

Citation: 2014 BCSECCOM 26

**Cinnabar Explorations Inc., Christopher James G. Bass,
Daniel Grant McGee and Dale Zucchet**

Securities Act, RSBC 1996, c. 418

Hearing

Panel	Bradley Doney	Commissioner
	Audrey T. Ho	Commissioner
	Don Rowlatt	Commissioner

Submissions completed November 28, 2013

Date of Decision January 17, 2014

Submissions filed by
Veda Kenda For the Executive Director

Christopher James G. Bass For himself

Decision

I Introduction

¶ 1 This is the sanctions portion of a hearing under sections 161(1), 162 and 174 of the *Securities Act*, RSBC 1996, c. 418. Our Findings on liability made on September 3, 2013 (2013 BCSECCOM 361) are part of this decision.

¶ 2 We found that:

1. Cinnabar Explorations Inc., Christopher James G. Bass, and Dale Zucchet contravened section 61(1) of the Act when they illegally distributed Cinnabar shares for proceeds of \$21,500 from seven investors without having filed a prospectus, and
2. Zucchet contravened section 50(1)(d) when, with the intention of effecting a trade in Cinnabar shares, he made statements to a Commission staff investigator that he knew or ought to have known were misrepresentations.

II Positions of the Parties

¶ 3 The executive director seeks orders:

1. permanently cease trading Cinnabar securities, and permanently prohibiting Cinnabar from trading in securities,
2. permanently prohibiting Bass from acting as a director or officer of any issuer, and prohibiting him for a period of 8-10 years from trading securities, acting as a registrant or promoter, acting in a management or consultative capacity in connection with activities in the securities market, and engaging in investor relations activities,
3. prohibiting Zucchet, for a period of 8-10 years, from acting as a director or officer of any issuer, trading securities, acting as a registrant or promoter, acting in a management or consultative capacity in connection with activities in the securities market, and engaging in investor relations activities,
4. requiring Cinnabar and Bass to disgorge \$21,500,
5. requiring Bass and Zucchet to pay an administrative penalty of \$20,000 each, and
6. that the prohibitions remain in place until the financial orders are paid, including, in the case of Bass, \$3,500 outstanding from a previous decision of the Commission.

¶ 4 Bass submitted that it would be more appropriate if he were asked to pay back to investors the \$21,500 and attend a training course for directors and officers. He says no additional administrative penalty or prohibitions would be appropriate.

¶ 5 Zucchet did not appear at the hearing on sanctions and filed no submissions.

III Analysis

A. Factors

¶ 6 In *Re Eron Mortgage Corporation* [2000] 7 BCSC Weekly Summary 22, the Commission identified 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.”

Seriousness of the conduct; damage to markets

¶ 7 Contraventions of section 61 are inherently serious because that section is a part of the foundation requirements for protecting investors and the integrity of capital markets. Section 61(1) requires that those who wish to distribute securities file a prospectus with the Commission, so that investors and their advisors get the information they need to make an informed investment decision. The specific requirements for exemptions from section 61(1) are designed to protect investors and markets, so an issuer who intends to rely on the exemptions must ensure they are met. Any contravention of section 61(1) is therefore inherently serious: *Corporate Express Inc.* 2006 BCSECCOM 153, *Solara Technologies Inc. and William Dorn Beattie*, 2010 BCSECCOM 357.

Enrichment

¶ 8 The executive director entered into evidence at the hearing a banking analysis of the cheques drawn on and cash withdrawn from Cinnabar's bank account in an attempt to trace how the money raised by Cinnabar through the share distributions was spent. There is no evidence on how the cash withdrawn from the account was spent. Of the cheques drawn on Cinnabar's bank account, the evidence suggests that Bass received only \$4,000 for expenses and does not suggest that Bass was personally enriched. The evidence does indicate that Zucchet was personally enriched in that he was paid \$3,000 as consulting fees.

Harm to investors

¶ 9 There is harm to the investors. Cinnabar has been subject to a cease trade order since July 21, 2011. There is no evidence that Cinnabar shares have any present or future value or that the investors could recover their funds.

Mitigating or aggravating factors

¶ 10 There are no mitigating or aggravating factors beyond Bass' past regulatory misconduct.

Past conduct

¶ 11 Bass was sanctioned by the Commission in *Capital Reserve Inc. et al* ([1988] BCSC Weekly Summary 98; 1988 LNBCSC 685). The Commission found that Bass allowed

himself to be used as a nominee president and director for a co-respondent, thereby assisting that individual in executing his scheme and serious violations of the Act, which included an illegal take-over bid, illegal distributions from a control position, failure to make timely disclosure of material changes, misrepresentations in prospectus and news releases, and late filing of insider trading reports. The Commission banned Bass from acting as a director or officer for a period of four years, and ordered him to pay \$3,500 for costs related to that hearing. To date, those costs remain unpaid.

¶ 12 There is no evidence that Zucchet has any history of regulatory misconduct.

Risk to investors and markets; fitness as director, officer, advisor

¶ 13 Although Bass himself raised only \$3,000 of the \$21,500 illegal distributions from only two investors, as Cinnabar's chief executive officer, he was responsible for ensuring that the claimed exemptions were in fact available to Cinnabar. But he made no effort to do so; he accepted without question the representations on availability of exemptions as stated in the subscription agreements signed by investors.

¶ 14 Zucchet testified that he did not know the rules regarding exempt distributions, yet he made no effort to learn them. Indeed, he told an undercover Commission staff investigator posing as a potential investor that the financial eligibility tests for the exemptions were "legal jargon" and that the investigator could still make a purchase even though he did not meet those eligibility tests.

¶ 15 Bass' and Zucchet's carelessness and indifference to learning about and ensuring regulatory compliance when raising capital present a risk to our capital markets were they permitted to continue in the capital markets without restrictions.

Specific and general deterrence

¶ 16 The sanctions we impose must be sufficiently severe to ensure that the respondents and others will be deterred from engaging in similar conduct.

¶ 17 Bass was registered as an investment advisor with a national investment dealer for a brief period in 1986-1987. He had been a director of an issuer and was sanctioned for misconduct as a director. He should have been aware of, and complied with, his regulatory obligations.

¶ 18 That he did not do so indicates that a market ban and administrative penalty are warranted to protect the public and deter future misconduct.

¶ 19 Zucchet did not know the rules yet did not bother to find out about them. Instead, he told the staff investigator posing as an investor that the language in the forms was just "legal jargon". Zucchet also made misrepresentations. In our view, a market ban and administrative penalty are also warranted.

Previous orders

- ¶ 20 We considered the following past decisions of the Commission cited by the executive director.
- ¶ 21 In *John Arthur Roche McLoughlin, MCL Ventures Inc., Blue Lighthouse Ltd. and Robert Douglas Collins* 2011 BCSECCOM 299, the Commission found that Blue Lighthouse and Collins raised \$317,636 from 22 investors through illegal distributions, purporting to rely on exemptions that were not available. Collins received \$14,607 in commission. The Commission banned Collins from the capital markets for five years, and ordered him to pay an administrative penalty of \$20,000 and disgorge the \$14,607.
- ¶ 22 In *Solara* (cited above), the Commission found that the respondents raised \$790,000 from 46 investors through illegal distributions, without taking sufficient care to ensure that the requirements of the exemptions were met. In addition, the Commission found that Solara and Beattie filed false and misleading reports with the Commission and made misrepresentations to the investors in the offering memorandum regarding Beattie's salary. The Commission found that Solara and Beattie did not knowingly contravene the Act but were sloppy about ensuring that exemptions were available. The Commission banned Beattie from the capital markets for five years, ordered him to pay an administrative penalty of \$50,000, but did not order disgorgement. The Commission permitted Beattie to continue to act as a director and officer of Solara.
- ¶ 23 In *VerifySmart Corp.* 2012 BCSECCOM 176, the Commission found that the respondents raised over \$1.2 million from 99 investors through illegal distributions, purporting to rely on exemptions that were not available. The Commission banned Scammel and de Beer from the capital markets for five years, ordered them to each pay an administrative penalty of \$50,000, and ordered them and the issuers to disgorge the \$1.2 million raised.
- ¶ 24 The executive director also cited *Pacific Ocean Resources Corporation and Donald Verne Dyer* 2012 BCSECCOM 104, but in our opinion the facts of that case are very different from those here and so we did not find it helpful.

B. Orders

Cease trade orders

- ¶ 25 There is no evidence that Cinnabar shares have any present or future value or that the company is active. We agree with the executive director that Cinnabar should be permanently cease traded, and that Cinnabar itself should be permanently prohibited from trading in securities.
- ¶ 26 With respect to Bass, we agree with the executive director that a market ban is appropriate. Although Zucchet does not have any history of regulatory misconduct, a

market ban is also appropriate to protect the public in light of his casual attitude to the law and his misrepresentations.

- ¶ 27 In our opinion it is not appropriate to prohibit them from acting as registrants. The misconduct we found does not support that prohibition, given that none of it had anything to do with conduct as a registrant. That said, were either of them to apply for registration, his conduct in this case would be a relevant consideration in the decision whether to grant registration.
- ¶ 28 We find that the duration of the market ban proposed by the executive director to be high in light of the circumstances, even after we take into account Bass' regulatory history. There is no evidence that Bass or Zucchet deliberately set out to contravene the Act; they were careless and did not pay attention to their regulatory obligations.
- ¶ 29 We find that a market ban of five years against Bass and Zucchet to be appropriate.

Disgorgement

- ¶ 30 When the Commission has found an illegal distribution, it is often appropriate in the circumstance to order disgorgement of the amount raised: *VerifySmart Corp.*
- ¶ 31 We find that it is appropriate to order Cinnabar and Bass to disgorge the \$21,500 raised in contravention of the Act.
- ¶ 32 Although there was no evidence of personal enrichment by Bass, we find that it is appropriate to order him to disgorge the entire \$21,500 given that he was a director and the chief executive officer of Cinnabar at the relevant times and should be held responsible for Cinnabar.
- ¶ 33 Although the evidence appears to us to support a \$3,000 disgorgement order against Zucchet, the executive director did not seek any disgorgement from Zucchet so we have not done so.

Administrative penalty

- ¶ 34 We considered in particular the *Blue Lighthouse* decision in determining the appropriate amount of administrative penalty.
- ¶ 35 Even though the scale of the illegal distributions here is significantly less than that in *Blue Lighthouse* and the other authorities cited by the executive director, the executive director submitted that a \$20,000 administrative penalty (same as that ordered against Collins in *Blue Lighthouse*) is appropriate because Bass' prior misconduct and Zucchet's disregard of the law should balance out the lesser scale of the illegal distributions here.

- ¶ 36 The amount illegally raised by Cinnabar was less than 7% of the amount illegally raised in *Blue Lighthouse*. Collins (a director of Blue Lighthouse and the one who made the significant decisions about its affairs) was only ordered to disgorge the amount he personally received from the illegal distributions. Here, there is no evidence of personal enrichment by Bass but we are ordering him to disgorge the total amount that was illegally raised. When we weigh the relative small scale of the illegal distributions and the magnitude of the disgorgement order we are making against Bass personally against Bass' past misconduct, we find that a penalty of \$10,000 is significant and adequate for deterrence.
- ¶ 37 Bass presented some evidence regarding his current health, but we do not find that relevant in determining the appropriate sanction. He also submitted that he was in financial hardship but presented no corroborating evidence in that regard, so we have not considered whether financial hardship should be relevant here.
- ¶ 38 The executive director asked us to order that the sanctions we issue today remain in place until Bass pays the \$3,500 levied in 1988. We do not feel it is necessary to link the sanctions today to sanctions from a proceeding some 25 years ago on a different matter, assuming we have the authority to do so. Rather, we consider the non-payment of that amount when determining the magnitude of the sanctions here, and we note it remains open to the executive director to pursue collection of that amount.
- ¶ 39 Zucchet was responsible for bringing in most of the illegally raised funds and was the individual who made the misrepresentations. He received consulting fees for his work. We find that an administrative penalty is necessary for deterrence. As with Bass, we find that a penalty of \$20,000, as proposed by the executive director, is high in light of the far smaller scale of the illegal distributions weighed against the nature of his misconduct. But we are of the view that Zucchet should pay a higher administrative penalty than Bass given their relative conduct. We find that an administrative penalty of \$15,000 against Zucchet is appropriate.

III Orders

- ¶ 40 Considering it to be in the public interest, we order that:

Cinnabar

1. under section 161(1)(b), Cinnabar permanently cease trading in, and is prohibited from purchasing, any securities or exchange contracts;
2. under section 161(1)(g), Cinnabar pay to the Commission \$21,500, being the outstanding amount obtained, directly or indirectly, as a result of contraventions of the Act, provided that the aggregate amount paid by Cinnabar and by Bass under paragraph 5 shall not exceed \$21,500;

Bass

3. under section 161(1)(d)(i), Bass resign any position he holds as a director or officer of an issuer or registrant, and
4. until the later of January 16, 2019 and the date on which the payments ordered in paragraphs 5 and 6 have been made, Bass is prohibited from:
 - a. under section 161(1)(b), trading in securities, except that he may trade and purchase securities through accounts in his own name at a registered dealer;
 - b. under sections 161(1)(d)(ii), becoming or acting as a director or officer of any issuer or registrant;
 - c. under section 161(d)(iii), becoming or acting as a promoter;
 - d. under section 161(1)(d)(iv), acting in a management or consultative capacity in connection with activities in the securities market; and
 - e. under section 161(1)(d)(v), engaging in investor relations activities;
5. under section 161(1)(g), Bass pay to the Commission \$21,500, being the outstanding amount obtained, directly or indirectly, as a result of contraventions of the Act, provided that the aggregate amount paid by Bass and by Cinnabar under paragraph 2 shall not exceed \$21,500; and
6. under section 162, Bass pay an administrative penalty of \$10,000;

Zucchet

7. under section 161(1)(d)(i), Zucchet resign any position he holds as a director or officer of an issuer or registrant, and
8. until the later of January 16, 2019 and the date on which the payment ordered in paragraph 9 has been made, Zucchet is prohibited from:
 - a. under section 161(1)(b), trading in securities, except that he may trade and purchase securities through accounts in his own name at a registered dealer;
 - b. under sections 161(1)(d)(ii), becoming or acting as a director or officer of any issuer;
 - c. under section 161(d)(iii), becoming or acting as a promoter;

- d. under section 161(1)(d)(iv), acting in a management or consultative capacity in connection with activities in the securities market; and
 - e. under section 161(1)(d)(v), engaging in investor relations activities; and
9. under section 162, Zucchet pay an administrative penalty of \$15,000.

¶ 41 January 17, 2014

¶ 42 For the Commission

Bradley Doney
Commissioner

Audrey T. Ho
Commissioner

Don Rowlatt
Commissioner