BRITISH COLUMBIA SECURITIES COMMISSION
Section 171 of the *Securities Act*, RSBC 1996, c. 418

Citation: Re Loughery, 2019 BCSECCOM 78 Date: 20190304

Stewart Douglas Loughery and Military International Limited

Panel	Nigel P. Cave	Vice Chair
	Judith Downes	Commissioner
	Gordon Holloway	Commissioner

Hearing date	January 9, 2019
Submissions Completed	January 9, 2019
Date of decision	March 4, 2019

Appearing

David Hainey	For the Executive Director

Decision

I. Introduction

[1] This is the sanctions portion of a hearing under sections 161(1) and 162 of the *Securities Act*, RSBC 1996, c. 418. The Findings of this panel on liability made on April 27, 2018 (2018 BCSECCOM 134) are part of this decision.

[2] We found that:

(a) the respondents contravened a cease trade order issued by the executive director on December 11, 2002; and

(b) Loughery, acting as either a *de facto* officer or director of Military International Limited, authorized, permitted or acquiesced to Military's contravention of the cease trade order and thereby, pursuant to section 168.2(1) of the Act, also contravened the cease trade order.

[3] The parties were given an opportunity to make written and oral submissions with respect to the appropriate sanctions in this case. The executive director provided written and oral submissions.

[4] The hearing with respect to sanctions was originally scheduled for September 4, 2018. At 10:02 am on September 4, 2018 (i.e. after the commencement of the hearing), Loughery applied for, and obtained, an adjournment of the sanctions hearing for medical reasons. The hearing was rescheduled for January 9, 2019. On the morning of January 9, 2019, Loughery

applied for a further adjournment of the sanctions hearing for medical reasons. We dismissed that application on January 9, 2019, with reasons to follow.

[5] Prior to Loughery's adjournment application, neither of the respondents had provided written submissions. Therefore, the sanctions hearing proceeded without written or oral submissions from either of the respondents.

[6] These are our reasons with respect to dismissing Loughery's application for a further adjournment of the sanction hearing. This is also our decision with respect to sanctions.

II. Adjournment application

[7] Loughery's adjournment application for medical reasons was accompanied by doctor's notes authorizing his absence from work. There was nothing in the notes from the doctor indicating that they had been prepared in contemplation of our proceedings. The medical evidence gave no indication as to why Loughery would not have been able to prepare written submissions on sanctions (yet he was able to prepare a lengthy e-mail requesting an adjournment) or to attend the sanctions hearing in person or by phone to give oral submissions.

[8] On September 4, 2018, when we granted a lengthy adjournment in response to Loughery's previous adjournment application, we made it clear that our expectation was that if there were potental issues relating to Loughery's participation in the adjourned hearing, he would provide sufficient advance notice of those issues in order that attempts at accommodating any health related matters could be made.

[9] The Commission's record of the September 4, 2018 proceeding was provided to Loughery outlining the expectations for any subsequent adjournment application, outlined above.

[10] Loughery's January 9, 2019 adjournment application, again, arrived on the morning of the rescheduled hearing. He made no attempt to provide advance notice, and his application materials gave no reason for not doing so.

[11] There is a significant public interest in ensuring that our enforcement proceedings are handled in a timely and efficient manner. The respondents were provided with sufficient opportunity to provide written and oral submissions on sanctions. As a consequence, we dismissed Loughery's adjournment application.

III. Position of the parties on sanctions

[12] The executive director sought the following sanctions against Loughery in this case:

(a) under section 161(1)(d)(i), that Loughery resign any position he holds as a director or officer of an issuer or registrant;

(b) that Loughery be prohibited, for the later of six years or until such time as the amounts referred to in paragraphs 12(b) and (c) below have been paid:

i. under section 161(1)(d)(ii), from becoming or acting as a director or officer of any issuer;

ii. under section 161(1)(d)(iii), from acting as a registrant or promoter;

iii. under section 161(1)(d)(iv), from acting in a management or consultative capacity in connection with activities in the securities market; and

iv. under section 161(1)(d)(v), from engaging in investor relations activities.

(c) under section 161(1)(g), that Loughery pay to the Commission $170,000, being the amount he obtained indirectly as a result of his contraventions, payable on a joint and several basis with Military pursuant to paragraph 13(b) below; and

(d) under section 162, an administrative penalty of $30,000.

[13] The executive director seeks the following orders against Military:

(a) under section 161(1)(b)(i), that all persons cease trading in the shares of Military for the later of five years or until such time as the amounts referred to in paragraphs 13(b) and (c) below have been paid;

(b) under section 161(1)(g), that Military pay to the Commission $170,000, being the amount it obtained directly as a result of its contravention, payable on a joint and several basis with Loughery pursuant to paragraph 12(c) above, and

(c) under section 162, an order for an administrative penalty of $20,000.

[14] The executive director argued that his submissions on the appropriate financial sanctions set out above with respect to Loughery should be considered in totality and that, if we did not make an order under section 161(1)(g) against him, we should consider a larger administrative penalty under section 162 (from that set out above) to achieve the goals of specific and general deterrence.

IV. Analysis

A. Factors

[13] Orders under sections 161(1) and 162 of the Act are protective and preventative, intended to be exercised to prevent future harm. See *Committee for Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission)*, 2001 SCC 37.

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

B. Application of the factors

Seriousness of the Conduct

[15] Cease trade orders are one of the Commission's most important tools in protecting the capital markets. Failure to comply with them undermine the Commission's ability to effectively regulate the capital markets. Contravening a cease trade order is therefore serious misconduct.

[16] In this case, the misconduct is made more serious by evidence that the respondents' breach of the cease trade order was intentional. Loughery was advised by Commission staff prior to Military entering into loan agreements with investors that attempts by Military to enter into financing agreements might constitute a contravention of the cease trade order.

[17] Finally, Loughery's misconduct is also made more serious by his previous status as a registrant under the Act. That previous registration status would have, or should have, made him aware of the role of the Commission in regulating the capital markets, the significance of a cease trade order issued by the Commission, and the seriousness of any subsequent contravention of such an order.

Harm suffered by investors and the enrichment of the respondents

[18] The investors who provided the loans to Military have all suffered financial loss – none of that money has been repaid. We heard testimony from investors as to the financial impacts of those losses.

[19] Military has also been enriched by their misconduct. Military received, in first instance, the proceeds raised from its contraventions of the cease trade order.

Aggravating or mitigating circumstances

[20] There are no mitigating circumstances in this case.

[21] With respect to Loughery, there is the aggravating factor of his prior history of securities regulatory misconduct. He was previously sanctioned by a securities self-regulatory body (the Investment Dealers Association of Canada) in 2002 for misconduct that occurred while he was a registrant.

Participation in our capital markets and fitness to be a registrant or a director or officer

[22] The intentional breach of a cease trade order demonstrates an unwillingness to comply with the directives of the regulator in a highly regulated industry. Those who breach such orders must be viewed as a significant risk to our capital markets.

[23] In this case, Loughery was in *de facto* control of Military and was largely responsible for causing it to contravene the cease trade order. This demonstrates the risk he poses to the capital markets if he were allowed to continue to act as a director or officer of an issuer.

Specific and general deterrence

[24] The sanctions that we impose must be sufficient to establish that both the respondents and others will be deterred from breaches of cease trade orders.

[25] Our orders must also be proportionate to the misconduct (and the circumstances surrounding it) of the respondents.

Previous decisions

[26] The executive director directed us to two recent decisions of this Commission involving the contravention of a previously issued order: *Re Malone*, 2016 BCSECCOM and *Re Jardine*, 2016 BCSECCOM.

[27] Both *Malone* and *Jardine* involved contraventions by the respondents of previous orders made specifically against the applicable respondent following enforcement proceedings. In that sense, the misconduct in both *Malone* and *Jardine* is more serious than in the present case. However, in neither *Malone* nor *Jardine* was there direct investor losses arising from the respondents' misconduct or evidence of direct financial enrichment to the respondents. Therefore, the cases are not directly applicable but are helpful as rough guidance in terms of the applicable sanctions.

[28] In *Malone*, the panel ordered that the respondent be subject to broad market prohibitions lasting for seven years and that he pay an administrative penalty of $60,000. In *Jardine*, the panel ordered that the respondent be subject to broad market prohibitions lasting for seven years and that he pay an administrative penalty of $40,000.

Analysis of appropriate orders

Market prohibitions

[29] The executive director sought a prohibition under section 161(1)(b)(i) of the Act, that all persons cease trading in the securities of Military for a period of five years or until such time as all financial sanctions imposed on Military are paid. In addition, the executive director sought orders imposing broad market prohibitions against Loughery to last for six years or until all financial sanctions imposed upon Loughery are paid by him.

[30] This case is unusual in that there is an existing cease trade order outstanding under section 161(1)(b)(i) of the Act with respect to the securities of Military. The existing order is of an indefinite length but could, in theory, be revoked upon the rectification of the disclosure deficiencies that led to its issuance. We are concerned about the existence of two separate orders under section 161(1)(b)(i), one time limited and the other not, with respect to the securities of Military and any confusion that may arise as a consequence. Therefore, we think the proper course of action is to vary, under section 171 of the Act, the existing cease trade order with respect to the securities of Military to take into account the orders that we think are appropriate arising from this proceeding.

[31] The suggested length of the market prohibitions of five and six years, respectively, are generally consistent with the previous decisions of this Commission for misconduct of this type. That Loughery's prohibitions should be of a longer duration is also appropriate given that he has an aggravating factor (a prior history of securities regulatory misconduct, albeit unrelated to this misconduct) and that he was largely responsible for Military's misconduct. The length of the market prohibitions suggested by the executive director are also proportionate to the misconduct in this case.

Section 161(1)(g) orders

[32] The executive director submitted that we should make an order under section 161(1)(g) of the Act, jointly and severally, against Loughery and Military in the amount of $170,000.

[33] The British Columbia Court of Appeal in *Poonian v. British Columbia Securities Commission*, 2017 BCCA 207, recently adopted a two-step approach to considering applications for orders under section 161(1)(g) (para 144):

> I now turn to apply these principles to the three appeals before this Court. I agree with and adopt the two-step approach identified by Vice Chair Cave in *SPYru* at paras 131-132:
>
> > [131] The first step is to determine whether a respondent, directly or indirectly, obtained amounts arising from his or her contraventions of the Act. This determination is necessary in order to determine if an order can be made, at all, under section 161(1)(g).
> >
> > [132] The second step of my analysis is to determine if it is in the public interest to make such an order. It is clear from the discretionary language of section 161(1)(g) that we must consider the public interest, including issues of specific and general deterrence.

[34] The Court of Appeal in *Poonian* further adopted several principles to apply in interpreting section 161(1)(g) (para 143):

> 1. The purpose of s. 161(1)(g) is to deter persons from contravening the *Act* by removing the incentive to contravene, i.e. by ensuring the person does not retain the "benefit" of their wrongdoing.
>
> 2. The purpose of s. 161(1)(g) is not to punish the contravener or to compensate the public or victims of the contravention. Those objectives may be achieved through other mechanisms in the *Act*, such as the claims process set up under Part 3 of the *Securities Regulation* or the s.157 compliance proceedings in the *Act*.
>
> 3. There is no "profit" notion, and the "amount obtained" does not require the Commission to allow for deductions of expenses, costs, or amounts other persons paid to the Commission. It does, however, permit deductions for amounts returned to the victim(s).
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> 4. The "amount obtained" must be obtained *by that respondent, directly or indirectly*, as a result of the failure to comply with or contravention of the *Act*. This generally prohibits the making of a joint and several order because such an order would require someone to pay an amount that person did not obtain as a result of that person's contravention.
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> 5. However, a joint and several order may be made where the parties being held jointly and severally liable are under the direction and control of the contravener such that, in fact, the contravener obtained those amounts *indirectly*. Non-exhaustive examples include the use of a corporate *alter ego*, use of other person's accounts, or use of other persons as nominee recipients.

[35] Finally, the Court of Appeal in *Poonian* approved an approach to determining the amounts obtained, directly or indirectly, by a respondent that requires the executive director to provide evidence of an "approximate" amount, following which the burden of proof switches to the respondent to disprove the reasonableness of this number.

Step 1 – Can section 161(1)(g) orders be made?

[36] The evidence during the hearing was that Military obtained the benefit of the full amount of the $170,000 that was obtained from investors by the respondents' breach of the cease trade order.

[37] Therefore, there is no doubt that we could make an order under section 161(1)(g) of the Act against Military with respect to the full amount obtained from its misconduct.

[38] This issue is more complicated with respect to Loughery.

[39] The executive director submitted that Loughery indirectly obtained the $170,000 as a consequence of his control and direction over Military.

[40] As noted in the fifth principle set out in paragraph 34 (above) and as set out in the Act, there are circumstances in which we may make an order (and make it a joint and several obligation with another respondent) against a respondent, where that respondent may be held to have indirectly obtained an amount as a consequence of his misconduct.

[41] The evidence in this case demonstrated that Loughery was acting as a *de facto* officer and/or director of Military and that the actual directors of Military at the relevant time were largely acting as directed by Loughery. Loughery was clearly exercising significant control over the company. However, the question of when it is appropriate to determine that a respondent has indirectly obtained an amount as a consequence of direction and control of another entity is a difficult one that must be dependent on the facts and circumstances of each case.

[42] In this case, Military was a widely held public company. Notwithstanding the evidence of Loughery's control over the board, there was not sufficient evidence to establish that Loughery financially benefitted from the funds directly obtained by Military through the breach of the cease trade order. We do not know how many shares of Military that Loughery held at the relevant time. This was not a circumstance in which it would be possible to characterize Military as the corporate alter ego of Loughery. As a consequence, we do not think that we could make an order against Loughery under section 161(1)(g) of the Act in the amount of $170,000.

[43] The evidence did establish that following the deposit of the $170,000 into the accounts of Military the company then subsequently (over a period of time) paid approximately 70% of that amount to Loughery. The evidence also established that the payments made to Loughery by Military were a combination of reimbursements to Loughery for out-of-pocket expenses incurred by him on behalf of the company and salary/management fees.

[44] It might be possible to characterize the 70% of the $170,000 paid to Loughery by Military as an amount indirectly obtained by Loughery arising from his misconduct (and, hence, an amount that could be made subject to an order under section 161(1)(g)). However, we do have concerns about that characterization, as there was no evidence to suggest that the payments by Military to Loughery were other than for legitimate business expenses.

Step 2 – Is it in the public interest to make a section 161(1)(g) order?

[45] There is no reason why it would not be in the public interest to make orders under section 161(1)(g) against Military in the amount of $170,000.

[46] As noted above, even if it were possible to make an order under section 161(1)(g) with respect to 70% of the $170,000, we would not find it to be in the public interest to do so. As noted, some of the expenditures were reimbursements of amounts expended on behalf of the company and the remainder were for salary/management fees for which there was no suggestion that they were not legitimately earned.

Administrative penalties

[47] The executive director submitted that it would be appropriate to impose administrative penalties of $20,000 and $30,000 against Military and Loughery, respectively.

[48] As noted above, the executive director submitted that, in the event that we did not make an order under section 161(1)(g) against Loughery, then the amount of the administrative penalty ought to be higher than $30,000.

[49] We do not agree with this conceptual approach to sanctions. We agree that the totality of our sanctions (market prohibitions and financial sanctions) must be proportionate to the misconduct of the respondent. However, orders under section 161(1)(g) and 162 serve very distinct purposes. Orders under section 161(1)(g) are intended to deprive wrongdoers of the financial benefits of their misconduct. Orders under section 162 serve as a penalty for that misconduct. Orders under section 161(1)(g) and 162 should be considered separately with a view to their separate and distinct purposes.

[50] The *Malone* and *Jardine* decisions suggest that the amount of an administrative penalty for a contravention of an order of this Commission may be significantly higher than $30,000. While Loughery's misconduct may not be as serious as the respondents in those two cases, it was still significant misconduct. He intentionally contravened the cease trade order and caused Military to do so as well. In order to achieve the goals of both specific and general deterrence, while still being proportionate to the misconduct, we find that an administrative penalty in the amount of $50,000 against Loughery is appropriate in all the circumstances.

[51] We also find that a $20,000 administrative penalty against Military is appropriate in the circumstances. The smaller administrative penalty is reflective of its lack of an aggravating factor and the reality that, although Military is a separate legal entity, Loughery was largely responsible for Military's misconduct.

V. Orders

[52] Considering it to be in the public interest, and pursuant to sections 161 and 162 of the Act, we order that:

Loughery

(a) under sections 161(1)(d)(i), that Loughery resign any position he holds as a director or officer of an issuer or registrant;

(b) that Loughery be prohibited, for the later of six years or until such time as the amount referred to in paragraph (c) below has been paid:

i. under section 161(1)(d)(ii), from becoming or acting as a director or officer of any issuer;

ii. under section 161(1)(d)(iii), from acting as a registrant or promoter;

iii. under section 161(1)(d)(iv), from acting in a management or consultative capacity in connection with activities in the securities market; and

iv. under section 161(1)(d)(v), from engaging in investor relations activities; and

(c) under section 162, that Loughery pay an administrative penalty of $50,000.

[53] Considering it not to be prejudicial to the public interest, and pursuant to section 171 of the Act, we order that the previously issued order against Military (Cease Trade Order, dated December 11, 2002) under section 161(1)(b)(i) be varied, such that it may not be revoked until the later of five years or until such time as the amounts referred to in paragraphs (a) and (b) below have been paid:

(a) under section 161(1)(g), that Military pay to the Commission $170,000, being the amount it obtained directly as a result of its contravention; and

(b) under section 162, that Military pay an administrative penalty of $20,000.

March 4, 2019

For the Commission

Nigel P. Cave
Vice Chair

Judith Downes
Commissioner

Gordon Holloway
Commissioner