

# 2003 BCSECCOM 184

COR#03/036

## Decision

**Carl Glenn Anderson and Douglas Victor Montaldi**

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

## Hearing

<b>Panel</b>	Brent W. Aitken	Vice Chair
	Neil Alexander	Commissioner
	Robert J. Milbourne	Commissioner

**Date of Hearing** February 26, 2003

**Date of Decision** March 7, 2003

### Appearing

James Sasha Angus For Commission staff  
Lorne Herlin

Robert W. Taylor For Carl Glenn Anderson and Douglas Victor Montaldi  
Carey D. Veinotte

Susan A. Griffin For Area Finance Inc.

### Introduction

- ¶ 1 This decision should be read with our Findings in this matter, made on February 14, 2003 (see 2003 BCSECCOM 132). On February 26, 2003, we heard submissions on the matter of sanctions. Area Finance Inc. applied for standing to make submissions on sanction, and we granted its application. Area Finance is the successor company to the business of 439288 B.C. Ltd. (439) under the Proposal described in the Findings.
- ¶ 2 The respondents Anderson and Montaldi were the principals of a business operated by 439 from January 1, 1996 to April 30, 2002. 439's principal business was represented to investors as the making of loans to individuals and small businesses in and around Burns Lake, British Columbia. To raise the necessary capital for its lending activities, it sold promissory notes to investors. 439's

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operations came to an end when the British Columbia Financial Institutions Commission (FICOM) froze its bank accounts and ordered it to cease carrying on business at the end of April 2002. By then, 439 had raised \$41 million from approximately 450 investors, nearly all of whom are residents of the Burns Lake area.

### Findings

- ¶ 3 Anderson and Montaldi admitted to trading and distributing securities without being registered and without filing a prospectus, contrary to sections 34 and 61 of the *Securities Act*, RSBC 1996, c. 418. In addition, we found that Anderson and Montaldi:
- made misrepresentations, contrary to section 50(1)(d) of the Act;
  - perpetrated a fraud on persons in British Columbia, contrary to section 57(b) of the Act; and
  - acted contrary to the public interest.
- ¶ 4 We found that Anderson and Montaldi made misrepresentations to investors by failing to disclose that the funds from new investors were used to pay interest and capital due to existing investors. This is significant. Based on what they were told by Anderson and Montaldi, investors believed that the funds 439 used to pay them their capital and interest came from the business of lending their funds to borrowers, not by obtaining new funds from new investors. As noted in the Findings, many investors said that had they known about this, they would have thought twice about investing.
- ¶ 5 We found that Anderson and Montaldi perpetrated a fraud by failing to disclose to investors the true state of 439's financial affairs, and by using investors' funds for their own purposes. This was dishonest conduct. Again, the evidence makes it clear that some investors, had they known about 439's cash problems and the related party loans, would have asked more questions before deciding to invest.
- ¶ 6 We found that Anderson and Montaldi acted contrary to the public interest by failing to keep adequate records to allow 439 to keep track of payments due to it by borrowers, and by failing to adequately supervise the collection of loans. They also chose not to prepare financial statements on a timely basis, or to rely on them in running the business. As a result of these failures, Anderson and Montaldi were unable to monitor the performance of the business and its profitability, a major contributor to the investors' losses. This conduct, we found, was in breach of their duties as directors and officers of 439 under the *Company Act*, RSBC 1996, c. 62.

### Discussion

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¶ 7 In *Re Eron Mortgage Corporation* [2000] 7 BCSC Weekly Summary 22, the Commission discussed the factors relevant to sanction as follows (at page 24):

In making orders under sections 161 and 162 of the Act, the Commission must consider what is in the public interest in the context of its mandate to regulate trading in securities. The circumstances of each case are different, so it is not possible to produce an exhaustive list of all of the factors that the Commission considers in making orders under sections 161 and 162, but the following are usually relevant:

- the seriousness of respondent's conduct,
- the harm suffered by investors as a result of the respondent's conduct,
- the damage done to the integrity of the capital markets in British Columbia by the respondent's conduct,
- the extent to which the respondent was enriched,
- factors that mitigate the respondent's conduct,
- the respondent's past conduct,
- the risk to investors and the capital markets posed by the respondent's continued participation in the capital markets of British Columbia,
- the respondent's fitness to be a registrant or to bear the responsibilities associated with being a director, officer or adviser to issuers,
- the need to demonstrate the consequences of inappropriate conduct to those who enjoy the benefits of access to the capital markets,
- the need to deter those who participate in the capital markets from engaging in inappropriate conduct, and
- orders made by the Commission in similar circumstances in the past.

¶ 8 This list of factors has to be read in light of *Re Cartaway Resources Corp.* 2002 BCCA 461, where the court held that the Commission cannot consider general market deterrence in issuing sanctions (at paragraph 98):

. . . past misconduct is relevant only to the extent that it may lead the Commission to conclude that future misconduct by the respondent, not by any and all other market participants, is likely.

¶ 9 Applying these factors to this case:

- Anderson's and Montaldi's conduct was serious. By the time 439 was shutdown by FICOM, Anderson and Montaldi had raised \$41 million from over 450 investors, much of it through misrepresentation and fraud. Once in possession of investors' funds, they managed them poorly and invested

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them for their own purposes and not for the proper conduct of 439's business, with the result that 439 became insolvent.

- The full extent of the deprivation suffered by investors is as yet unknown, but some degree of deprivation is certain: the investors' funds, originally invested on a short-term basis, are now tied up for seven years, and their return is only one-quarter of what they were originally promised. For some investors, this has already resulted in significant inconvenience and suffering.
- This sort of conduct, with these kinds of consequences, damages the integrity of British Columbia's capital markets.
- Anderson and Montaldi also benefited substantially by loaning investors' funds to themselves, not repaying the principal, not paying interest on it, and causing 439 to forgive some interest altogether.
- In mitigation, both Anderson and Montaldi have guaranteed repayment of all the investors' funds and have pledged all of their current and after-acquired assets as security for those guarantees. An additional mitigating factor in Anderson's case is his acceptance of the criticisms in the Pricewaterhouse report of his and Montaldi's conduct.

¶ 10 The Proposal contemplates that Anderson and Montaldi be directors and officers of Area Finance. Both they and Area Finance argue that their continued involvement in Area Finance is necessary for that company's success, and that any concerns about their fitness to act are put to rest by Area Finance's governance structure. They point out that the investors in 439 voted heavily in favour of the Proposal, and that when they voted, the investors were aware of the related party loans, 439's investment in its other assets, and the criticisms in the Pricewaterhouse report of Anderson's and Montaldi's conduct of the business.

¶ 11 Given their conduct, we do not think that Anderson and Montaldi are fit to be directors or officers of an issuer raising money from the public, and that there would be considerable risk to investors and British Columbia's capital markets by allowing them to do so. However, it appears to be the will of the current 439 and Area Finance investors to have Anderson, at least, remain involved. He is regarded as essential if Area Finance and 439 are to maximize collections under their current loans. Under these unusual circumstances, we believe that it is in the interests of the current investors that we permit Anderson to remain involved with Area Finance and 439 to deal with the current loan portfolios, as long as no new investors are brought into these companies. There is less evidence about the

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importance of Montaldi's role and it is more equivocal. The main rationale for Anderson's continued involvement (his knowledge of, and relationships with, the borrowers) does not appear to apply to Montaldi.

- ¶ 12 We do, however, have significant concerns over Anderson's involvement if Area Finance were to decide to raise new capital from new investors. His conduct shows he is not fit to have a significant role in an issuer raising money from the public, and we are not confident that the Area Finance governance arrangements address all the issues of concern. For example:
- None of the Area Finance directors appears to have any experience in overseeing or managing a lending business; indeed, it is not clear that any of the directors has any experience or training at all regarding the obligations of being a director of a company that raises money from the public. It is not always necessary that directors have expertise directly related to the business of the company concerned, but when they do not, they are completely reliant in those areas on the expertise of management. In this case, they would essentially be relying on Anderson.
  - Even today, with the temporary orders in place, it appears that Area Finance is, putting it charitably, interpreting those orders rather liberally. Anderson's title is "Manager", but he has the same authority to bind the company and sign cheques as any other single officer or director, and appears to be the person with primary responsibility for the making and collecting of loans, which is currently the only business of Area Finance. He is being paid \$160,000 annually. The board oversees his activities directly, which is more consistent with a senior officer position than a lower management one. It is difficult to distinguish Anderson's current duties and compensation from those that would be associated with an officer of Area Finance, considering the nature of its current operations.
  - The board's lending policy leaves considerable discretion in the hands of the loans officer (which, for loans up to \$75,000, is Anderson acting alone). Although there are "guidelines" for analyzing loan applications, these guidelines defer to "the loans officer's personal knowledge about the applicant and their overall qualifications, including future creditworthiness". It appears that the effect is that Anderson will be free to make the same judgments about borrowers that he has made in the past, which led to 65% of 439's loan portfolio being classified in the Fair, Poor, and Bad categories. The lending policy also appears to allow any loan of less than \$75,000 to be made without security, and any loan below \$35,000 to be made without any

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security, without a credit check, and without the borrower having to produce a net worth statement.

- The lending policy requires the board's credit committee to approve any loans above \$75,000, and states that the credit committee must have "knowledge applicable to the granting of credit", but we have no evidence before us that the current members of the credit committee have that expertise. To the contrary, the evidence we have on the point suggests that they do not. Nor do we have any evidence of the percentage of the Area Finance loan portfolio that is expected to fall above the \$75,000 threshold, so we have no insight into how much of Area Finance's lending business will be subject to credit committee approval.
- The lending policy sets out a detailed process for collecting delinquent loans. The policy does not set the criteria for delinquency, but it sets performance targets for delinquent loans as a percentage of the total portfolio. The target is for delinquent loans to be less than 3% of the total portfolio. The policy says that if the target is missed, then the target is to "reduce the delinquent loan balances by 2% each month" but imposes no overall timeframe in which the loan portfolio must re-achieve the general 3% target.

¶ 13 Considering these controls as a whole, we believe that there remains a substantial risk that the result could be Anderson's carrying on the business much as he has in the past. The majority of the current investors may have concluded that this is acceptable for them, but we do not think the controls are adequate to protect new investors coming into Area Finance if Anderson is playing the primary operational role.

¶ 14 It is also not certain that Area Finance needs to raise new capital in order to succeed in making the original 439 investors whole. We questioned several witnesses on this point, and although they testified that it was likely to be difficult for Area Finance to do so without new capital, all acknowledged it was possible.

### **Orders – Anderson**

¶ 15 Considering it to be in the public interest, we order:

1. under section 161(1)(c) of the Act, that the exemptions described in sections 44 to 47, 74, 75, 98 and 99 of the Act do not apply to Anderson for a period of 12 years, except that he may trade in securities for his own account through a single account with a person registered to trade securities under the Act;

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2. under section 161(1)(d)(i) of the Act, that Anderson resign any position he holds as a director or officer of any issuer, other than: (a) 439, on condition that 439 does not issue any securities; (b) Area Finance, on condition that Area Finance does not issue any securities to any person that is not a securityholder of Area Finance as of the date of this order; (c) an issuer, all of the securities are owned directly and beneficially by him, his wife or his children; (d) the issuers listed in Appendix A to this decision, on condition, with respect to each issuer, that the issuer not issue any securities;
3. under section 161(1)(d)(ii) of the Act, that Anderson is prohibited from becoming or acting as a director or officer of any issuer, other than the issuers described in paragraph 2, for 12 years;
4. under section 161(1)(d)(iii) of the Act, that Anderson is prohibited from engaging in investor relations activities, except to the extent necessary to facilitate the operations of loans for Area Finance, on condition that Area Finance does not issue any securities to any person that is not a securityholder of Area Finance as of the date of this order;
5. under section 162 of the Act, that Anderson pay an administrative penalty of \$200,000; and
6. under section 174 of the Act, that Anderson pay, jointly and severally with Montaldi, the costs of or related to the hearing incurred by the Commission and the Executive Director, the amount to be determined following further submissions from the parties.

### **Orders – Montaldi**

¶ 16 Considering it to be in the public interest, we order:

1. under section 161(1)(c) of the Act, that the exemptions described in sections 44 to 47, 74, 75, 98 and 99 of the Act do not apply to Montaldi for a period of 12 years, except that he may trade in securities for his own account through a single account with a person registered to trade securities under the Act;
2. under section 161(1)(d)(i) of the Act, that Montaldi resign any position he holds as a director or officer of any issuer, other than: (a) an issuer, all of the securities are owned directly and beneficially by him, his wife or his children; (b) the issuers listed in Appendix B to this decision, on condition, with respect to each issuer, that the issuer not issue any securities;

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3. under section 161(1)(d)(ii) of the Act, that Montaldi is prohibited from becoming or acting as a director or officer of any issuer, other than the issuers described in paragraph 2, for 12 years;
  4. under section 161(1)(d)(iii) of the Act, that Montaldi be prohibited from engaging in investor relations activities for 12 years;
  5. under section 162 of the Act, that Montaldi pay an administrative penalty of \$200,000; and
  6. under section 174 of the Act, that Montaldi pay, jointly and severally with Anderson, the costs of or related to the hearing incurred by the Commission and the Executive Director, the amount to be determined following further submissions from the parties.
- ¶ 17 We direct Commission staff to send a bill of costs to Anderson and Montaldi on or before March 31, 2003, and we direct Anderson and Montaldi to make submissions relating to the bill of costs on or before April 21, 2003.

March 7, 2003

### **For the Commission**

Brent W. Aitken  
Vice Chair

Neil Alexander  
Commissioner

Robert J. Milbourne  
Commissioner



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## Appendix A

J & B Services Ltd.  
Key-Oh Logging Ltd.  
Lakes District Envirowood Ltd.  
Gerobeco Holdings Ltd.  
Anderson Lindaas Logging Ltd.  
376688 B.C. Ltd  
489876 B.C. Ltd.  
346280 B.C. Ltd.  
Nordic Ford Ltd.  
Glenn Anderson Insurance Ltd.  
Maronnette Holdings Ltd.  
O'Sullivan's Fine Clothing Ltd.  
610022 B.C. Ltd.

## Appendix B

J & B Services Ltd.  
Key-Oh Logging Ltd.  
Lakes District Envirowood Ltd.  
DVM Holdings Ltd.  
Omineca Lama Ranch Inc.  
Raymark Enterprises Ltd.  
Beartoe Resorts Ltd.  
Frame Realty (1984) Ltd.  
346280 B.C. Ltd.  
573796 B.C. Ltd.  
476284 B.C. Ltd.  
497868 B.C. Ltd.