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

Citation: Re Loughery, 2018 BCSECCOM 134 Date: 20180427

Stewart Douglas Loughery and Military International Limited[1]

Panel	Nigel P. Cave	Vice Chair
	Judith Downes	Commissioner
	Gordon Holloway	Commissioner
Hearing Dates	December 14 and 15, 2017	
Submissions Completed	March 12, 2018	
Date of Findings	April 27, 2018	
Appearing		
David Hainey	For the Executive Director	

Findings

I. Introduction

[1] This is the liability portion of a hearing under sections 161(1) and 162 of the *Securities Act*, RSBC 1996, c. 418.

[2] On December 17, 2015, the executive director issued a notice of hearing against the respondents (2015 BCSECCOM 460).

[3] On September 12, 2016, the executive director amended the original notice of hearing (2016 BCSECCOM 311), such that the executive director alleged that:

a) Military International Limited and Stewart Douglas Loughery contravened a cease trade order issued by the executive director on December 11, 2002 against Military; and
b) Loughery, as a *de facto* director or officer of Military, authorized, permitted or acquiesced in Military's contravention of the cease trade order and, pursuant to section 168.2 of the Act, he thereby also contravened the cease trade order.

[1] The original style of cause in this matter was Stewart Douglas Loughery, Richard Dean Reoji Nawata, and Military International Limited. On October 21, 2016, the Executive Director filed a notice of discontinuance against Nawata. Therefore, the style of cause has been amended to refer only to the remaining respondents in this matter.

[4] This hearing was originally scheduled to be heard on June 6-10, 2016.

[5] On May 11, 2016, we granted an adjournment of the hearing to October 17-21, 2016 on the application of the executive director due to a change of counsel.

[6] On October 18, 2016, we granted an adjournment of the hearing generally on the application of Loughery due to his unavailability for the hearing dates arising from health issues.

[7] On December 20, 2016, we set new hearing dates for March 6-9, 2017.

[8] On January 13, 2017, we granted a further adjournment of the hearing to June 5-8, 2017 on the application of the executive director due to the unavailability of one of the witnesses.

[9] On May 17, 2017, we granted a further adjournment to December 4-8, 2017 of the hearing on the application of the executive director due to the unavailability of one of the witnesses.

[10] During the hearing, the executive director called three witnesses (a Commission investigator and two investors), tendered documentary evidence and provided written and oral submissions.

[11] Although the respondents received notice of the various hearing dates, neither respondent attended the hearing, tendered documentary evidence or provided any written or oral submissions.

II. Background

The respondents

[12] Loughery is a resident of Pitt Meadows, British Columbia. He was formerly registered in various capacities under the Act but was not registered in any such capacity during the period relevant to the matters in the notice of hearing.

[13] Loughery was an undischarged bankrupt during the period relevant to the matters in the notice of hearing.

[14] Military is a corporation incorporated under the laws of Alberta that was a reporting issuer in British Columbia during the period relevant to the matters in the notice of hearing.

[15] On December 11, 2002, the executive director issued a cease trade order against Military for failure to file interim financial statements as required pursuant to section 144(1) of the Act. The cease trade order has remained in effect since the date of its issuance.

[16] The material term of the cease trade order is that "all trading in the securities of [Military] cease until they file the required record."

The financing

[17] Loughery was first introduced to Military in 2006 through its former President.

[18] In a compelled interview under oath with Commission investigators, Loughery said that he took over financial responsibility for Military on January 1, 2007. However, his status as an undischarged bankrupt prevented him from being appointed as a director of the company.

[19] Commission staff interviewed N under oath, who was appointed as a director and President of Military in February of 2010. The Commission also contacted two other individuals (G and P) who were directors of Military during the period relevant to the matters in the notice of hearing.

[20] Loughery (in his interview with Commission staff), N (in his interview with Commission staff and in a settlement agreement with the Commission dated October 13, 2016) and the two other directors all confirmed that it was Loughery who:

- recruited N and G to become members of the board of Military;
- did everything in the company, including, preparing its books and records, drafting securities regulatory filings, dealing with accountants and lawyers, etc.;
- made all key decisions with respect to the company and its activities; and
- solicited investors on behalf of the company.

[21] Military applied, unsuccessfully, to have its cease trade order revoked in 2007 and in 2010. Loughery made the applications on behalf of the company and dealt with Commission staff with respect to the applications.

[22] During its review of Military's application to revoke the cease trade order in 2010, Commission staff advised Loughery, in a letter dated September 3, 2010, that entering into agreements with respect to financings for Military may constitute a breach of the cease trade order.

[23] Notwithstanding this warning, between November 1, 2010 and December 11, 2011 Military entered into loan agreements (along with corresponding promissory notes) with six investors (in seven transactions) for aggregate proceeds of $170,000. All of the proceeds of these loans were deposited into a Military bank account.

[24] Two of the investors testified during the hearing. One of the investors testified that they were introduced to the investment through a finder hired by Military. However, they both confirmed that it was Loughery alone with whom they dealt respecting their investment in Military. Both confirmed that they were told that the loan was actually a deferred arrangement to acquire shares of Military at $.05 per share, where the shares would be issued after the cease trade order was revoked.

[25] Although they did not testify at the hearing, Commission staff corresponded with three of the other investors who entered into loan arrangements with Military. The information that they provided to the Commission in that correspondence was generally consistent with the testimony of the two investor witnesses.

III. Analysis and Findings

A. Applicable Law

Standard of Proof

[26] The standard of proof is proof on a balance of probabilities. In *F.H. v. McDougall*, 2008 SCC 53, the Supreme Court of Canada held (at paragraph 49):

> 49 In the result, I would reaffirm that in civil cases there is only one standard of proof and that is proof on a balance of probabilities. In all civil cases, the trial judge must scrutinize the relevant evidence with care to determine whether it is more likely than not that an alleged event occurred.

[27] The Court also held (at paragraph 46) that the evidence must be "sufficiently clear, convincing and cogent" to satisfy the balance of probabilities test.

[28] This is the standard that the Commission applies to allegations: see *David Michael Michaels and 509802 BC Ltd. doing business as Michaels Wealth Management Group*, 2014 BCSECCOM 327, paragraph 35.

Definition of "security" and "trade"

[29] The relevant provisions of the Act are as follows:

a) Section 1(1) defines "trade" to include "(a) a disposition of a security for valuable consideration" and "(f) any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of any of the activities specified in paragraphs (a) to (e)".

b) Section 1(1) defines "security" to include "(a) a document, instrument or writing commonly known as a security", "(b) a document evidencing title to, or an interest in, the capital, assets, property, profits, earnings or royalties of a person", "(d) a bond, debenture, note or other evidence of indebtedness, share, stock..." and "(l) an investment contract."

Liability under section 168.2

[30] Section 168.2(1) of the Act states that if a corporate respondent contravenes a provision of the Act, an individual who is an employee, officer, director or agent of the company also contravenes the same provision of the Act, if the individual "authorizes, permits, or acquiesces in the contravention".

[31] There have been many decisions which have considered the meaning of the terms "authorizes, permits or acquiesces". In sum, those decisions require that the respondent have the requisite knowledge of the corporate contraventions and have the ability to influence the actions of the corporate entity (through action or inaction).

B. Analysis

[32] The executive director submits that both of the respondents contravened the cease trade order in that they both traded in securities of Military during the tenancy of the order. He further submits that Loughery was a *de facto* director or officer of Military at the relevant time and that, pursuant to section 168.2(1) of the Act, Loughery is liable for Military's contravention of the order.

[33] There are three issues in this case:

a) are the loan agreements entered into by Military with the investors "securities" as defined in the Act?;
b) did both of the respondents "trade" in securities of Military?; and
c) was Loughery a *de facto* director or officer of Military during the relevant period?

[34] We find that the answer to all three of those issues is "yes".

[35] The Commission recently considered the issue of whether a loan arrangement was a "security" as defined under the Act in *Re FS Financial Strategies*, 2017 BCSECCOM 238 (at paragraphs 25-32):

> [25] Section 1(1) of the Act defines "security" to include "(a) a document, instrument or writing commonly known as a security", "(b) a document evidencing title to, or an interest in, the capital, assets, property, profits, earnings or royalties of a person", "(d) a bond, debenture, note or **other evidence of indebtedness**, share, stock..." and "(l) **an investment contract**." (emphasis added)
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> [26] On a plain reading of that definition, each of the loan agreements would clearly qualify as an "evidence of indebtedness".
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> [27] However, not all debtor/creditor arrangements have been found to give rise to "securities" under the Act (or under similar securities legislation in other jurisdictions in North America). Loan arrangements (whether called notes, loan agreements, etc.) can arise in a wide spectrum of transactions, from arrangements that are principally investments in nature (which transaction would fall within the definition of a "security") to those which serve a specific commercial purpose or support a specific commercial transaction (which transaction is less likely to fall within the jurisdiction of the Act).
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> [28] The question of when a loan arrangement, whatever it is called, is a "security" under the Act and when it is not requires a purposive analysis of the definition of "security". It also requires an analysis of the factual context in which the individual loan arrangement occurs and the context in which the issuer, more broadly, is raising capital.
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> […]

[30] The statutory interpretation analysis starts with two basic, but important, concepts as set out in *Pacific Coast Coin Exchange of Canada Ltd. v. Ontario (Securities Commission)*, 1977 CanLII 37 (SCC), [1978] 2 S.C.R. 112:

a) that the Act must be construed broadly to ensure that one of its primary purposes (of protecting the investing public) is met; and

b) that in interpreting whether an instrument falls within the definition of "security", it is the instrument in question's substance, not form, which is paramount.

[31] In *Gill*, faced with the issue of whether loan arrangements between an investment advisor and two of his clients where securities under the Act, the Court of Appeal considered the United States Supreme Court decision *Reves v. Ernst & Young*, 494 U.S. 56 (1990) and applied a purposive approach to the definition of "security".

[32] In *Reves*, the court considered the scope of the word "note" in the context of securities law and set out a rebuttable presumption that any "note" is a security. It further adopted a "family resemblance" test by which it set out criteria for when an instrument might be considered as similar to some of the judicially accepted categories of commercial arrangements that are exceptions to this presumption. The court listed four factors which were relevant in determining whether an instrument is a security:

a) the motivation that would prompt a reasonable seller and buyer to enter the transaction: if the seller's purpose is to raise money for general business purposes and the buyer's purpose is to profit from the returns the instrument is expected to generate, the instrument is likely a security;

b) the intended distribution of the instrument: if it is one in which there will be "common trading for speculation or investment" it is likely a security;

c) the reasonable expectations of the investing public: the more the public expects that an instrument will be a security and thereby regulated by the securities laws, the more likely it is a security; and

d) the existence of another regulatory regime: if there is no other regulatory regime that significantly reduces the risk of the instrument, thereby rendering securities regulation necessary, the more likely it is a security.

[36] We agree with that approach to the consideration of the loan arrangements in this case.

[37] The loan arrangements entered into by Military are, on their face, either notes or evidences of indebtedness within the definition of security. They are presumptively a security unless that presumption can be rebutted by the facts and circumstances of this case. The facts do not support a rebuttal of that presumption.

[38] The loans to Military did not arise in the context of a specific commercial transaction. In fact, the loans were simply a way for Military to raise funds to carry on business. These were unsecured arrangements and the investors believed the loans were really just a deferred arrangement to acquire shares in Military. There is no way to view these loans as anything other than investment arrangements.

[39] The Act defines "trade" to include the disposition of a security for valuable consideration and any acts in furtherance of that disposition. By entering into the loan transactions, Military was clearly trading in securities. Loughery was responsible for all material aspects of the investment on behalf of Military. It is clear that he was responsible for dealing with the investors and getting them to invest in the company. We find that Loughery engaged in multiple acts in furtherance of the issuance of the loans by Military and was thereby trading as well.

[40] Therefore, we find that both Military and Loughery contravened the terms of the cease trade order issued by the executive director on December 11, 2002.

[41] Finally, we find that Loughery was acting as either or both a *de facto* director or officer of Military at the relevant time. Loughery admitted to doing everything on behalf of the company and that it was only because he was an undisclosed bankrupt that he could not become a director of the company. All three of the directors admitted to Commission staff that it was really Loughery who was making all of the key decisions on behalf of the company and that they acted on his instruction.

[42] In the words of section 168.2(1), Loughery clearly "authorized, permitted or acquiesced" to Military's contravention of the cease trade order. Therefore, we find that, pursuant to section 168.2(1), Loughery also contravened the cease trade order.

[43] We direct the executive director and the respondents to make their submissions on sanction as follows:

By May 18, 2018	The executive director delivers submissions to the respondents and to the secretary to the Commission.
By June 1, 2018	The respondents deliver their response submissions to the executive director and to the secretary to the Commission. Any party seeking an oral hearing on the issue of sanctions so advises the secretary to the Commission. The secretary to the Commission will contact the parties to schedule the hearing as soon as practicable after the executive director delivers reply submissions (if any).
By June 8, 2018	The executive director delivers reply submissions (if any) to the respondents and to the secretary to the Commission.

April 27, 2018

For the Commission

Nigel P. Cave
Vice Chair

Judith Downes
Commissioner

Gordon Holloway
Commissioner