

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

Citation: Re Pegasus Pharmaceuticals, 2019 BCSECCOM 453

Date: 20191230

**Pegasus Pharmaceuticals Group Inc., Careseng Cancer Institute Inc.  
and Winter Huang (also known as Dong Huang)**

<b>Panel</b>	Nigel P. Cave Deborah Armour, QC Judith Downes	Vice Chair Commissioner Commissioner
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**Submissions Completed** November 15, 2019

**Date of Decision** December 2, 2019

**Date of Reasons** December 30, 2019

**Appearing**

Mila Pivnenko  
William L. Roberts

For the Executive Director

Owais Ahmed  
Andrew Tang  
Roselle Wu

For Pegasus Pharmaceuticals  
Group Inc.

**Reasons for Decision**

**I. Introduction**

- [1] Pegasus Pharmaceuticals Group Inc. (the Applicant) applied on October 1, 2019, under section 171 of the *Securities Act*, RSBC 1996, c. 418 (the Act), for an order to vary certain freeze orders issued by the Commission on August 15 and October 26, 2012 (the Freeze Orders).
- [2] In particular, the Applicant applied for the release of CDN\$1,205,467.43 from bank accounts of the Applicant subject to the Freeze Orders for the redemption of a mortgage and the payment of outstanding property taxes and utility bills in respect of the Properties (defined below) owned by the Applicant.
- [3] The executive director opposed the application. The Applicant and the executive director provided written submissions on the application.
- [4] We heard oral submissions from the parties on October 16, 2019 following which we requested further written submissions.

- [5] On November 15, 2019 the parties appeared before us to speak to those further submissions. At the conclusion of that hearing, we indicated that we were prepared to grant the application to vary the Freeze Orders but that we first required from the parties:
- a) the form of variation order that the Applicant believed it needed; and
  - b) confirmation that the form of order and any mechanics to ensure the application of the released funds to redeem the mortgage are in place to the satisfaction of the executive director.
- [6] On December 2, 2019, we received the agreed form of variation order and confirmation from the parties that the procedural steps were in place, satisfactory to the executive director. Accordingly, on December 2, 2019, we granted the application and made an order varying the Freeze Orders, with reasons to follow.
- [7] These are our reasons.

## **II. Facts**

- [8] A notice of hearing was issued on January 28, 2016 and amended on October 17, 2018 naming as respondents the Applicant and related parties. The allegations against the Applicant in the amended notice of hearing are:
- a) fraud contrary to s. 57(b) of the Act totaling US\$62.6 million; and
  - b) illegal distributions contrary to s. 61 of the Act of approximately US\$56 million.
- [9] The Applicant is a company involved in the development and production of natural healthcare products and operates its business at units 110, 112, 114 and 116 of 11800 River Road, Richmond, BC (the Properties).
- [10] On February 20, 2017, the Commission registered a charge under section 151(5) of the Act (the Charge) against the Properties.
- [11] The Properties have two mortgages registered against them. The first is held by an individual and an entity (neither of whom are respondents in this matter) (the Mortgage). The second mortgage is held by Winter Huang, a respondent in this matter and a director of the Applicant, and another individual (who is not a respondent in this matter).
- [12] An affidavit of Winter Huang made October 1, 2019 establishes that:
- the Applicant produces Caresang RH (the Product) which has been licensed for sale in China by the Chinese Food and Drug Administration (CFDA);
  - the Applicant's license is tied to the Properties;
  - the Applicant has a purchase order from a Chinese entity for a large quantity of the Product (the Purchase Order) which could generate up to US\$7,500,000 in revenues if all of the product is produced and delivered under the terms of the Purchase Order; and

- revenues received from the Purchase Order would be put towards increasing the Applicant's manufacturing capacity of the Product.

[13] YZ, in an affidavit attached as exhibit "G" to the affidavit of JC made October 1, 2019, attested:

- he has expertise in the CFDA licensing process and has been retained by the Applicant to seek renewal of the Applicant's CFDA license;
- CFDA requires all license applicants to have business and manufacturing addresses that have been certified through an onsite inspection;
- the Properties have been inspected and determined to meet the necessary requirements;
- CFDA permits a registrant to change a certified address but the change is subject to strict requirements and the new address must be certified. CFDA is cautious about changes to manufacturing addresses; and
- usually one to two years are required to successfully change the manufacturing address.

[14] The Commission issued the Freeze Orders against four accounts held by the Applicant at a financial institution (collectively, the Accounts). As at August 20, 2019, the Accounts held the following amounts:

- a) CDN\$96,627.36;
- b) US\$580,724.82;
- c) US\$252,710.08; and
- d) CDN\$132,614.17.

[15] We were advised that the total amount held in the Accounts was the equivalent of approximately CDN\$1,332,959.37 based on the Canada/US exchange rate as of September 30, 2019.

[16] The Applicant has defaulted on payments under the Mortgage resulting in ongoing foreclosure proceedings. The petitioner in the foreclosure application has obtained an order for sale and has received an offer of CDN\$1.8 million for the Properties. The Properties have been appraised at a total of CDN\$1.795 million. As of October 1, 2019, the aggregated amount outstanding on the Mortgage, unpaid property taxes and metered utility bills was CDN\$1,205,467.43.

[17] The hearing on the allegations, following several adjournments, is scheduled to begin on June 22, 2020.

### **III. Positions of the Parties**

#### **A. Applicant**

[18] The Applicant submitted that failure to vary the Freeze Orders to allow for the redemption of the Mortgage would cause the Applicant to lose the Properties in the foreclosure proceedings which would in turn cause the Applicant to lose its license with the CFDA. Without its license, the Applicant would be unable to fulfill the Purchase Order all of which amounts to significant prejudice to the Applicant. The granting of the variation order would substantially benefit the Applicant as it would be able to carry on its business including fulfilling the Purchase Order.

[19] The Applicant submitted that if the order to vary the Freeze Orders was granted, the funds would be applied to the Properties resulting in increased equity in the Properties available to satisfy judgments of investors or the Commission (in the event that any financial sanctions are ultimately issued by a panel against the Applicant pursuant to either section 161 or 162 of the Act). As a consequence, the risk of loss of the funds subject to the Freeze Orders if the variation order was granted, would be minimal.

[20] Finally, the Applicant submitted that in determining whether there would be no prejudice to the public interest if the order was granted, the panel must weigh the interests, prejudice and benefits to various stakeholders including the Applicant.

### **B. Executive Director**

[21] The executive director took the position that:

- a) the public interest is in preserving the funds for persons who may have statutory claims to them, including investors in the Applicant;
- b) granting the variation order could result in a loss of the frozen funds; and
- c) a variation order would not benefit the Applicant's business.

[22] The executive director cited the following reasons why a variation of the Freeze Orders could result in a loss of the frozen funds:

- the Applicant did not establish that any money generated through the Purchase Order would benefit investors;
- the movement of the funds from the Accounts to additional equity in the Properties would represent a change in the status quo as the Charge would not have an identical legal effect as the Freeze Orders;
- the Charge prevents subsequent transfers or registered encumbrances of the Properties pending resolution of the allegations in the Notice of Hearing but with some exceptions. It does not create a special priority and in any event does not prevent other statutory claims such as builders' liens from being registered after the Charge and ultimately taking priority over the Commission's interest; and
- some "involuntary" charges such as property taxes have a super priority and would come ahead of the Charge regardless of when registered. There is an issue as to whether registration of a builder's lien would have a similar effect. While claims by third parties could also be made against the Accounts, practically speaking land is easier to claim against than cash given the ability of creditors to do searches of the Land Title and Survey Authority of BC.

[23] The executive director also submitted that a variation of the Freeze Orders would not benefit the Applicant's business because:

- the Applicant's financial statements show that it consistently lost money from its operations from 2005 to 2012. In 2012, the losses amounted to approximately US\$14.2 million. The Applicant has not generated any revenue since 2015; and
- the Applicant did not establish that any profit would accrue from the Purchase Order nor that the Purchase Order will have a positive impact on the Applicant's business as a whole.

[24] The executive director submitted that for the reasons set out above it would be prejudicial to the public interest to grant the application to vary the Freeze Orders.

#### **IV. Analysis**

[25] The Commission in *Re Tan*, 2016 BCSECOM 138 cited *Amswiss* [1992], 7 BCSCWS which described the purpose of freeze orders at pp. 21 and 22:

In our view, the purpose of section 135(1) [Note: a predecessor to section 151] is to preserve property for the persons who may have common law or statutory claims to or interests in it, for example by way of rescission or damages under Part 14 of the Act.

...

The immediate effect of a freeze order is to maintain the status quo, ensuring that the frozen property is not dissipated or destroyed before the Commission is in a position to determine what, if any, further steps or orders in the public interest should be made under the Act.

...

The power to freeze property quickly is one of those regulatory powers given specifically to the Commission by the Legislature to enhance its capacity to protect the public markets.

[26] Section 171 of the Act says that the Commission may vary or revoke a previous decision if it considers that to do so "would not be prejudicial to the public interest." The Commission does not determine disposition of frozen assets. A court ultimately does.

[27] In *Zhu v. British Columbia (Securities Commission)*, 2013 BCCA 248, para. 48, the Court cited with approval the panel's decision under review where it said that it regarded itself as having a very broad discretion in determining whether revocation of the freeze order in that case would not be prejudicial to the public interest.

[28] In *Tan*, the panel stated that the public interest is broader than considerations of investor protection. The potential prejudice to an applicant must also be considered. We agree with that proposition.

- [29] In essence, granting the application, from the perspective of the Commission “freezing” assets of the Applicant for the purpose of satisfying future claims (including investor claims and financial sanctions that may result from these proceedings), would result in the swapping of the Freeze Orders against approximately \$1.2 million in cash in the Accounts for a commensurate increase in equity in the Properties over which the Commission has a Charge. Accordingly, it is important for us to consider the legal import of the Charge as compared to the Freeze Orders.
- [30] Pursuant to section 151(5) and (7) of the Act, the legal effect of the registration of the Charge is the same as a certificate of *lis pendens* or a caveat. Section 31 of the *Land Title Act*, RSBC 1996, c. 250 provides that once the claim secured by the certificate of pending litigation or caveat (or in this case the Charge) is established by a judgment then those charges take priority, from the original date of filing the certificate of pending litigation or caveat, over charges or claims subsequently registered on the property. Therefore, any monetary orders that we might make in these proceedings, when they are filed as judgments in the BC Supreme Court become secured and would take priority over charges filed after the date the Charge was filed (subject to some exceptions discussed below).
- [31] Subsections 216 (1) and (2) of the *Land Title Act* prevent the registration of transfers or encumbrances after a *lis pendens* or caveat is registered against title with some exceptions. Those subsections read:
- 216 (1) After registration of a certificate of pending litigation, the registrar must not make any entry in the register that has the effect of charging, transferring or otherwise affecting the land described in the certificate ....
- (2) Subsection (1) does not apply to the lodging of a caveat or the registration of
- ...
- (f) a certificate of judgment, order, notice, claim of lien under the *Builders Lien Act*, certificate of pending litigation or any other involuntary charge.
- [32] The parties were in agreement that the Charge does not create an *in rem* interest in the Properties. They were also in agreement that the Freeze Orders likewise do not create a substantive right in the cash held in the Accounts.
- [33] We agree with the submissions of the executive director that there is uncertainty whether the Purchase Order will be profitable given the fact that the Applicant has not run the business in a profitable way to date.
- [34] However, the Applicant filed an affidavit which sets out that the gross profit on the first instalment of the Purchase Order will be 60% or greater. The executive director did not challenge this evidence and we have no basis to reject it.
- [35] The evidence before us is that, if we do not vary the Freeze Orders, the Properties would be foreclosed and sold and the CFDA license would likely be revoked, preventing the Applicant

from fulfilling the Purchase Order. All this would happen before the hearing on the merits has commenced and before any determinations are made by the Commission. Therefore, we conclude that the Applicant has established, on a balance of probabilities, that it would suffer significant prejudice if we did not vary the Freeze Orders.

- [36] We also agreed with the submissions of the executive director that there is some risk that the Commission and investors will be worse off by exchanging the Freeze Orders against the Accounts for increased equity in the Properties (which is subject to the Charge). For example, new statutory charges could be registered against the Properties which could ultimately have priority over an order of the Commission under section 161 or 162. There is no way of determining the size of that risk. However, given the short time between now and the hearing in June, we believe that risk is relatively small.
- [37] We agree that granting the application would result in a change to the status quo. Having the Freeze Orders registered against the Accounts is not exactly the same as having the Charge over the Properties. The two underlying assets are different. Third parties may have differing rights (resulting from tracing or constructive trusts, for example) in cash versus in fee simple property. However, whether the change to the status quo would result in a positive or negative impact on the future ability of investors or the Commission to satisfy judgments against the Applicant is merely speculative at this point. While the purpose of freeze orders is to maintain the status quo, a change to the status quo is not, in and of itself, sufficient to determine that it would be prejudicial to the public interest to grant a variation order.
- [38] In summary, there could be claims with higher priority than any the Commission might ultimately have against either or both of the cash in the Accounts and the equity in the Properties.
- [39] We determined that the significant harm that the Applicant will likely experience if we do not vary the Freeze Orders outweighs the risk of the Commission and investors being in a worse position if we do vary them. Therefore, we determined that, on balance, it is not prejudicial to the public interest to vary the Freeze Orders and we so ordered.

December 30, 2019

**For the Commission**

Nigel P. Cave  
Vice Chair

Deborah Armour, QC  
Commissioner

Judith Downes  
Commissioner