Commission does not provide parties with a second opinion on a matter decided by a Recognized Entity. If the decision under review is reasonable and was made in accordance with the law, the evidence, and the public interest, the Commission is generally reluctant to interfere simply because it might have made a different decision in the circumstances. For this reason, generally, the person requesting the review presents a case for having the decision revoked or varied and the Recognized Entity responds to that case.
>
> The Commission generally confirms the decision of the Recognized Entity, unless:
> - the Recognized Entity has proceeded on an incorrect principle
> - the Recognized Entity has made an error in law
> - the Recognized Entity has overlooked material evidence
> - new and compelling evidence is presented to the Commission or
> - the Commission's view of the public interest is different from that of the Recognized Entity

[36] Mr. Johnston asserts that we should review the Decision on a correctness standard. The Exchange argues that the appropriate course is to defer in the first instance to a decision of the Exchange, presuming it to be reasonable, unless the applicant can prove to the satisfaction of the panel that one or more of the criteria set out above in section 7.9(a) applies, rendering the decision unreasonable. Only then, says the Exchange, should the Commission apply a correctness standard in its review. The executive director shares the Exchange's view.

[37] Mr. Johnston initially relied on the recent Supreme Court of Canada decision in *Canada (Minister of Citizenship and Immigration) v. Vavilov*, [2019] SCC 65. Mr. Johnston argues that following *Vavilov*, a correctness standard of review is appropriate given that there exists a specific statutory regime granting appellate authority to the Commission, a statutory body with a public interest mandate, over decisions of the Exchange, a commercial enterprise having a contractual relationship with its listed issuers.

[38] Both the Exchange and the executive director argue that *Vavilov*, which is applicable to the review of administrative decisions by courts, has no application to a review of a decision of the Exchange, a private entity, by the Commission, an administrative body. We agree, and we note that by the time of the oral hearing in this matter, Mr. Johnston placed significantly less emphasis on this line of argument.

[39] Mr. Johnston's primary argument regarding the standard of review we should apply references the decision of the British Columbia Court of Appeal in *Investment Industry Organization of Canada v. Rahmani*, 2010 BCCA 93. Following a hearing and review by the Commission of a decision of the predecessor to the Investment Industry Regulatory Organization of Canada (IIROC), another private entity that regulates its members by contract, IIROC appealed the Commission's order, arguing that the Commission is required to give significant deference to a decision of a self-regulatory organization (SRO). At paragraph 45, the Court of Appeal concluded otherwise:

> 45 As with all decisions it makes under the *Act*, the Commission exercises its authority according to its view of the public interest. The Commission need not give deference to a recognized SRO's view of the public interest and that is reflected in Section 5.9(a) of *BC Policy 15-601*.
> …

[40] Mr. Johnston urges us to read the Court of Appeal's conclusion in *Rahmani* as a direction that, given our supervisory role over the Exchange, we must apply a correctness standard to our review of the Decision. Mr. Johnston urges us to perform our own analysis of all of the issues he has raised and substitute our views for those expressed in the Decision. We do not agree that the suggested approach flows from the *Rahmani* analysis or is the appropriate approach.

[41] The decision in *Rahmani* that the Commission is not required to defer to the view taken by an SRO is settled law in British Columbia and was not disputed by either the Exchange or the executive director. The question in each case is whether there are circumstances that cause the panel to conclude that it should interfere with the decision reached by the SRO.

[42] We are of the view that it is within our power to apply a correctness standard in any review of an Exchange decision which properly comes before us. However, this does not imply that we should automatically apply a correctness standard. We have a discretion to exercise in reviewing Exchange decisions. The Commission has chosen to adopt in Policy 15-601 a principled general policy which takes account of the factors usually

considered in similar situations here and across Canada. It also empowers each panel in each application to apply that policy with appropriate flexibility.

[43] We see nothing in the circumstances of this proceeding which should lead us not to apply the principles set out in section 7.9(a) of Policy 15-601. Accordingly, unless Mr. Johnston can show that the Exchange proceeded on an incorrect principle, made an error of law or overlooked material evidence, or our view of the public interest differs from that of the Exchange, we will not interfere with the Decision.

[44] Regarding discretionary elements of decisions made by the Exchange, we adopt and repeat the following language from the panel in *Re Chilean Metals Inc.*, 2019 BCSECCOM 24 at para. 119:

> The Exchange plays a significant role as a gatekeeper in our capital markets. Part of that role, as a gatekeeper (as set out in the Exchange's recognition order from the Commission), is the enforcement of its rules and policies in the public interest. With the authority to enforce its rules and policies, must come some latitude for the Exchange to reasonably use its discretion to apply, waive or modify (through the imposition of conditions) those rules and policies in a nuanced manner, applicable to the specific circumstances of each situation. This concept is clearly reflected in Policy 1.1, section 4.1 of the TSXV Manual, as outlined above.

B. Did the Exchange Have Jurisdiction to Make the Decision, Does the Decision Fetter the Exchange's Discretion?

[45] Mr. Johnston argues that the Decision is outside the Exchange's jurisdiction, and that it impermissibly fetters the Exchange's discretion in any future consideration of Mr. Johnston as a proposed director or officer of a listed issuer. He characterizes both matters as errors of law that compel this panel to apply a correctness standard and to substitute our views for those of the Exchange.

[46] Mr. Johnston acknowledges that its rules and policies afford the Exchange broad discretion to assess the fitness of an existing or proposed officer or director of a listed issuer, but argues that they do not confer any jurisdiction on the Exchange to impose terms and conditions on the circumstances in which an individual will be accepted by the Exchange, where that person is neither involved with an issuer at the time, nor proposed to be involved with an issuer.

[47] Mr. Johnston asks us to recognize that the Decision will have significant practical consequences for him. He does not suggest that his prior conduct should not be considered in any future application by him for Exchange approval. Instead, Mr. Johnston argues that the appearance that the Exchange has already made findings against Mr. Johnston will dissuade any company from proposing Mr. Johnston for any form of Exchange approval. Mr. Johnston suggests that given this barrier to obtaining support from listed issuers, the Decision bars him from senior roles for many market participants in his particular field of expertise.

[48] The position of the Exchange is that it has not yet made a decision on the substance of the question of whether Mr. Johnston is unsuitable to be a director or officer of a listed issuer based on his conduct in connection with Desert Lion. The Exchange submits that it "has in no way determined (and has therefore not prejudged) whether it will accept the Applicant as a director or officer in the future".

[49] We have carefully reviewed the Decision to form our own opinion as to the effect of the Decision and how the Decision should properly be characterized.

[50] The Decision begins with a description of the materials reviewed by the decision maker and follows with three paragraphs under the heading "Decision", the substance of which we have summarized above. The Decision then continues with a description of the factual background, including this statement:

> We note that the responses provided in your letter, dated October 24, 2019, (written in response to our letter written October 11, 2019) were not satisfactory and did not alleviate our concerns.

[51] The Decision then includes the heading "Reasons for the Exchange's Determination". Under that heading is an introductory paragraph followed by a number of conclusions about misconduct by Desert Lion. The introductory paragraph reads as follows:

> Our determination and restrictions placed on you are based on our conclusions that the Company contravened Exchange Requirements during your tenure as CEO, President and a Director. As CEO, President and a Director, you held a responsibility to ensure the Company fully complied with Exchange Requirements. The Company materially failed, in multiple instances, to comply with very fundamental Exchange Requirements as detailed below:.

[52] The Decision does not analyze the specifics of Mr. Johnston's personal involvement in Desert Lion's breaches or provide any analysis of Mr. Johnston's position that he relied on legal advice (except that the Decision references those responses in the October 24, 2019 letter as quoted above).

[53] Our characterization of the Decision is as follows:

a) The Exchange found that Desert Lion had materially breached fundamental Exchange requirements;

b) The Exchange found that Mr. Johnston had a duty to ensure that Desert Lion complied with Exchange requirements;

c) The Exchange considered Mr. Johnston's assertions of reliance on legal advice unsatisfactory and not deserving of any detailed analysis at that stage; and

d) The Exchange imposed conditions on future applications by Mr. Johnston for Exchange approval which would necessitate that Mr. Johnston address the concerns it raised in the Decision with the informed support of whatever listed issuer Mr. Johnston was then applying to join.

[54] While the Decision states that the Exchange considered Mr. Johnston's submissions, which included his submissions regarding his reliance on legal advice, and that those submissions did not alleviate the Exchange's concerns, the Decision does not limit his ability to provide more detailed and specific submissions in the future. The balance of the decision, and especially the relief provided, is procedural.

[55] With respect to Mr. Johnston's comments about the practical impact of the Decision on his employment future, we accept that it may have some impact. However, we find it hard to quantify that impact. Mr. Johnston concedes that the Exchange is entitled to consider the events related to Desert Lion in connection with any future application by him to serve as a director or officer of a listed issuer. In any potential future application, Mr. Johnston would be motivated to make advanced disclosure of the Exchange's expected concerns to any issuer he might seek to join. That being so, the potential roadblock to Mr. Johnston's return to a management position with an Exchange-listed issuer arises from the fact that unresolved issues about his past conduct will re-emerge upon any future application for approval, and not from the Decision itself.

[56] We return to the issue of whether the Exchange had jurisdiction to impose conditions on future approval applications by Mr. Johnston at a time when Mr. Johnston was no longer a director or officer and was not then applying to become a director or officer of a listed issuer. Exchange Policy 3.1 governs matters involving directors and officers of listed issuers. Section 2.3(a) of that policy states that, in exercising "the Exchange's discretion involving individuals involved or proposed to be involved with an Issuer, the Exchange may … prohibit an individual from serving as a Director or Officer" or impose restrictions on any director or officer. Section 4.1 of that policy states that each director must "be otherwise acceptable to the Exchange." It is clear that the Exchange's jurisdiction extends to regulating those who propose involvement with a listed issuer, which is when the Decision actually takes effect. The Decision does no more than define, in advance, the information which must be provided to the Exchange and the process that must be followed if Mr. Johnston proposes to become a director or officer of another Exchange-listed issuer. In our view, the Exchange's right and obligation to assess the suitability of an applicant for such a position is a critical aspect of its role as a gatekeeper in our capital markets.

[57] We also note that in signing the declaration attached to his PIF, Mr. Johnston expressly agreed to be bound by any rulings of the Exchange, and that if any acceptance, approval or other right granted by the Exchange were revoked, terminated or suspended, not to resume association or involvement with any Exchange-listed issuer except with the prior approval of the Exchange. The Decision applies a consequence explicitly contemplated by the declaration.

[58] We conclude that the Exchange has the jurisdiction to evaluate the acceptability of an applicant and the associated jurisdiction to establish, in its discretion, procedures for conducting such an evaluation. Those procedures can be customized in particular circumstances, such as those in Mr. Johnston's case. The existence of jurisdiction is a legal question on the basis of which we would interfere if the Exchange was in error. It is not.

[59] We note the submissions of the Exchange committing, on the record of this proceeding, that it has not reached conclusions regarding the suitability of Mr. Johnston to be a director or officer of a listed company in future or regarding how it might address arguments made by Mr. Johnston at that time. We are not suggesting that post-Decision behavior by the Exchange is an answer to any of the issues raised in this proceeding. We are deciding each issue on the merits of that issue. But if Mr. Johnston was concerned that a potential future employer might be unclear about Mr. Johnston's future ability to raise issues about the appropriateness of his own conduct and have the Exchange consider those issues with fresh eyes, the positions taken by the Exchange in this proceeding should resolve any lack of clarity.

[60] The above conclusions that the Decision is merely procedural in effect and that no decision has been made about Mr. Johnston's suitability to be a director or officer of an Exchange-listed issuer in future also resolve any suggestion that the Exchange's discretion has been fettered. We find that it has not and, accordingly, that the Exchange has made no legal error in that regard.

C. Is Mr. Johnston's Reliance on Legal Advice an Answer?

[61] Most of Mr. Johnson's arguments were focused on the propositions that he relied throughout on Desert Lion's internal legal counsel to interact with the Exchange, complete all required filings, and see to all required disclosure, and that that reliance constitutes a complete defence to any sanction by the Exchange. That argument is at the core of Mr. Johnston's submission about the appropriateness of his conduct, it is at the core of his submission that the Exchange overlooked evidence and arguments in conducting its assessment, and it is at the core of his submission that the reasons expressed by the Exchange in the Decision are not adequate. Mr. Johnston relies on the Exchange's alleged failure to consider all material evidence as cause for this panel to apply a correctness standard of review of the Decision pursuant to section 7.9(a) of Policy 15-601.

[62] The Exchange's argument in this regard is four-fold:

(a) Its rules and policies do not provide for such a defence; rather, they specifically assign responsibility to the directors and officers of a listed issuer to ensure that the issuer complies with Exchange requirements and securities laws;

(b) No such defence is available to Mr. Johnston under corporate or securities law;

(c) Reliance on legal advice is an argument that in securities law can be relevant only to the issue of what sanction is appropriate in any particular circumstance; and

(d) In any event, the defence cannot be established in Mr. Johnston's case, where there was a complete delegation of responsibility to counsel, there was no evidence of specific advice sought or given, and certain of the documents in issue were wrong on their face.

[63] The availability of a defence of reliance on legal advice has been considered by various securities commissions at various times. The leading decision is *Mega-C Power Corp et al*, 2010 ONSEC 19. In that case, the Ontario Securities Commission considered an argument of reliance on legal advice and left open the question of whether the argument amounted to a legal defence. In the course of its reasoning, the Ontario Securities Commission addressed, at paragraph 261, the requirements that would have to be proved to make out the defence, if it existed:

> Assuming, without deciding, that the defence of reliance on legal advice is available to Mr. Pardo, on the facts of this case the defence will fail unless he can establish four things:
> - the lawyer had sufficient knowledge of the facts on which to base the advice;
> - the lawyer was qualified to give the advice;
> - the advice was credible given the circumstances under which it was given; and
> - that Mr. Pardo made sufficient enquiries and relied on the advice.

[64] The same factors were explicitly adopted in the subsequent decision of the Ontario Securities Commission in *David Charles Phillips et al.,* 2015 ONSEC 24, at paragraph 212:

> Both Phillips and Wilson testified that they received legal advice that they could not disclose the Grant Thornton Report. The Commission has previously held that even if a defence of reliance on legal advice is available, that defence will fail unless the respondent can establish four things: …

[65] In *Re Robinson,* 2013 ABASC 203, the Alberta Securities Commission adopted the same approach of setting out the factors that would have to be satisfied in order to establish the defence, if it exists. In *Arbour Energy Inc.*, the Alberta Securities Commission concluded that reliance on legal advice would at best amount to a submission related to sanction, rather than a substantive defence. In the course of reaching that conclusion, the Alberta Securities Commission noted that even if the defence existed in law, it would not apply on the facts of the case before it because the factors enumerated in *Mega-C* had not been made out.

[66] This Commission has weighed in on the availability of a defence of reliance on legal advice on more than one occasion. In one important decision, *Re HRG Healthcare*, 2015 BCSCCOM 326, the Commission concluded that the argument could only go to sanction:

> [66] The respondents submit that they received legal advice to the effect that HRG was not required to disclose the bonuses paid by HRG as they were not commissions for the purposes of the required disclosure. First, the respondents did not provide any evidence in support of this submission, nor the factual basis given to the lawyer who supposedly provided this advice. Second, even if they did receive this advice, we find that these bonuses were required to be disclosed in the EDRs and the receipt of incorrect advice can only go to the question of sanction and not liability.

[67] There has been considerable consistency expressed by Canadian securities regulators about what would be needed to prove a defence of reliance on legal advice, assuming the defence exists, but considerable doubt about whether the defence exists in the context of an administrative proceeding to enforce securities laws. However, a recent decision of a panel of this Commission in *Re SunCentro Corporation et al.,* 2017 BCSECCOM 58, takes a different approach. The key analysis from that decision is set out below:

> **Availability of a Due Diligence Defence**
>
> [59] …the availability of a due diligence defence to an alleged contravention of section 61 of the Act is dependent on whether there is such a defence in the common law.
>
> [60] In *R. v. Sault Ste. Marie (City)*, [1978] 2 S.C.R. 1299 (S.C.C.), 1978 CanLII 11 (SCC), (CanLII), pg. 1325, the Supreme Court of Canada recognized three categories of offences: offences for which *mens rea* must be proved; strict liability offences for which there is no necessity to prove the existence of *mens rea*, leaving it open to an accused to avoid liability by proving that they took all reasonable care; and absolute liability offences, which assign guilt without having to prove the subjective intent of the accused.
>
> [61] The question is whether a contravention of section 61, which proceeds in an administrative process before a Commission panel, is an absolute liability offence or a strict liability offence.
>
> …
>
> [64] We agree that previous Commission decisions and decisions of securities regulatory authorities across the country do not provide clear guidance on this issue.
>
> [65] The executive director submits that the British Columbia Court of Appeal decision in *Whistler Mountain Ski Corp. v. British Columbia (General Manager Liquor Control and Licensing Branch)*, 2002 BCCA 426 provides precedential guidance for the proposition that contraventions of the Act that are pursued in the administrative context should be strict, and not absolute, liability offences. We agree.

> [66] In *Whistler Mountain*, our Court of Appeal looked at a regulatory regime under which enforcement proceedings could be pursued under both criminal or quasi-criminal proceedings and under administrative or regulatory proceedings. Administrative proceedings under that regime could result in significant sanctions being imposed for contraventions. The Court of Appeal expressly rejected the notion that these types offences that are dealt with in administrative/regulatory proceedings should be absolute liability offences. The Court of Appeal stated (para. 29):
>
> • A public welfare offence should be interpreted as a strict liability offence for which the defence of due diligence is available, unless there is clear legislative language that indicates an offence is one of absolute liability: R. v. Martin (1991) 63 C.C.C. (3d) 71 (Ont. C.A.), aff'd [1992] 1 S.C.R. 838
>
> [67] The enforcement regime under the Act is analogous to that considered by the Court of Appeal in Whistler Mountain in that our administrative/regulatory proceedings may lead to significant financial sanctions being imposed on respondents. We also do not see language in the Act that provides clear legislative language that such contraventions are to be absolute liability offences. In fact, section 1.9 of the CP suggests an interpretation of securities regulatory statutes by securities regulators that is not consistent with absolute liability offences in this context. We do not see a reason to deviate from the reasoning in Whistler Mountain as it applies to administrative/regulatory proceedings under the Act.
>
> **Consideration of a Due Diligence Defence in this case**
>
> [68] Having found that a due diligence defence is available in the context of alleged contraventions of section 61, the question becomes whether such a defence was made out in the facts and circumstances of this case.

[68] The *SunCentro* case arose in the context of alleged breaches of section 61 of the Act. It does not necessarily follow that alleged breaches of requirements of the Exchange that arise under contract between Mr. Johnston and the Exchange rather than under the Act will lead to the same conclusion. It is unnecessary in these proceedings to resolve that issue here, as the initial question of whether a defence of reliance on legal advice can be established on the facts of this case is determinative of the matter. In the absence of a proper factual foundation for it, we do not need to determine whether or not the legal defence exists.

[69] We turn to a more detailed analysis of the conduct of Mr. Johnston which he submits can be explained by his reliance on legal advice.

[70] The initial agreement executed between Desert Lion and AIP was executed on behalf of Desert Lion by Mr. Johnston. In the letter the Exchange wrote to Mr. Johnston on October 11, 2019, alerting Mr. Johnston that it was reviewing his suitability, the Exchange asked Mr. Johnston about that document. Mr. Johnston did not suggest at that time, and he has not suggested since, that he was unaware of the essential terms of the

agreement. Mr. Johnston did indicate that he "had been advised that all appropriate and necessary disclosure had been made to the TSX." He went on to note that he relied on legal counsel to clear the agreement with the Exchange, saying that he had no reason to doubt that he could rely on their legal work.

[71] Desert Lion then issued the November 5, 2018 news release that is summarized above, which purports to quote Mr. Johnston in describing "AIP's commitment to investment of a minimum of $5,000,000…".

[72] In its October 11, 2019 letter, the Exchange asked Mr. Johnston about that news release. Mr. Johnston's reply includes his acknowledgement that the news release "should have been more fulsome" and a partial explanation that at the time he had been focused on the business of Desert Lion, given its financial difficulties. Mr. Johnston also said that he believed at the time based on the advice of counsel that the disclosure was appropriate. We take that as an admission by Mr. Johnston that he was aware of the content of the news release.

[73] Mr. Johnston signed the initial form 4B, also described above, which did not disclose the planned $1,000,000 discount. When the Exchange studied the agreements which accompanied the Form 4B, the Exchange had serious concerns.

[74] Extensive discussions followed between Desert Lion and the Exchange during which the Exchange advised that the discount from the face value of the AIP investment was unacceptable. Desert Lion then negotiated new terms with AIP which did not in fact eliminate the discount, although it was implied in communications between Desert Lion and the Exchange that the Exchange's concern regarding the discount had been addressed. Desert Lion later explained the issue as a misunderstanding on its part, although an innocent one. Mr. Johnston acknowledged that he was copied on many of the communications which were a part of the misunderstanding, but noted that the authors of the communications on behalf of Desert Lion were lawyers authorized to lead the discussions and he relied on them to perform the work properly.

[75] On December 10, 2018, Desert Lion issued a further news release which announced "gross proceeds of $5,000,000", without any mention of the $1,000,000 discount.

[76] In explaining both the November 5, 2018 news release and the December 10, 2018 news release, Mr. Johnston includes a comment in his October 24, 2019 letter to the effect that there was no intent to mislead the public. Again, emphasizing that he relied on advice as to the appropriateness of the disclosure, he implicitly admits that he was aware of the fact of the disclosure.

[77] We have reviewed the statements and the related conduct of Mr. Johnston which were of concern to the Exchange. We do not consider it necessary to provide our analysis of each event which Mr. Johnston explains by reference to reliance on legal advice. Depending on what future applications are made on Mr. Johnston's behalf and what level of detail

and specificity is provided, the Exchange may at some point have to do that. For present purposes it is sufficient if we address just one issue, that of the disclosure in the November 5 and December 10, 2018 news releases.

[78] There is no ambiguity in the November 5 and December 10, 2018 news releases. Read fairly and as a whole, each of those news releases would indicate to a member of the public, whether a casual and uninformed reader or an informed reader reasonably familiar with the financial position of Desert Lion, that Desert Lion would receive gross proceeds of $5,000,000, from which certain expenses would be deducted. This was never to be the case, and we consider the lack of candour in the two news releases to be a very serious matter which, in and of itself, would justify significant concern by the Exchange.

[79] Counsel for Mr. Johnston argued against the above conclusion with a number of points which together suggest that Desert Lion and its managers and advisors were aware of other transactions which had been approved by the Exchange and which had included a discount between the face amount of a financing and the proceeds paid by the investor, so therefore Desert Lion had a reasonable basis to believe the transaction with AIP was appropriate and would be approved by the Exchange. Even if that is so, it does not address the main underlying concern about the news releases, which is the false impression they create about what proceeds Desert Lion would receive.

[80] When announcing a transaction which clearly and unequivocally will not generate proceeds in excess of $4,000,000, a news release is false if it indicates that proceeds will be higher. This is not a question of any complexity or one which turns on an analysis of the law. The disclosure was wrong on its face.

[81] Assuming without deciding that directors of listed companies under the jurisdiction of the Exchange can rely upon a due diligence defence, including one based on reliance on legal advice, the party asserting the defence has the onus to establish the elements of the defence.

[82] In the securities law context, it is very difficult to imagine a situation where a respondent can make out a defence of reliance on legal advice simply by asserting the fact that legal advice was received and relied upon. Any decision maker given the responsibility of considering the defence must be given the facts from which to assess the presence or absence of the factors enumerated in *Mega-C* and the other decisions that reference it.

[83] Mr. Johnston did not provide any reasonable basis upon which the Exchange could reasonably evaluate the *Mega-C* factors. Mr. Johnston also did not provide us any reasonable basis upon which we could reasonably evaluate the *Mega-C* factors.

[84] Instead of doing what he might have done to provide an evidentiary foundation for a potential defence of reliance on legal advice, Mr. Johnston chose to be vague. The Exchange was not told what advice was sought or given, and the Exchange was not given a proper factual context to assess the reasonableness of Mr. Johnston's asserted reliance.

We conclude that although Mr. Johnston asserted that a defence of reliance on legal advice existed, he failed to provide sufficient evidence to allow the merits of the defence to be evaluated.

D. Does the Decision Provide Adequate Reasons?

[85] Finally, Mr. Johnston relies on the alleged inadequacy of the Exchange's reasons for decision as cause for this panel to substitute its view of the matter for the view of the Exchange. Our analysis of this topic is relatively brief because we have already stated our conclusions above on two issues which are relevant here. First, we have concluded that the Decision does not determine whether Mr. Johnston is suitable or unsuitable as a director or officer of an Exchange-listed issuer in the future. This is significant because we consider that the level of detail and analysis which must be given to support any particular decision will vary based upon the nature of the decision being made. Secondly, we have concluded that where a due diligence defence might exist on the basis of reliance on legal advice, the onus is on the party raising the defence to assert it and to present the evidence necessary to support it. When told that his suitability was being reviewed and when asked a number of key factual questions, Mr. Johnston provided the Exchange with little more than an assertion that he had relied on legal counsel to ensure that appropriate disclosure had been made. This is relevant to the degree of detail which would be necessary for a decision maker to provide in order to respond to the argument.

[86] Mr. Johnston's primary argument regarding the adequacy of the Decision is based on the principles enunciated in *Re Hudbay Minerals Inc.*, 2009 ONSEC 15. In that case, the Toronto Stock Exchange had made a decision about the listing of common shares of HudBay Minerals Inc. to be issued in the context of a proposed business combination between that company and Lundin Mining Corporation. The Toronto Stock Exchange's corporate manual listed certain factors to be taken into account in decisions of that type, but the decision that was issued not to require shareholder approval of the transaction did not enumerate those factors. The Ontario Securities Commission held:

> In our view, however, in order for us to defer to the decision of the Filing Committee, we must be able to determine the facts and circumstances that were before the Filing Committee and the factors and considerations it weighed. We must also be able to understand the reasoning the TSX applied in making its decision. As stated in *Northwestern Utilities*, "conclusions without any hint of the reasoning process" are not enough. Adequate reasons or some other reasonable explanation are particularly important in this case because it involves a decision (not to require a HudBay shareholder vote) that is controversial, has very significant consequences to the parties directly affected and to other market participants, and involves considerations as to market quality and integrity.
>
> In a review under section 21.7 of the Act, in order for us to defer to a decision of the TSX, we must have a reasonable basis to do so on the evidence before us. We have an obligation as a supervisory body not to defer to a decision that we cannot conclude is made on a reasonable basis.

[87] Mr. Johnston does not assert that no basis was given for the Exchange's Decision, but that a key argument was ignored. Mr. Johnston asserts that the Exchange failed to take into account the claim of reliance on legal advice which Mr. Johnston raised repeatedly in his October 24, 2019 letter to the Exchange. Mr. Johnston characterizes this failure as a failure to consider relevant arguments, a failure to consider relevant evidence and a fatal defect in the Decision.

[88] We do not accept Mr. Johnston's submission.

[89] Our view that the reasons for the Decision were sufficient is influenced by an aspect of the Supreme Court of Canada's decision in *Vavilov*. That decision is most often cited for its analysis of presumptions which should be made about the standard of review applicable in judicial review applications. *Vavilov* also addresses the topic of the duty of administrative decision makers to provide adequate reasons, including at paragraphs 91 to 95:

> [91] A reviewing court must bear in mind that the written reasons given by an administrative body must not be assessed against a standard of perfection. That the reasons given for a decision do "not include all the arguments, statutory provisions, jurisprudence or other details the reviewing judge would have preferred" is not on its own a basis to set the decision aside: *Newfoundland Nurses*, at para. 16. The review of an administrative decision can be divorced neither from the institutional context in which the decision was made nor from the history of the proceedings.
>
> [92] Administrative decision makers cannot always be expected to deploy the same array of legal techniques that might be expected of a lawyer or judge — nor will it always be necessary or even useful for them to do so. Instead, the concepts and language employed by administrative decision makers will often be highly specific to their fields of experience and expertise, and this may impact both the form and content of their reasons. These differences are not necessarily a sign of an unreasonable decision — indeed, they may be indicative of a decision maker's strength within its particular and specialized domain. "Administrative justice" will not always look like "judicial justice", and reviewing courts must remain acutely aware of that fact.
>
> [93] An administrative decision maker may demonstrate through its reasons that a given decision was made by bringing that institutional expertise and experience to bear: see *Dunsmuir*, at para. 49. In conducting reasonableness review, judges should be attentive to the application by decision makers of specialized knowledge, as demonstrated by their reasons. Respectful attention to a decision maker's demonstrated expertise may reveal to a reviewing court that an outcome that might be puzzling or counterintuitive on its face nevertheless accords with the purposes and practical realities of the relevant administrative regime and represents a reasonable approach given the consequences and the operational impact of the decision. This demonstrated experience and expertise may also explain why a given issue is treated in less detail.

> [94] The reviewing court must also read the decision maker's reasons in light of the history and context of the proceedings in which they were rendered. For example, the reviewing court might consider the evidence before the decision maker, the submissions of the parties, publicly available policies or guidelines that informed the decision maker's work, and past decisions of the relevant administrative body. This may explain an aspect of the decision maker's reasoning process that is not apparent from the reasons themselves, or may reveal that an apparent shortcoming in the reasons is not, in fact, a failure of justification, intelligibility or transparency. Opposing parties may have made concessions that had obviated the need for the decision maker to adjudicate on a particular issue; the decision maker may have followed a well-established line of administrative case law that no party had challenged during the proceedings; or an individual decision maker may have adopted an interpretation set out in a public interpretive policy of the administrative body of which he or she is a member.
>
> [95] That being said, reviewing courts must keep in mind the principle that the exercise of public power must be justified, intelligible and transparent, not in the abstract, but to the individuals subject to it. It would therefore be unacceptable for an administrative decision maker to provide an affected party formal reasons that fail to justify its decision, but nevertheless expect that its decision would be upheld on the basis of internal records that were not available to that party.

[90] We read the Decision in the context of what would have been known to Mr. Johnston at the time. Mr. Johnston would have known that his arguments as to reliance on legal advice had been made in his counsel's letter of October 24, 2019. In that context Mr. Johnston would have known from the Decision's reference to that letter (where it said that "the responses … were not satisfactory and did not alleviate our concerns") that his arguments had been considered and were not considered persuasive. If Mr. Johnston had provided a more specific argument which properly addressed the factors we have identified above as important in a defence of reliance on legal advice, we might have found that the Exchange was obligated to address the defence in more detail. Similarly, if the Exchange were making a final decision about Mr. Johnston's suitability to be a director or officer of an Exchange-listed issuer in the future, we might have found that the Exchange was obligated to address Mr. Johnston's defence in more detail. As it is, however, we conclude that the reasons provided in the Decision were adequate in the circumstances and that there is no merit to the suggestion that important evidence or arguments were overlooked.

IV. Conclusion

[91] We have concluded that the Exchange had the jurisdiction to issue the Decision and that there is no proper basis for us to interfere with it. As a result, this application is dismissed.

February 19, 2021

For the Commission:

Gordon Johnson
Vice Chair

Judith Downes
Commissioner

Marion Shaw
Commissioner