

**IN THE MATTER OF THE SECURITIES ACT
R.S.O. 1990, c. S.5, AS AMENDED**

AND

**IN THE MATTER OF
MARK EDWARD VALENTINE**

HEARING: July 2, 2002 and July 8, 2002

**PANEL: Howard I. Wetston, Q.C. - Chair of the Panel
Robert W. Davis, FCA - Commissioner
Derek Brown - Commissioner**

**COUNSEL: Melissa Kennedy - For the Staff of the Ontario Securities
Alexandra S. Clark Commission
Kate Wootton**

**Joseph Groia - For Mark Edward Valentine
Janice Wright
Matthew Scott**

REASONS FOR ORDER ISSUED JULY 8, 2002

These are the reasons for an order issued by the Commission on July 8, 2002, in which a temporary order against Valentine was extended pursuant to s. 127 of the *Securities Act*.

Background

Mark Edward Valentine (“Valentine”) is the Chairman and largest shareholder of Thomson Kernaghan & Co. Ltd. (“TK”). He is a Registered Representative with the Investment Dealers’ Association and is a Director and the designated trading officer for TK.

Valentine is also the President, CEO, Director and shareholder of two private companies, VMH Management Ltd. (“VMHM”) and VC Advantage Limited (“VCA”). VMHM is the General Partner that manages the Canadian Advantage Limited Partnership (“CALP”) and the Advantage (Bermuda) Fund Ltd. (“CALP Offshore Fund”). VCA is the General Partner that manages the VC Advantage Fund Limited Partnership (“VC Fund”) and the VC Advantage (Bermuda) Fund Ltd. (“VC Offshore Fund”). (These funds will be referred to collectively as the “funds”).

Valentine was authorized to recommend, advise and enter into all investments on behalf of the funds. He was also the Registered Representative at TK for the funds, however, neither Valentine nor the management companies are registered with the Commission as Investment Counsel/Portfolio Manager.

Staff, by Notice of Hearing dated June 24, 2002, alleges that Valentine engaged in conduct that was contrary to the public interest. It is alleged that Valentine created a culture of conflict and non-compliance at TK and breached Ontario securities laws in respect of a series of transactions. Staff alleges, by way of a Statement of Allegations dated June 24, 2002, that Valentine benefited from these transactions at the expense of his clients.

The Temporary Order

On June 17, 2002, the Commission concluded that the public interest warranted the issuance of a temporary order against Valentine suspending his registration and further ordered that his trading in any securities cease. The suspension took effect immediately and was to expire on the fifteenth day after its issuance unless further extended by the Commission. The temporary order restrained Valentine from making trades in the funds' accounts, his own accounts or in any TK client accounts.

Staff and the IDA have been conducting an intensive investigation into the affairs of Valentine, including his actions as General Partner of limited partnerships including the Canadian Advantage Limited Partnership and the VC Advantage Limited Partnership. In addition, Staff were informed that on June 13, 2002, as a result of an internal investigation, TK suspended Valentine's employment and took steps to and exclude him from TK's premises. The Commission was of the opinion that a temporary order was required since the time necessary to conclude a hearing in this matter would be prejudicial to the public interest.

Staff's Submissions

Staff relies on s. 127(7) to seek an extension of the temporary order that was issued on June 17, 2002. In the alternative, Staff seeks to extend the order on the basis that Valentine has failed to provide satisfactory information to the Commission pursuant to s. 127(8).

Staff submits that a temporary order should be extended when it is necessary to protect the investing public and the capital markets in general. Furthermore, Staff submits that there is no requirement to find a specific violation of the *Securities Act* in order to grant the extension; *Re C.T.C. Dealer Holdings Ltd. et al. And Ontario Securities Commission et al.* (1987), 59 O.R. (2d) 79. Staff contends the Commission need only determine whether sufficient information has been provided to demonstrate that the public interest is at risk and that the public requires protection; *Pezim v. British Columbia (Superintendent of Brokers)* (1994), 114 D.L.R. (4th) 385 (S.C.C.).

Staff contends that the Commission must take steps to ensure that confidence in the capital markets is not undermined when those whose integrity is questioned participate in them. This is essential to help further the goals of fostering fair and efficient capital markets and protecting investors from unfair, improper and fraudulent practices.

Staff submit that they have presented sufficient evidence to call into serious question Valentine's integrity. By creating a culture of conflict and non-compliance and acting in

his own interests at the expense of his clients, Valentine failed to deal fairly, honestly and in good faith with his clients. Staff, therefore, argues that the temporary order against Valentine should be extended to prevent any likely future harm to investors and the capital markets. The purpose of such an order is not punitive but to restrain any future conduct that is likely to be prejudicial to the public interest.

In this regard, Staff called two witnesses with respect to certain matters contained in the allegations dated June 24, 2002, against Valentine. The first witness was Michael Hubley, the Assistant Manager of Investigations in the OSC's Enforcement Branch. He is also the case manager for this particular investigation.

Mr. Hubley testified with respect to Staff's investigations into Valentine's trading activities. He indicated that the OSC is also monitoring an investigation being conducted by the IDA. He provided details of TK's own internal investigation of Valentine's activities, particularly the Chell and IKAR transactions, as contained in TK's investigation report.

The second witness was Paul Kennedy. Mr. Kennedy is a commercial real estate lawyer in Toronto who testified that he was harmed as a result of being a client of TK. On the recommendation of TK, he invested in securities of a company called JAWZ Inc. ("JAWZ") in which he alleges that he later discovered a potential conflict of interest relating to a financing in which Valentine participated. Through this financing, Valentine is alleged to have created a situation where one client of TK, namely CALP, was

motivated to engage in a particular trading strategy regarding securities of JAWZ. At the same time, however, TK was recommending to other clients that they buy securities of JAWZ, without disclosure of this financing.

Valentine's Submissions

Mr. Groia submits that Staff's investigation into Valentine's conduct is likely to be a long and arduous process. The main issue for the Commission is what should happen to Valentine while that process unfolds.

Counsel contends that people are encouraged to invest in Ontario and trade in this marketplace and they do so in reliance on the fairness and the integrity of our markets. They also do so in reliance on an understanding that access to our marketplace will not be removed or restricted for reasons that are arbitrary or capricious. Mr Groia submits that the Commission is being asked to take Valentine out of the marketplace before Staff's investigation has been completed. In this regard, Mr. Groia contends that the Commission's public interest jurisdiction under s. 127 should not be used to punish Valentine on the basis of alleged wrongdoings.

Valentine does not consent to an extension of his temporary registration suspension, but he does not oppose it. Valentine does, however, oppose any extension of the cease trade order.

Counsel submits that there must be clear and compelling evidence that Valentine poses some kind of menace that would require the removal of his personal trading privileges. Therefore, although this is not an injunction application, Mr. Groia contends that there must be some evidentiary standard that satisfies the Commission that the relief requested by Staff is in the public interest.

In this regard, Mr. Groia argues that the impugned conduct, which Staff submits as being contrary to the public interest, is related to activities that Valentine is alleged to have carried out in his capacity as a registrant. As such, there is no basis to suggest that the public interest requires protection from Valentine's own personal trading activities. Alternatively, counsel submits that Valentine be permitted to trade on his own account subject to certain conditions and reporting requirements.

Analysis

The Commission may make an order in the public interest under section 127(1) provided a hearing is held pursuant to section 127(4). Section 127(5) recognizes a temporary order may be made, *ex parte*, in circumstances where the length of time required to hold a hearing would be prejudicial to the public interest. Section 127(9) requires that a notice of hearing accompany the temporary order and, according to s. 127(6), the temporary order takes effect immediately and expires on the fifteenth day after its making unless further extended by the Commission.

Section 127(7) allows the Commission to extend a temporary order issued under s. 127(5) until the hearing is concluded provided a hearing is commenced within the fifteen-day period prior to expiry. In the case of a cease trade order made pursuant to subsection 127(1)2, the Commission, under s. 127(8), may extend a temporary order for such period as it considers necessary if satisfactory information has not been provided to the Commission within the fifteen-day period.

Valentine suggested that there was little if anything on the face of the order that would provide a sufficient basis for issuing the order. While there must be a reasonable basis to issue the temporary order under s. 127(5), the reasons for its issuance are not before us. The issue herein is not whether the temporary order should have been issued. In this hearing we must determine, on the evidence before us, whether the temporary order should be extended.

The role of the Commission in matters relating both to the protection of the public interest and sanctions is discussed in *Re Mithras Management Ltd. et al* (1990), 13 OSCB 1600. While Mithras does not deal with the extension of a temporary order, its reasons are instructive:

Under sections 26, 123 and 124 [now section 127] of the Act, the role of this Commission is to protect the public interest by removing from the capital markets – wholly or partially, permanently or temporarily, as the circumstances may warrant – those whose conduct in the past leads us to conclude that their conduct in the future may well be detrimental to the integrity of those capital markets. We are not here to punish past conduct; that is the role of the courts, particularly under section 118 of the Act. We are here to restrain, as best we can, future conduct that is likely to be prejudicial to the public interest in having capital markets that are both fair and efficient. In so doing we must, of necessity, look to past

conduct as a guide to what we believe a person's future conduct might reasonably be expected to be; we are not prescient after all. And in so doing, we may well conclude that a person's past conduct has been so abusive of the capital markets as to warrant our apprehension and intervention, even if no particular breach of the Act has been made out... (at p. 1610). [Emphasis added.]

It is apparent that the Commission may be required to extend a temporary order before an investigation is completed. This authority enhances the Commission's capacity to protect the capital markets by allowing it to take preventative action; *Re C.T.C. Ltd.* (1987), 10 OSCB 857.

In *Biller v. British Columbia (Securities Commission)*, [1998] B.C.J. No. 451 (BCCA), the BCSC had made a temporary order against Mr. Biller. Mr. Biller alleged that a temporary order was akin to an injunction and, as such, the BCSC erred in failing to consider the tests of irreparable harm and balance of convenience. At paragraph 11 the BCCA stated:

The submission is, in my view, misconceived. *Temporary orders under the Act undoubtedly have much the same effect as interlocutory injunctions but are fundamentally different in that they are based upon statutory provisions which empower the orders to be made if the Commission or executive director "considers it to be in the public interest"*. To apply the tests applicable to common law injunctions to the exercise of that power would create a confusion of concepts. One may expect that the Commission will have due regard to the potential for harm to those who are subjects of the orders and reasonable regard to the convenience of any persons who might be affected by them. *But, because the basic issue is whether it is in the public interest to make the order, the matters to be balanced are different.* [Emphasis added.]

Section 127(7) provides the Commission with the discretion to extend a temporary order. That discretion, to promote and protect the public interest, is very broad. Having regard

to the legislative scheme as contained in s. 127, as well as the length of time required to conclude a hearing in this matter, we must satisfy ourselves, at this time, that there is sufficient evidence of conduct which may be harmful to the public interest.

In exercising its regulatory authority, the Commission should consider all of the facts including, as part of its sufficiency consideration, the seriousness of the allegations and the evidence supporting them. The Commission should also consider any explanations or evidence that may contradict such evidence. This will allow it to weigh the threat to the public interest against the potential consequences of the order.

In brief, the Notice of Hearing and the Statement of Allegations assert that:

- Mr. Valentine played multiple roles at TK thereby failing to deal fairly, honestly and in good faith with his clients by putting his own interests ahead of his clients;
- Valentine conducted transactions which were not prudent business practices and which did not serve his clients adequately;
- Neither Valentine nor the funds are registered, as required, as an Investment Counsel/Portfolio Manager;

- Valentine failed to maintain adequate books and records necessary to record properly the business transactions and financial affairs which he carried out; and

- Valentine made representations that were contrary to s. 38(1) of the Act.

TK conducted an internal investigation of Valentine's activities. The investigation found that the propriety of certain transactions was "questionable"; there was "inadequate documentation" for other transactions; Valentine failed to provide documents to TK to support certain transactions; and "the rationale was not supportable" for an entire series of transactions.

TK took highly unusual steps against Valentine. He is the Chairman and largest shareholder of TK. Nevertheless, TK suspended his employment and barred him from contact with any of its employees. TK also reversed the Chell and IKAR transactions and delivered its Investigation Report to the IDA.

The IDA and the OSC are currently and actively investigating these matters. This includes the financing of JAWZ Inc. in which it is alleged that Valentine created an environment where one client, namely CALP, was strongly motivated to engage in a trading strategy that was harmful to investors while TK was recommending to other clients to buy without adequate disclosure of this financing.

The Commission requires sufficient evidence to extend a temporary order if such extension is not on consent. Mr. Hubley explained in some detail the nature of the investigation and certain key facts underpinning the Notice of Hearing and Statement of Allegations. Similarly, Mr. Kennedy provided some evidence in support of the allegations against Valentine.

If proven, the allegations against Valentine demonstrate that we are not dealing with a single isolated event. Moreover, two of the transactions, namely the Chell and IKAR transactions, are very recent, taking place at the end of March 2002. It is also apparent that the issues are very complex and the investigation is far from complete. In fact, according to Mr. Hubley's testimony, Staff are currently reviewing over 1,900 boxes of material and 240 gigabytes of computer data as part of the investigations into Valentine's conduct.

Mr. Groia argues that the disputed transactions are related to Valentine's activities as a registrant and, therefore, should have no impact on his personal trading activities. While it may be possible to differentiate Valentine's activities as a registrant from his personal trading activities, in this case, we are not persuaded by this submission. In *Barbara A. Danuke et al*, September, 1981 O.S.C.B. 31, an insider trading case, the Commission commented on the conduct of registrants at p. 41:

“Ethical conduct, for that is what we are considering, cannot be defined in advance and with that kind of precision. Indeed if any regulatory body, such as the Commission or the T.S.E., were to attempt to do so the unethical would pattern their conduct as closely to the borders of the defined ethical conduct as the language in which that definition is phrased permits. **It is for registrants to be sensitive to their responsibilities to**

their clients and to their employers and to the integrity of the marketplace which they serve in the conduct of their personal trading. It is trite to observe that the grant of special status as a registered sales person or trading officer carries with it a commensurate obligation.” [Emphasis added.]

No final determination can be made with respect to the allegations against Valentine until the hearing is completed. That is in the future. However, at this time, in order to protect the public interest, we must not hesitate to use the regulatory tools that are at our disposal. This includes, when appropriate, the extension of temporary orders under s. 127.

At this stage, despite Valentine’s non-opposition to the registration suspension, we are satisfied that Staff has provided sufficient evidence of conduct that may be harmful to the public interest and, accordingly, justifies an extension of the temporary order. There is little doubt that additional time is required to complete the investigation and, unless the temporary order is extended, there is a reasonable likelihood that Valentine’s alleged objectionable conduct may continue. Such conduct would present a serious risk to the integrity of Ontario’s capital markets as well as to the protection of the public interest.

While we have permitted Valentine to trade, subject to certain restrictions set out in the order, it is not because we accept counsel’s argument that Valentine’s activities as a registrant can be disconnected from his personal trading. We permitted Valentine to trade because it is our opinion that there would be little or no risk of harm to the public to allow him to do so on a restricted basis.

Conclusion

For the above reasons, the Commission extended the temporary order dated June 17, 2002 by order dated July 8, 2002. The terms of the order are:

- the registration of Valentine is suspended and the exemptions contained in Ontario securities law do not apply to Valentine for a period ending January 31, 2003;
- during this period, Valentine is cease traded from trading certain securities except for trades made for his own account or for the account of his registered retirement savings plan of those securities referred to in clause 1 of subsection 35(2) and those that are listed on the Toronto Stock Exchange or the New York Stock Exchange (or their successor exchanges);
- Valentine is restricted from owning directly, or indirectly through another person or company or through any person or company acting on his behalf, more than one (1) percent of the outstanding securities of the class or series of the class in question; and
- if a hearing pursuant to the Notice of Hearing dated June 24, 2002, in connection with the matters set out in the Statement of Allegations, is not commenced before January 31, 2003, staff may apply to the Commission for an order to extend this order for such further period as the Commission considers appropriate.

Dated at Toronto this 30th day of July, 2002.

“Robert W. Davis”

“Derek Brown”

“Howard I. Wetston”