



Ontario
Securities
Commission

Commission des
valeurs mobilières
de l'Ontario

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Citation: Fauth (Re), 2021 ONSEC 4

Date: 2021-01-21

File No. 2020-36

**IN THE MATTER OF
VERNON RAY FAUTH**

**REASONS AND DECISION
(Subsections 127(1) and 127(10) of the
Securities Act, RSO 1990, c S.5)**

Hearing: In Writing

Decision: January 21, 2021

Panel: Wendy Berman Vice-Chair and Chair of the Panel

Appearances: Vivian Lee For Staff of the Commission
Alvin Qian

No submissions were made on behalf of Vernon Ray Fauth

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REASONS AND DECISION

I. OVERVIEW

- [1] On November 8, 2018, the Alberta Securities Commission (the **ASC**) issued a decision and found that Vernon Ray Fauth (**Fauth**) contravened Alberta securities laws by illegally dealing in securities, making misrepresentations to investors and perpetrating a fraud on investors (the **ASC Merits Decision**).¹
- [2] On June 24, 2019, the ASC issued its decision on sanctions and costs (the **ASC Sanctions Decision**) and imposed various sanctions, restrictions and requirements on Fauth, including a permanent prohibition from participating in Alberta's capital markets, disgorgement in the amount of \$2,585,414.87, an administrative penalty in the amount of \$400,000 and costs in the amount of \$250,000, as described more fully below.²
- [3] Staff of the Ontario Securities Commission (**Staff** of the **Commission**) has applied for a protective order in the public interest pursuant to s. 127(10) of the *Securities Act*,³ (the **Act**), which provides that an order may be made under s. 127(1) of the Act against a person who has been convicted in any jurisdiction of an offence arising from a transaction, business or course of conduct related to securities or derivatives. Staff submits that the precondition for a protective order has been met and that it is in the public interest, based on these circumstances, for the Commission to make an inter-jurisdictional enforcement order permanently prohibiting Fauth from participating in Ontario's capital markets.
- [4] For the reasons that follow, I find that it is in the public interest to issue an order substantially in the form requested by Staff.

II. SERVICE AND PARTICIPATION

- [5] Staff served Fauth with the Notice of Hearing, Statement of Allegations and Staff's hearing brief,⁴ written submissions and brief of authorities by email on October 21, 2020 and by courier to Fauth's last known mailing address on October 22, 2020.⁵
- [6] Staff elected to proceed by way of the expedited procedure for a written hearing provided for in the Commission's *Rules of Procedure and Forms*.⁶ As stated in the Notice of Hearing, Fauth had 21 days from the date of service to file a request for an oral hearing, and 28 days from the date of service to file a hearing brief and written submissions. The deadlines for Fauth to request an oral hearing and to serve and file a hearing brief and written submissions have passed. No

¹ Exhibit 1, Staff's Hearing Brief, *Re Fauth*, 2018 ABASC 175, Tab 1 (**ASC Merits Decision**)

² Exhibit 1, Staff's Hearing Brief, *Re Fauth*, 2019 ABASC 102, Tab 2 (**ASC Sanctions Decision**)

³ RSO 1990 c S.5

⁴ Staff's Hearing Brief marked as Exhibit 1

⁵ Exhibit 2, Affidavit of Service of Michelle Spain, Sworn October 27, 2020 at paras 2-5.

⁶ (2019) 42 OSCB 9714 (**OSC Rules of Procedure**), r 11(3)

request for an oral hearing was made and no materials were filed by, or on behalf of, Fauth.

- [7] Pursuant to the *Statutory Powers Procedure Act*⁷ and the *OSC Rules of Procedure*,⁸ the Commission may proceed in the absence of a party who has been provided adequate notice of a proceeding. I am satisfied that Fauth was provided with adequate notice of this proceeding and that I may proceed in his absence.

III. FACTUAL BACKGROUND

A. ASC Proceedings and Conduct at Issue

- [8] Fauth is a resident of Alberta⁹ and has never been registered with the Commission in any capacity.¹⁰ Fauth has not been registered with the ASC in any capacity since December 31, 2003, although he was registered as a mutual fund salesperson prior to that date.¹¹
- [9] Fauth's misconduct took place between October 2006 and September 2014 (the **Material Time**).¹² During that time, Fauth solicited investments in Espoir Capital Corporation (**Espoir**), a corporation for which he was the founder, a director and officer and the sole shareholder.
- [10] Over a period of approximately 10 years (which included the Material Time), Fauth raised approximately \$15.5 million for Espoir from investors, who either purchased three-year debentures or advanced loans under promissory notes with Espoir. Approximately 70 investors in Alberta, British Columbia and Ontario invested approximately \$15 million by way of debentures¹³ and five investors invested \$545,000 by way of promissory notes.¹⁴
- [11] Fauth made misleading or untrue statements to, and/or omitted material information from, investors regarding their investment in Espoir, both through direct discussions with investors and through promotional materials and correspondence provided to investors.¹⁵
- [12] Investors were told that their investment was "safe" and "secure" and that funds were, or would be, invested in real estate and mortgages and secured by that real estate.¹⁶ Contrary to such representations, investor funds were primarily invested in, or loaned to, Fauth-owned, controlled or managed entities. The vast majority of these non-arm's length transactions were undocumented and unsecured.¹⁷ In addition, some of the investor funds were used to repay principal

⁷ RSO 1990, c S.22, s 7(2)

⁸ OSC Rules of Procedure, r 21(3)

⁹ ASC Merits Decision at para 25.

¹⁰ Exhibit 1, Staff's Hearing Brief, Section 139 Certificate Re: Fauth dated May 4, 2020, Tab 3.

¹¹ ASC Merits Decision at para 27.

¹² ASC Merits Decision at para 4.

¹³ ASC Merits Decision at para 46.

¹⁴ ASC Merits Decision at para 63.

¹⁵ ASC Sanctions Decision at paras 16 and 17.

¹⁶ ASC Merits Decision at para 334.

¹⁷ ASC Merits Decision at para 339; ASC Sanctions Decision at paras 18 and 19.

and make interest payments to other Espoir investors in the manner of a Ponzi scheme.¹⁸

[13] While some debenture holders and promissory noteholders were paid out and interest was paid until approximately mid-2013, most investors lost their invested funds. As of December 31, 2014, investors were owed over \$12.3 million and there is little to no prospect that these funds will ever be repaid.¹⁹

[14] Investors suffered significant financial and personal hardship as a result of the loss of some or all their invested funds. The impact was especially significant on those investors who lost their life savings and were retired or nearing retirement.²⁰

B. ASC Findings

[15] In the ASC Merits Decision, the ASC found that:

- (a) from approximately September 28, 2010 to November 19, 2012, Fauth breached s. 75(1)(a) of the Alberta *Securities Act*²¹ (the **Alberta Act**) by acting as a dealer in securities while not registered to do so and without an exemption from that requirement;
- (b) from approximately October 6, 2006 to November 19, 2012, Fauth breached s. 92(4.1) of the Alberta Act by making representations he knew or reasonably ought to have known were materially misleading or untrue, or by failing to state facts that were required to be stated or necessary to make the statements not misleading; and
- (c) from approximately January 1, 2009 to September 30, 2014, Fauth breached s. 93(b) of the Alberta Act by directly or indirectly engaging or participating in an act, practice or course of conduct relating to a security that he knew or reasonably ought to have known perpetrated a fraud on investors.²²

[16] The ASC found that Fauth illegally sold and promoted securities, deliberately misled investors over an extended period and made unauthorized use of investment funds.²³ The ASC stated that the Fauth's misconduct was among the most serious, and was "deliberate, self-serving and caused substantial harm".²⁴

[17] The ASC Panel further held that Fauth's misrepresentations went to "the heart of what the Espoir investors specifically wanted: safety and minimal risk." Fauth used these investor funds in unauthorized, unsafe and high-risk investments and exposed investors to significant risk, which ultimately resulted in the loss of the majority of investor funds.²⁵

¹⁸ ASC Sanctions Decision at para 20.

¹⁹ ASC Sanctions Decision at para 21.

²⁰ ASC Sanctions Decision at para 45.

²¹ RSA 2000, c S-4

²² ASC Merits Decision at paras 255, 312, 363.

²³ ASC Sanctions Decision at para 41.

²⁴ ASC Sanctions Decision at paras 40 and 47.

²⁵ ASC Sanctions Decision at paras 41-43.

B. ASC Sanctions

- [18] On June 24, 2019 the ASC issued the ASC Sanctions Decision which imposed the following sanctions, requirements and restrictions on Fauth:
- (a) pursuant to s. 198(1)(d) of the Act, Fauth must resign from any positions he holds as a director or officer (or both) of any issuer, registrant, investment fund manager, recognized exchange, recognized self-regulatory organization, recognized clearing agency, recognized trade repository, designated rating organization or designated benchmark administrator;
 - (b) pursuant to ss. 198(1)(b), (c), (e) and (e.3), Fauth is permanently prohibited from:
 - i. trading in or purchasing any security or derivative, and from relying on any exemptions contained in Alberta securities laws;
 - ii. becoming or acting as a director or officer (or both) of any issuer or other person or company that is authorized to issue securities, registrant, investment fund manager, recognized exchange, recognized self-regulatory organization, recognized clearing agency, recognized trade repository, designated rating organization or designated benchmark administrator; and
 - iii. acting in a management or consultative capacity in connection with activities in the securities market.
 - (c) pursuant to section 198(1)(i) of the Alberta Act, Fauth must pay to the ASC disgorgement in the amount of \$2,585,414.87;
 - (d) pursuant to section 199 of the Alberta Act, Fauth must pay to the ASC an administrative penalty of \$400,000; and
 - (e) pursuant to section 202 of the Alberta Act, Fauth must pay costs to the ASC in the amount of \$250,000.²⁶

IV. LEGAL FRAMEWORK IN ONTARIO

- [19] Subsection 127(10) of the Act provides that an order may be made under s. 127(1) where a person has been subject to an order by a securities regulatory authority in any jurisdiction that imposes sanctions, conditions, restrictions or requirements. If that precondition is met, the Commission must consider whether it should exercise its jurisdiction to make a protective order in the public interest.
- [20] In determining whether such an order should be made in the public interest, the Commission may consider, among other factors, the seriousness of the misconduct, the harm suffered by investors, specific and general deterrence and any aggravating or mitigating factors.²⁷ The purpose of such an order is “protective and preventive” and made to restrain potential conduct that could be

²⁶ ASC Sanctions Decision at para 134.

²⁷ *Belteco Holdings Inc. (Re)* (1998), 21 OSCB 7743 at 7746-7747.

detrimental to the integrity of Ontario's capital markets and therefore prejudicial to the public interest.²⁸

V. ANALYSIS AND CONCLUSION

- [21] I am satisfied that Fauth has been subject to an order by a securities regulatory authority, namely the ASC, that imposed sanctions, conditions, restrictions or requirements and that the precondition for an order under s.127(1) of the Act has been met.
- [22] Fauth's misconduct was extremely serious. Over a period of approximately ten years, he raised investor funds totaling about \$15.5 million from at least 75 investors without being registered and without any exemption from registration. Fauth had extensive experience in the capital markets, was previously a registrant in Alberta, was familiar with the regulatory environment and knew that there were requirements under securities laws which could affect his fundraising activities on behalf of Espoir.²⁹
- [23] Fauth solicited these investor funds through misleading and fraudulent representations, which caused significant financial and personal hardship to investors. The impact was especially significant on those investors who lost their life savings and were retired or nearing retirement.³⁰
- [24] Registration is a cornerstone of securities law designed to ensure that those who sell or promote securities are proficient, solvent and act with integrity. Unregistered trading or promotion of securities defeats some of these necessary legal protections and undermines investor protection and the integrity of the capital markets.³¹
- [25] Fraud is one of the most egregious securities regulatory violations. It causes direct and immediate harm to its investors, and it significantly undermines confidence in the capital markets.³²
- [26] It is important that this Commission impose sanctions that will protect Ontario investors by specifically deterring Fauth from engaging in similar or other misconduct in Ontario, and by acting as a general deterrent to other like-minded persons.
- [27] Staff submits that an order permanently prohibiting Fauth from participating in Ontario's capital markets is necessary in the circumstances. I agree that such an order is in the public interest.
- [28] The findings of the ASC demonstrate the Fauth's conduct has an Ontario connection as funds were raised by Fauth from Ontario investors.³³ However, in the circumstances of this matter, including the serious nature of the misconduct, an Ontario connection is not a necessary condition to my granting an order imposing sanctions on Fauth. The Commission has previously relied on findings

²⁸ *Cartaway Resources Corp.*, 2004 SCC 26 (CanLII) at para 60; *Committee for Equal Treatment of Asbestos Minority Shareholders v Ontario (Securities Commission)*, 2001 SCC 37 (CanLII) at paras 42 to 43.

²⁹ ASC Sanctions Decision at para 50.

³⁰ ASC Sanctions Decision at para 45.

³¹ *Meharchand (Re)*, 2019 ONSEC 7 at para 47 (**Meharchand**).

³² *Meharchand* at para 51.

³³ ASC Merits Decision at para 46.

made by other provincial securities regulators and not required an Ontario connection in determining that an inter-jurisdictional order is necessary to protect Ontario investors and the integrity of the Ontario capital markets.³⁴

A. Differences between Alberta and Ontario sanctions

[29] Due to differences between the Act and the Alberta Act, some of the sanctions I impose differ from those imposed by the ASC, as outlined below.

[30] The ASC prohibited Fauth from “acting in a management or consultative capacity in connection with activities in the securities market.”³⁵ This terminology is not used in subsection 127(1) of the Act.³⁶ Such activities will largely be prohibited by an order prohibiting Fauth from acting as a director or officer of any issuer or registrant or from becoming or acting as a registrant or promoter.³⁷

VI. CONCLUSION

[31] For the reasons set out above, a permanent ban prohibiting Fauth from participating in the Ontario capital markets is necessary to adequately protect investors and the Ontario capital markets. I therefore order that:

- a. pursuant to paragraph 2 of subsection 127(1) of the Act, trading in any securities or derivatives by Fauth shall cease permanently;
- b. pursuant to paragraph 2.1 of subsection 127(1) of the Act, the acquisition of any securities by Fauth is prohibited permanently;
- c. pursuant to paragraph 3 of subsection 127(1) of the Act, any exemptions contained in Ontario securities law do not apply to Fauth permanently;
- d. pursuant to paragraphs 7, 8.1 and 8.3 of subsection 127(1) of the Act, Fauth resign any positions he holds as a director or officer of an issuer or registrant;
- e. pursuant to paragraphs 8, 8.2 and 8.4 of subsection 127(1) of the Act, Fauth is prohibited permanently from becoming or acting as a director or officer of any issuer or registrant; and
- f. pursuant to paragraph 8.5 of subsection 127(1), Fauth is prohibited permanently from becoming or acting as a registrant or promoter.

Dated at Toronto this 21st day of January, 2021.

“Wendy Berman”
Wendy Berman

³⁴ *Cook (Re)*, 2018 ONSEC 6 at para 9; *Elliott (Re)* (2009), 32 OSCB 6931 at paras 24 and 25.

³⁵ ASC Sanctions Decision at para 134.

³⁶ *McClure (Re)*, 2017 ONSEC 34 at para 8 (**McClure**).

³⁷ *McClure* at para 9.