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

AND

IN THE MATTER OF
FIRST FEDERAL CAPITAL (CANADA) CORPORATION AND
MONTE MORRIS FRIESNER

Hearing:	**May 29, 2003**		
Panel:	**Paul M. Moore, Q.C.**	**-**	**Vice-Chair (Chair of the Panel)**
	M. Theresa McLeod	**-**	**Commissioner**
	Harold P. Hands	**-**	**Commissioner**
Counsel:	**Alexandra Clark**	**-**	**For Staff of the Ontario Securities Commission**
	Ronald Pelletier	**-**	**For First Federal Capital (Canada) Corp. & M. Friesner**

DECISION AND REASONS

I. The Proceeding

[1] This proceeding was a hearing under sections 127 and 127.1 of the *Securities Act*, R.S.O., 1990, c. S.5 (the Act) as to whether it would be in the public interest to make one or more of the orders referred to in the amended notice of hearing dated April 2, 2003[1] in the matter of First Federal Capital (Canada) Corporation (First Federal) and Monte Morris Friesner (Friesner).

[2] On December 11, 2000, the Commission ordered, pursuant to clause 2 of section 127(1) of the Act, that all trading in securities by First Federal and Friesner cease for a period of 15 days. On December 12, 2000, the Commission issued a notice of hearing in this matter commencing December 20, 2000. On December 20, 2000, the Commission adjourned the hearing *sine die*, to be brought back before the Commission on seven days notice by either party, and extended the order of December 11, 2000 until the hearing was concluded and a decision rendered or until otherwise ordered by the Commission.

[3] On April 2, 2000, staff of the Commission issued an amended statement of allegations in this matter, amending the statement of allegations accompanying the original notice of hearing.

[4] The purpose of the hearing was for the Commission to consider whether, pursuant to sections 127(1) and 127.1 of the Act, it is in the public interest for the Commission:

i) to make an order that the respondents cease trading in securities, permanently or for such time as the Commission may direct;

ii) to make an order that the respondents be reprimanded;

iii) to make an order that Friesner resign all positions that he holds as a director or officer of an issuer;

iv) to make an order that Friesner be prohibited from becoming or acting as director or officer of an issuer permanently or for such time as the Commission may direct;

v) to make an order that the respondents pay the costs of staff's investigation in relation to this matter;

vi) to make an order that the respondents pay the costs of this proceeding incurred by or on behalf of the Commission; and

vii) to make such other order as the Commission may deem appropriate.

II. The Allegations

[5] In essence, staff of the Commission alleged that First Federal and Friesner:

1 As set out in paragraph 4.

i) acted as advisers, as defined in the Act, without being registered under section 25 of the Act;

ii) traded securities, namely investment contracts evidenced in account agreements and related documents for its Asset Securitization Management Portfolios that were administered, created and managed by First Federal (the Trading Program), without being registered to trade securities under section 25 of the Act;

iii) made inappropriate statements to potential investors regarding the Trading Program (such as: "the investors' assets are guaranteed," and, "First Federal cannot perceive any circumstances in which the investor receives a return of less than 70% per annum"); and made promises regarding the risk-free nature of the Trading Program; and

iv) distributed the Trading Program without a prospectus contrary to section 53 of the Act.

[6] Staff further alleged that Friesner authorized, permitted or acquiesced in First Federal's conduct in connection with the Trading Program.

[7] Staff alleged that this conduct of the respondents contravened Ontario securities law and was contrary to the public interest.

III. Submissions of Counsel

A. Submissions of staff

[8] Staff submitted that

i) the Trading Program offered by the respondents was a security in that it was an investment contract;

ii) the offering of an investment contract to Mr. Samson was an act in furtherance of a trade, and therefore trading in a security;

iii) it was not necessary that an actual trade in the investment contract be consummated in order for the offering to constitute an act in furtherance of a trade; and

iv) the evidence established that the respondents held themselves out as being in the business of advising, and, therefore, acted as advisers, as well as trading in securities, contrary to section 25 of the Act.

B. Submissions of respondents

[9] The respondents submitted that

i) the facts and evidence do not disclose that there was a trading in or an advising of a distribution of securities;

ii) any trading required there to be consummated trades, and there was no evidence of such;

iii) portfolio securities were to be traded by the trading and settlement bank, not the respondents. The documentation explicitly disclaimed that the respondents were trading or advising and that the investor should do its own due diligence on its bankers; and

iv) Friesner was not responsible for the conduct of First Federal.

IV. Facts

[10] The following facts were agreed between staff and the respondents:

The Respondents

i) First Federal was incorporated under the laws of Ontario on January 7, 1999. First Federal is not a reporting issuer and has never been registered in any capacity under the Act.

ii) Friesner resides in Toronto, Ontario and was at all material times a director, the president and chief executive officer of First Federal. Friesner has never been registered in any capacity under the Act.

Chronology of events

iii) From approximately January 1999 to February 2000, and again from June 2000 to December 2000, First Federal operated a web site at www.firstfederalcanada.com (the web site). The web site first came to the attention of staff in or about September 1999.

iv) On January 19, 2000, Colin McCann, an investigator with the Commission, using a fictitious identity referred to as "B. Samson" (Mr. Samson), contacted the email address listed on the web site and requested information on investment products and services offered by First Federal. No response was received by Mr. Samson until on or about May 18, 2000.

v) By letter dated February 18, 2000 addressed to Friesner and First Federal, McCann advised that it was the opinion of staff that the content of the web site dealing with the solicitation of investment products may contravene the Act. Staff requested further information in order to reach a precise determination.

vi) In a telephone conversation with McCann on February 21, 2000, Friesner stated that he would shut down the web site until the matter could be resolved and Friesner could meet with staff. The web site was shut down that day.

vii) By email dated May 18, 2000, Friesner responded to the January 19, 2000 email from Mr. Samson asking him to advise as to the kind of secured investments he would be most interested.

viii) By email dated May 25, 2000, Mr. Samson advised Friesner that he was interested in investments with a higher than bank return and any other similar investments.

ix) By letter dated June 28, 2000, addressed to Mr. Samson and received by staff on July 13, 2000, Friesner provided Mr. Samson with a number of documents pertaining to the Trading Program which Mr. Samson had inquired about and expressed an interest in.

x) In or about June 2000, the web site was reinstated, which was confirmed by McCann on July 13, 2000. The content of the web site had been changed since it was shut down on February 21, 2000.

xi) Staff had no further communications with or from the respondents after receiving Friesner's letter of June 28, 2000 until after obtaining the temporary cease trade order.

xii) In particular, on or about December 11, 2000, without notice to the respondents, staff obtained the cease trade order.

xiii) After receiving notice of the cease trade order, First Federal closed down its web site and the web site has not been reinstated to date.

xiv) With the consent of the respondents on December 20, 2000, staff obtained an order extending the cease trade order "until the hearing is concluded and a decision rendered or until otherwise ordered by the Commission." This cease trade order is still in effect.

V. Evidence

[11] The hearing was held on May 29, 2003. No witnesses were called. However, in addition to an agreed statement of facts, several documents were tendered in evidence.

[12] The following extracts are from the web site on September 9, 1999 (italics added):

> First Federal Capital (Canada) Corporation is a very innovative, privately owned corporation specialized in Asset Management, Credit Facilities, Credit Enhancement Loans, High Yield Investments.
>
> First Federal Capital (Canada) Corporation benefits from the international experience of Pan Arab PetroChem Corporation's considerable client deposit base, and its worldwide network of agents and representative offices, *and from its particular skills in asset management.*

This accumulated expertise, the cornerstone of our past development, will continue to be the constant element in our approach. *Our aim is to enable our clients to benefit, as partners, from the positive results of our asset-management techniques*; the traditional quality of the banks we utilize, and of our client's deposits in the various banks *we have chosen for them* around the Globe.

Economic analysis of developers and their countries requiring attention from an investment standpoint is aimed at identifying investment opportunities, as they arise at any moment throughout the world. *We are thus able to offer our clients sound investments almost anywhere, and with practically no limits as to the complexity of the solutions.*

Our investment analysis is a continuous process. A strategy committee first establishes global investment parameters. The investment committee then makes an in depth study of the latest economic and financial events to identify investment sectors. *The investment committee's conclusions,* which define our position on yield and profit rates in different countries, major currencies, Corporate and Financial Bonds which are completely guaranteed, are immediately distributed to all our representative offices and departments *for the benefit of institutional and private investors.*

Our global view of economic and financial systems can include new and emerging markets that offer attractive investment opportunities. For accounts not managed by our banks, investment parameters established for asset allocation are essential to our managers for portfolio monitoring *and advice to our clients.*

In addition to direct investments, First Federal Capital (Canada) Corporation *offers its own investment products.* These instruments are targeted towards specific sectors or particular objectives, spreading investments across different categories of securities, geographical areas, investment sectors and innovative financial instruments.

The frequency and rapidity of political and economic changes tend to make investment decisions difficult for private clients. The minimum amounts necessary to take advantage of favorable rates and conditions often discourage private clients from changing positions held, preventing them from the active management indispensable for consistent results. Moreover, sophisticated financial techniques are by their very nature out of reach of many private clients. *These techniques however, are often applied in our Secured Investments, and may even constitute the basis of some of them.*

The wide range of our secured investments matches clients' requirements, representing satisfactory and inexpensive solutions, *which assure continuous and qualified management of assets,* irrespective of their size.

> Whether *managed entirely by our experts* or in association with the world's leading specialists, these investments reflect the image of our clients, their investment policies being molded on ours. In most cases, the specialists commissioned by us would be beyond the reach of a private client. Individuals can thus benefit from the same conditions and *advice* as institutional investors.
>
> As far as investments are concerned, we have always been active in the creation and management of corporate bonds and Equity issues *which are completely guaranteed,* and offer an annuity or interest of up to twenty-five percent per annum, as well as consortiums set up to acquire short or long-term participation in companies.

[13] On May 18, 2000, Friesner emailed Mr. Samson asking, "Kindly advise us, as to what kind of Secured Investments you would be most interested in."

[14] On May 25, 2000, Mr. Samson emailed Friesner, "As I recall, you were offering some investments with a higher than bank return and which were affiliated with an Arab Petro-bank. These (and any other) similar type of investments are of interest to me."

[15] On June 28, 2000, Friesner wrote to Mr. Samson enclosing documents for First Federal's Asset Securitization Management Portfolio.

[16] The letter states in part:

> The Asset Securitization Management Portfolio (ASMP) I have arranged with several European Banks is a safe and secure method of creating a Credit Facility (Funding), with benefits (Funds Generated) to the investor that can be utilized immediately. This general format is the same that I have successfully implemented in the past. The Investors' Funds are guaranteed, as they are on deposit with their own bank in a Custodial and Non-Depletion Bank Account. The Bank is expected to be an "AAA" rated bank (according to Standard and Poor's), and should be coded to a Federal Reserve. The Custodial and Non-Depletion Bank Account is in the Investor's own name, and is under his signatory control.
>
> THE INVESTOR can be a Partnership, Joint Venture, Corporation, Charity or even a Singular Party. The Investor controls the funds and the account via the signatory.
>
> The benefits generated are disbursed between the Investor, Bank Representatives, and the Introducing Parties. The Investor receives an estimated 70% return per annum on the amount of funds invested for the contracted period. We cannot perceive any circumstances in which the Investor receives a return of less than 70% per annum. 20% percent is shared amongst all the parties involved, such as, accountants, lawyers, bank fees and introducing parties. The net amount generated to the Investor, including interest earned on the account will be approximately 50% to 55% per annum.

The above Secured Investment Portfolio has been open to new and old investors as of January 5, 1999 when the Banks' Representative submitted to First Federal Capital (Canada) Corporation the itinerary for the ASMP. I am submitting to you with this letter of introduction the memoranda, which will explain and clarify this investment.

Please review the following paragraphs, as an introduction to the Investment:

Procedure:

Requirement - $10,000,000.00 USD on deposit with a major bank
- Proof of Funds letter from Investor's bank

Characteristics - A custodial and Non-Depletion Bank Account under control of Investor.

Trading:

The Investor will sign a Trading Contract directly with the Trading Settlement Bank (rated "AA") or better as per Standard and Poor's. The Trading and Settlement Bank will trade Bank Subordinate Notes and other securities on behalf of the Investor, on a best effort basis. The term of the Contract will be for a period of one (1) year, but maybe renewed for the following year.

The signatory (Investor) will attend at the Trading and Settlement Bank to meet with the Director of the Bank, and should conduct a complete due diligence in order to satisfy himself as to the validity and security of the investment. The Signatory can withdraw at any time, without any liability and without any reason, if he is not completely satisfied.

The safety of the Investor's capital (Funds) on deposit at his own bank is as secure as his own bank is in the financial community. The benefit (Profit) that is available should be of interest to your investors, and also to you as an investor. Complete due diligence and information that a knowledgeable investor desires to confirm, is made available at all times, since the Investor meets directly with the Director of the Trading and Settlement Bank.

Any major bank can administrate a Custodial and Non-Depletion Account, and the following banks have agreed to maintain a Custodial and Non-Depletion Bank Account and also have approved the Asset Management Joint Venture Agreement and Custodial and Non-Depletion Account Memorandum:

- © Royal Bank of Canada
- © ING - The Netherlands
- © RaboBank - The Netherlands

- © AGN/AMRO - The Netherlands
- © TD Trust - Toronto
- © Bank of America
- © Chase Manhattan Bank
- © Citicorp

[17] Included with the June 28, 2000 letter was a document entitled "Asset Securitization Management Portfolio Synopsis". It states in part:

> In recent years there has been a blossoming of many Asset Securitization Management Portfolios (programs), also known as Secured Investment Portfolios (programs). These portfolios are based on the continuous buying and selling of bank issued debenture instruments, and offer a superior return on investment for investors who are able to provide a minimum of $10,000,000.00, as outlined by the working capital. More recently, portfolios have cropped up that allow also the small investor to take advantage of this type of investing. However, $1,000,000.00 is still the minimum accepted in most of these portfolios, which become a partnership or Joint Venture.
>
> A secure portfolio, with compounding of investment funds, can make the investor profits of between 50% and 70% or MORE, with ZERO RISK! The money never leaves the investor's Custodial bank! If the portfolio works the investor gets the promised return, and if the portfolio does not work the investor still has the money in his bank. The investor has lost nothing more than the time necessary to fill in the forms. It is a pure *'win or not lose'* situation.
>
> . . . .
>
> Many of these institutions participate in fashioning *'self-liquidating credit enhancement loans'*, where the spread between the low issue price and the eventual collection of the principal and interest is used by the project being financed. This is still pretty much an insider's game. These Asset Securitization Management Portfolios are still known and understood by a very few privileged and wealthy investors. It is probably safe to say that 99% of the investing public in the United States has never heard of these types of Asset Securitization Management Portfolio (trading programs).
>
> If you were to walk into any American bank or brokerage firm and inquire about these types of portfolios, you would likely be told that such programs do not exist. There is no such thing as a *'bank subordinate note or debenture'* or a *'prime bank guarantee'* and that letters of credit are used only for trade transactions. Meanwhile, in the executive suites of these same firms, the top executives are actively pursuing investments in the very programs that the lower ranks are not even aware of.

> After talking to a number of bankers and brokers about these portfolios, it is clear that the rich and powerful would be pleased if this information were kept secret. In the United States the supply of money or credit is regulated by the Federal Reserve Corporation, a privately held corporation. It is not an agency of the federal government. The Federal Reserve Corporation is an independent body that came into existence through an act of Congress in 1913, and with the cooperation of certain key international banks, referred to as *'prime banks'* (coded to the Federal Reserve).
>
> . . . .
>
> This is a very private business; not advertised anywhere, nor covered by the press. Generally, these portfolios are only open to the most connected, wealthy entities with substantial cash to put up for investment. The privacy of this business is maintained from the original issuing bank all the way down to the retail buyer. As such it is evident, one of the keys to the profitability of these Asset Securitization Management Portfolios is having the resources and the contacts to be able to purchase these bank debenture instruments at a level as close to the issuing bank as possible (at the highest discount), and having the resources and contacts to sell the investments to the retail buyer at the highest price level.
>
> As you can imagine, these contacts are very jealously guarded. So the real secret of successful investing is not just in knowing *'the how, why and where'* of these types of transactions. The most important piece of the puzzle is in knowing the Bank Representatives, Bankers, or Intermediaries, who can weave these opportunities and the necessary resources into a secure, profitable and responsible investment portfolio.
>
> . . . .
>
> Many investment professionals have the ingrained belief that they already know everything significant that is going on in the world financially. When they are advised of these types of portfolios, their automatic reaction is that it must be a *'scheme'*.
>
> . . . .
>
> It is just so hard for the uninitiated to believe that such huge profits are possible. After all, the typical pension funds' manager struggles each year to beat the Standard and Poor average of 9% per year. Talking about 70% is simply light years outside the realm of experience and seems unbelievable to them.

[18] Also included with the June 28, 2000 letter was a document entitled "Memorandum Asset Securitization Management Portfolio (addendum A-1) (Secured investment Portfolio Currency Deposit)". It states in part:

All the Benefits generated on the Currency Deposit portfolio is deposited into the Custodial and Non-Depletion Account, and will be distributed accordingly, upon direct Payment Disbursement Directions.

. . . .

4. The Investment Funds will be deposited at a major bank in Europe, United States or Canada with a rating of an "AA" or better-rated bank, according to Standard and Poors, in order to be utilized in the creating of the Secured Investment Portfolio. The Account will be in the name of the Partnership or Company (Syndicate) that owns the Currency, and only their authorized signatory controls that account.

. . . .

WE DO NOT CONDUCT ANY FORM OF TRADING, NOR DO WE REPRESENT IN ANY MANNER THAT WE ARE THE TRADERS. THE TRADING AND SETTLEMENT BANK IS IN FULL CONTROL OF ALL TRADING AND SECURED INVESTMENT PORTFOLIOS.

. . . .

13. As a concise part of all Agreements, the Jurisdiction and signing of all Agreement will be conducted at the Corporate Offices of First Federal Capital (Canada) Corporate located at 25 King Street West, Suite 2900, Commerce Court North, Toronto, Ontario, M5L 1E2

. . . .

15. The Fee of 1/8% of the Portfolio will be paid to First Federal Capital (Canada) Corporation and Nederlandse Frugalman Private Trust, each on a weekly basis to the full term of the Trading. A Payment Direction must be signed by the Signatories to their Custodial Bank releasing the above funds.

16. The Trading and Settlement Bank will pay this amount. The Company of Investor does not pay any form of Commission or Fee at any time to either First Federal Capital (Canada) Corporation, or to Nederlandse Frugalman Private Trust.

17. The Company (Syndicate) will be responsible to pay out any fees out of the Benefit to the introducing Parties, Brokers, Accountants, Barristers and Solicitors and their own bank fees.

VI. The Respondents' Position

[19] The respondents argued the following:

i) They could not have been advising or trading in securities because the Trading Program did not constitute a security or an investment contract, particularly by reason that there was no bag of silver coins as in *Pacific Coast Coin Exchange* v. *Ontario Securities Commission*, [1978] 2 S.C.R. 112, 80 D.L.R.(3d) 529, or any other identifiable asset. Furthermore, the alleged Trading Program could not be bought, sold, pledged, or assigned. In addition, there was no identifiable issuer of the alleged Trading Program and all of the alleged trading would have taken place through a third party, the Trading and Settlement Bank (the Bank).

ii) The decision of the British Columbia Securities Commission in *Re Hrappstead*, [1999] 15 B.C.S.C.W.S 13, is not binding in Ontario and is inconsistent with Ontario law as evidenced by *Re Costello* (2003), 26 O.S.C.B 1617, *Re Canadian Shareholders Association* (1992), 15 O.S.C.B 617, *Re McGuire* (1995), 18 O.S.C.B 4623, *Re Dodsley* (2003), 26 O.S.C.B 1799 and *Re Donas*, [1995] 14 B.C.S.C.W.S 39.

iii) Even if the alleged Trading Program was a security, the conduct complained of did not constitute advising in securities because the web site contained nothing more than investment information and the documents mailed to Mr. Samson were authored by third parties and contained nothing more than investment information. Specifically, there was no proposal individually tailored to a particular customer or class of customers.

iv) Any fees or commissions to be paid to First Federal were to be paid by the Bank. It was no more than a referral fee. Specifically, there was no evidence that the investor/customer would pay any money, fees or commissions to the respondents either directly or through the payment of commissions or a portion of any profits that may be earned.

v) Posting of information on the Internet does not constitute trading if the document contains a prominently displayed disclaimer. In this regard, the web site clearly stated that First Federal did not represent itself as a trader, nor did it sell, purchase of trade in any securities or bonds. In addition, the documentation mailed to Mr. Samson clearly stated (in bold, capitalized letters) that First Federal did not conduct any form of trading.

vi) There was no act in furtherance of a trade because the activity in question did not have sufficient proximate connection to an *actual* trade (*Costello*). There was no evidence of any actual trading in this case. To the extent that *Dodsley* and *Hrappstead* suggest an act in furtherance of a trade does not require an actual trade, those cases are inconsistent with a plain reading of the Act and of the Commission's decision in *Costello*.

vii) Even assuming no actual trade was required, there was no evidence from which one could determine whether there is a proximate connection between the impugned conduct and any trade that might have taken place. Furthermore, there was no evidence that any trade which might have taken place would not have been exempt under the Act.

viii) The web site belonged to First Federal and the materials mailed to Mr. Samson were mailed on behalf of First Federal. Since First Federal was not a reporting issuer, Friesner should not be held responsible for what, in essence, was corporate activity. Friesner merely acted in his capacity as an officer and director of First Federal.

VII. Applicable Statutory Provisions

[20] Section 25(1) of the Act provides:

> No person or company shall,
>
> a) trade in a security or act as an underwriter unless the person or company is registered as a dealer, or is registered as a salesperson or as a partner or as an officer of a registered dealer and is acting on behalf of the dealer; or
>
> c) act as an adviser unless the person or company is registered as an adviser, or is registered as a representative or as a partner or as an officer of a registered adviser and is acting on behalf of the adviser,

[21] Section 1(1) of the Act provides:

> "adviser" means a person or company engaging in *or holding himself, herself or itself out as* (italics added) engaging in the business of advising others as to the investing in or the buying or selling of securities.
>
> "distribution", where used in relation to trading in securities, means,
>
> a) a trade in securities of an issuer that have not previously been issued,
>
> "security" includes,
>
> n) any investment contract
>
> whether any of the foregoing relate to an issuer or proposed issuer.
>
> "trade" or "trading" includes,
>
> i) any sale or disposition of a security for valuable consideration, whether the terms of payment be on margin, instalment of otherwise, but does not include a purchase of a security or, except as provided in clause (d), a transfer, pledge or encumbrance of securities for the purpose of giving collateral for a debt made in good faith,
>
> ii) any participation as a trader in any transaction in a security through the facilities of any stock exchange or quotation and trade reporting system,
>
> iii) any receipt by a registrant of an order to buy or sell a security,

iv) any transfer, pledge or encumbrancing of securities of an issuer from the holdings of any person or company or combination of persons or companies described in clause (c) of the definition of "distribution" for the purpose of giving collateral for a debt made in good faith, and

v) any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of any of the forgoing.

[22] Section 53(1) of the Act provides:

> No person or company shall trade in a security on his, her or its own account on behalf of any other person or company where such trade would be a distribution of such security, unless a preliminary prospectus and a prospectus have been filed and receipts therefor obtained from the Director.

[23] Section 122(3) of the Act provides:

> Every director or officer of a company or of a person other than an individual who authorizes, permits or acquiesces in the commission of an offence under subsection (1) by the company or person, whether or not a charge has been laid or a finding of guilt has been made against the company or person in respect of the offence under subsection (1), is guilty of an offence. . . .

VIII. Relevant Cases

A. Investment Contract

[24] In *Securities and Exchange Commission v. W.J. Howey Co. et al.* 328 US 293 (1946), the Supreme Court of the United States enunciated a three-part test to determine whether a scheme constitutes an investment contract. The three requirements are that the scheme involve (i) an investment of money, (ii) in a common enterprise, (iii) with profits solely to come from the efforts of others.

[25] In *Howey*, Mr. Justice Murphy stated with respect to the meaning of "investment contract":

> [i]t had been broadly construed by state courts so as to afford the investing public a full measure of protection. Form was disregarded for substance and emphasis was placed upon economic reality. An investment contract thus came to mean a contract or scheme "the placing of capital or laying out of money in a way intended to secure income or profit from its employment". . . . In other words, an investment contract for purposes of the *Securities Act* means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party, it being immaterial whether the shares in the enterprise are evidenced by

> formal certificates or by nominal interest in the physical assets employed in the enterprise. . . . It embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits.

[26] He stated:

> [i]t follows that the arrangements whereby the investors' interests are made manifest involve investment contracts, *regardless of the legal terminology in which such contracts are clothed*" (italics added) . . . the test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others.

[27] This test was refined and endorsed by the Supreme Court of Canada in *Pacific Coast* at page 540. In that case, the court observed:

> . . . to give a strict interpretation of the word "solely" . . . would not serve the purpose of the legislation. Rather we adopt a more realistic test, whether the efforts made by those others than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise . . . .The expression "common enterprise" has been defined to mean . . . one in which the fortunes of the investor are interwoven with and dependent upon the efforts and success of those seeking the investment of third parties.

B. Acting as Adviser

[28] In *Donas***,** the British Columbia Securities Commission clarified that there are two aspects to the question of whether an individual or company is acting as an adviser. The first issue to consider is whether an opinion or recommendation is being offered:

> [t]he nature of the information given or offered by a person is the key factor in determining whether that person is advising with respect to investment in or the purchase or sale of securities. A person who does nothing more than provide factual information about an issuer and its business activities is not advising in securities. A person who recommends an investment in an issuer or the purchase or sale of an issuer's securities, or who distributes or offers an opinion on the investment merits of an issuer or an issuer's securities, is advising in securities.

[29] The second issue to consider is whether the respondent offered the recommendation in a manner that reflected a business purpose, reference *Costello* and *Maguire*. Where a respondent expects to be remunerated in some respect with respect to his activities, a business purpose is reflected, reference *Hrappstead* and *Costello*. There is, however, no requirement that any investor actually follow the recommendation, pay a commission, or invest with the respondent, reference *Hrappstead* and *Re Etherington* (2002), 25 O.S.C.B. 5323.

[30] Documentation made it clear that First Federal was to receive fees from the Trading Program. Whether the fees were payable by the Bank out of its own funds or out of the funds deposited into the deposit account by the investor is not entirely clear. What is relevant, however, in determining whether there was a commercial purpose for First Federal in giving advice is the fact that it was to receive remuneration because of its activities, regardless of the specific manner or the specific person from whom the remuneration would be paid. We note, incidentally, that the documentation required a direction to be signed by the investor, directing the Bank to pay fees to First Federal.

[31] The use of a web site on the internet to solicit investors and to offer advice, in and of itself, may be suggestive of a business purpose.

[32] The distribution of a recommendation to a large number of potential investors, such as through the use of the Internet or other forms of advertisement, has also been held to be reflective of a business purpose, reference *Donas* and *Maguire*.

[33] The provision of recommendations and information formulated by others may, nevertheless, constitute advising on behalf of the person providing the information. As was stated by this Commission in *Dodsley* at page1801:

> [c]ounsel for Dodsley argued that the nature of the information provided by Dodsley was authored by third parties and Dodsley simply recommended or offered an opinion on the merits of investing in commodities generally and that each person is asked to exercise his or her own judgement as to the merits of an investment. We do not accept that position. While certain of the materials were authored by third parties, much was authored by Dodsley and that which was authored by third parties was sent in a package which contained hand-written notes of Dodsley and was sent in a manner in which he expressly or impliedly make recommendations as to investments.

C. Disclaimer

[34] In *Dodsley* the Commission confirmed that the inclusion of disclaimers to the effect that the author is not engaging in trading or advising is not sufficient to insulate a respondent from the requirement to register. The Commission stated:

> [i]t was also argued that the disclaimer contained in the material expressly advised clients that Dodsley's services are other than as an adviser. Again, we do not accept that position in that the material distributed by Dodsley and its contents are not consistent with the content of the disclaimer. Further, we are of the view that having regard to the purpose of section 25 of the Act, it would be inappropriate for one who acts in contravention of section 25 to seek to avoid its requirements simply through a disclaimer. To give any credit to such a disclaimer, in the circumstances, is to avoid the very purpose for which section 25 of the Act was enacted.

IX. Analysis

A. Disclaimer

[35] The disclaimer in the web site was clearly not adequate to bring First Federal within the exemption of section 22(2) of NP 47-201. There is no language saying the Trading Program is not available to Ontario residents and no precautions were entered in evidence by the respondents to ensure Ontario residents did not participate. In fact, First Federal pursued Mr. Samson who Friesner knew was an Ontario resident. The Investment Dealers' Association Member Regulation - 098 does not assist the respondents. The web site goes well beyond providing "investment information" because of the hyperbole used in promoting investments.

[36] The disclaimer in the Trading Program is contradicted by the facts.

B. Investment Contract

[37] The web site material included the statement "our aim is to enable our clients to benefit as partners from the positive results of our asset management techniques." There was to be a clear sharing of benefits of the Trading Program between investors, the Bank and First Federal. There is a promised return of at least 70% per year with 20% shared with the parties involved, including First Federal. This clearly brings the activities within the purview of *Howey*.

[38] The respondents promised fantastic returns. They stated that it is their special expertise and knowledge of matters not generally known to investors that will enable the investors to earn the fantastic returns. They charge a fee for their services which is extreme: 1/8 of a percent of "the portfolio" per week payable to "each of" First Federal and Nederlandse Frugalman Private Trust, likely a related party of First Federal or Friesner.

[39] There is a close parallel between the investment scheme in the *Hrappstead* case and the activities carried out by First Federal in this case. First the promoter would "introduce" the investor to the parties who would generate the profits. There was a common enterprise with both Nederlandse and First Federal receiving compensation. There were misleading representations and exorbitant investment promises. Both held themselves out as being in the business of advising others as to the investing in securities.

[40] The Trading Program is an investment contract and, therefore, a security. It provides for the investment of moneys (minimum US$10 million) from investors in a trading scheme with profits to come from the efforts of others.

[41] It is evidenced by several documents, all of which are provided by the respondents.

[42] The Trading Program and the arrangements for the management and trading of moneys provided by the investor together constitute the security in our case, and not just the assets of the portfolio of securities that would result from the investment of funds through the Trading Program.

[43] The Trading Program revealed in the documents, when carefully analyzed, is incomprehensible. In some respects it is incredible. That does not mean it is not an investment contract and therefore not a security. It clearly is a scheme that, simplistically speaking, says: "Give us your money. We'll find others to invest it for you in accordance with our Trading Program. We

have access to experts who know what they're doing although the vast majority of persons have no idea. The returns you're going to make are fantastic." We find this to be an investment contract within the meaning of *Howey* and *Pacific Coast.*

[44] The fact that the website contained very poor disclosure on the type of underlying investments the trading and settlement bank might make is no reason to conclude that there were no underlying assets forming the *corpus* of the thing to be managed, such as bags of silver in ***Pacific Coast*** or a citrus grove in the *Howey* case.

C. Act in Furtherance of a Trade

[45] The Trading Program was offered to investors on the Internet. Such offering was an act in furtherance of anticipated trades that would result from investors committing to the Trading Program. As an act in furtherance of anticipated trades, the offering itself constituted trading in the investment contract.

[46] In the case before us there was no evidence that any investment contract was ever entered into by a potential investor. Certainly, Mr. Samson never made an investment. However, in *Hrappstead*, the British Columbia Securities Commission found that an act in furtherance of a trade does not require a completed sale of a security. This Commission came to a similar conclusion in *Dodsley*.

[47] The respondent argued that *Costello* stood for the proposition that if no trades actually occurred, there was no trade in the form of an act in furtherance of a trade. That, however, is a misreading of *Costello*. In *Costello* there were actual trades that were anticipated when acts of Costello occurred and those trades ultimately were actually carried out by registered persons or by persons exempt from registration. *Costello* held that if the acts of Costello were acts in furtherance of those trades (which, incidentally, the Commission found them not to be) then those acts in furtherance of the exempt trades, or of trades for which registration was not required, would themselves have been exempt.

[48] In *Costello*, the Commission distinguished between actual trades that had happened and acts by Costello that might or might not be acts in furtherance of those actual trades. The Commission stated at paragraph 47:

> There is no bright line separating acts, solicitations and conduct directly and indirectly in furtherance of a trade from acts, solicitations and conduct not in furtherance of a trade. Whether a particular act is in furtherance of an actual trade is a question of fact that must be answered in the circumstances of each case. A useful guide is whether the activity in question had a sufficiently proximate connection to an actual trade.

[49] The Commission used the term "actual trade" in *Costello* because the Commission was dealing with actual trades by other parties and actions by Costello that may or may not have been in furtherance of those actual trades. In the case at hand the activities of First Federal and Friesner, amounting to the offering of investment contracts, were acts in furtherance of entering into those investment contracts. There is a direct proximate connection between the offering and any trade that was anticipated as a result of those solicitations.

[50] It is nonsensical to deem an act in furtherance of a trade only to exist, as a trade within the extended meaning of paragraph (d) of the definition in the Act, if as and when an ultimate, actual trade occurs. Rather, we believe the intention of the Act is that the act in furtherance of a trade becomes a trade within the extended meaning at the time the act occurs. We have no difficulty in concluding that the precedents were correct in treating an act in furtherance of a trade as a trade regardless of whether the anticipated trade actually occurred.

[51] In summary, *Costello* does not stand for the proposition that there never could be an act in furtherance of a trade where the trade anticipated by the act in furtherance does not ultimately occur. Such a reading down of *Costello* would artificially limit the effectiveness and purpose of the Act: to regulate those who trade, or purport to trade, in securities.

D. Exemptions

[52] The respondents argued that there was no evidence that any trade which was anticipated or which might have taken place would not have been exempt under the Act. However, as this Commission observed in *Lydia Diamond Exploration of Canada Ltd., Jurgen Prince von Anhalt and Emilia Prince von Anhalt* 2003, 26 O.S.C.B. 2511 at paragraphs 83 and 84, once it is established that a respondent has engaged in an activity for which registration is required and for which a respondent argues that it had an exemption, the onus is on the respondent to prove facts establishing the availability of the exemption.

[53] The Trading Program required the investor to deposit US$10 million with the investor's own Bank to be used as capital by the Bank in trading for the investor in accordance with the trading strategy of First Federal. It is not clear how this would be done.

[54] Although the investor was required to deposit a minimum of US$10 million to participate in the Trading Program, this sum was the investor's capital. There was no evidence, apart from fees payable, that the investor had to pay any purchase price or other cost for the Trading Program.

[55] Sophisticated investors are not approached with investment opportunities through the Internet. Relatively unsophisticated retail investors are the target of solicitations through the Internet. The reach of the Internet is far and wide. We have no reason to believe that First Federal intended only to attract the interest of accredited investors with respect to whom there may exist exemptions from the registration and prospectus requirements of Ontario securities law. Indeed, an examination of the material that was contained on the web site refers to unsophisticated people and retail investors that are unaware of how the bank market operates.

E. Non Compliance with Ontario Securities Law

[56] Section 122(3) of the Act deals with a director or officer of a company who authorizes, permits or acquiesces in the commission of an offence under the Act. It does not require that a charge be laid or a finding of guilt be made against the company prior to its application.

[57] We are not dealing with allegations under section 122 of the Act. We are dealing with the question of whether it is in the public interest to issue one or more orders under sections 127 and 127.1 of the Act with respect to the respondents. While we will not be making a finding whether an

offence has occurred contrary to section 122 of the Act, we are entitled to make a finding of whether or not Ontario securities law has been complied with for purposes of section 127.

[58] Although a breach of the Act is not a precondition to any order under section 127, certain orders may be made in cases where the Commission is satisfied that Ontario securities law has not been complied with.

[59] Friesner was the president, the chief executive officer and a director of First Federal. He was the only contact person listed on the web site and the only person to contact Mr. Samson on behalf of First Federal. No evidence was led by Friesner to suggest others were responsible for the web site or for First Federal's decisions. Friesner authorized and signed the letter to Mr. Samson which promoted the Trading Program and solicited Mr. Samson's participation in an investment contract contrary to the provisions of Ontario securities law. He referred to the actor in the letter as "I" and not "First Federal" in some instances. There is reason to conclude that First Federal may have been merely an alter ego for Friesner.

[60] The evidence clearly establishes that Friesner was acting as the directing officer and agent of First Federal in respect of the conduct impugned in this matter. There is no doubt in our minds that in determining whether to issue one or more orders under section 127 and section 127.1 and the extent of the orders, it is appropriate to take into account the conduct of Friesner as well as First Federal.

F. Advising

[61] First Federal held itself out as being in the business of advising as evidenced by several statements on its web site.

[62] Posting information on a web site, including the holding out of being in the business of advising, solicitations, and offerings of securities, is not an isolated act, because the posting is available to persons who can access the Internet and is available during the time the information remains posted.

[63] When it comes to determine whether or not the respondents held out that First Federal was in the business of advising, the assets and securities that are relevant are more than the Trading Program and other investments provided by First Federal. They also include all the other securities such as public and private debt that are referred to in the documentation and promotional literature contained on the web site.

X. Sanctions

[64] Friesner has a criminal record. In 1966 he received a suspended sentence and nine months probation for possession of property obtained by crime. He failed to comply with probation. In 1969 he was sentenced to two years less a day for uttering a forged document in attempted fraud. He was convicted of other offences, namely common assault, arson, assault causing bodily harm, theft over $200, on various occasions up to 1986.

[65] In 1993 he was indicted in the United States District Court for the District of Oklahoma on 21 counts relating to advising a scheme and artifice to defraud, and to obtain money by means of

false and fraudulent pretences, representations and promises, from various individuals and businesses who were seeking multi-million dollar commercial loans.

[66] It was part of the scheme and artifice to defraud that Friesner would represent that he could obtain for the individuals and businesses sufficient collateral for them to obtain multi-million dollar loans sought by them. Friesner would represent to clients that for performing his services he would not require an advance fee but instead would obtain his commission when the loan was closed by charging a fee of 1/8 of one per cent of the completed loan amount. Furthermore, Friesner would falsely represent to clients that some international bank or financial institution (which varied from victim to victim) had been contacted and was ready to provide the letter of credit or other collateral necessary for clients' multi-million dollar loans, but that the bank or financial institution required a fee – usually US$250,000 – before the confirmation of the letter of credit or other collateral could be provided by the bank.

[67] In 1994, based on the convictions, Friesner was sentenced to seven years imprisonment and ordered to pay a restitution sum based on his ability to pay but not in the full amount of the loss of clients, estimated to be approximately US$1,250,000.

[68] While the scheme and artifice relating to the 21 counts for which Friesner was indicted was not identical to the scheme evident in the documentation relating to the Trading Program, there were some similarities.

[69] In making an order in the public interest under section 127 of the Act, the Commission's jurisdiction is to be exercised in a protective and preventative manner. As this Commission stated in *Re Mithras Management Ltd.* (1990), 13 O.S.C.B. 1600 at 1610-1611:

> [u]nder sections 26, 123, and 124 of the Act, the role of this Commission is to protect the public interest by removing from the capital market – wholly or partially, permanently or temporarily, as the circumstances may warrant – those who's conduct in the past leads us to conclude that their conduct in the future may well be detrimental to the integrity of the 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.

[70] This view was endorsed by the Supreme Court of Canada in *Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission),* (2001) 2 S.C.R. 132, 199 D.L.R. (4th)at 59 at paragraph 43:

> Rather, the purpose of an order under s. 127 is to restrain future conduct that is likely to be prejudicial to the public interest in fair and efficient capital markets. The role of the OSC under s. 127 is to protect the public interest by removing from the capital markets those whose past conduct is so abusive as to warrant apprehension of future conduct detrimental to

the integrity of the capital markets: *Re Mithras Management Ltd.* (1990), 13 O.S.C.B

[71] A respondent's past criminal conduct may be an important indicator of the need for protective action. In particular, criminal conduct in securities-related matters may call for "a vigorous package of preventative sanctions": *Re Banks* (2003), 26 O.S.C.B. 3377 at 3387 and *Re Kinlin* (2000), 23 O.S.C.B. 6535.

[72] Where impugned conduct involves actions undertaken as a director or officer of an issuer, sanctions removing a respondent from these roles will often be appropriate: *Banks*. Respondents who persist in trading and advising without registration even after contact by the staff of the Commission raise a public interest concern and require preventative sanctions: *Etherington*.

[73] There is nothing redeeming in the conduct of the respondents. We found no mitigating factors with respect to the conduct and attitude of the respondents. The fact that we had no evidence of actual loss by investors in respect of the Trading Program and other investments referred to in the materials before us did not impress us.

[74] The agreed statement of facts and the materials before us which were taken largely from First Federal's web site and correspondence between First Federal and Mr. Samson do no disclose all of the facts that undoubtedly would be available if actual investments by investors had been completed. We suspect, but have no evidence before us, that when implemented, there could occur a sting to the investor in implementing the scheme evidenced in the documentation similar to the methodology employed by Friesner in the schemes for which he was convicted in Oklahoma.

[75] Nevertheless, the documentation in the matter before us, on its own, contains sufficient statements of hyperbole, outrageous promises, and misleading statements to satisfy us, as a matter of fact, that the proposed Trading Program was not *bona fide*. On the face of the documents, the investment proposals were not credible. The amounts of money one supposedly could make by putting up money are astronomical by reference to any kind of historical returns that any asset class has ever been able to generate. It would have been helpful to have examples from the respondents where the scheme had been in operation at earlier times and who the parties were to lend some credibility to the Trading Program. The documents raise a lot of concerns. Those concerns were not answered by the respondents and nothing we heard explained away or showed us that we were wrong or somehow misinterpreted what the documents purported.

[76] Much of the documentation packaged by First Federal included the names of reputable Canadian financial institutions. There was no evidence that those institutions consented to participate with First Federal or Friesner in the Trading Program. Indeed, based on our experience with the Canadian capital markets, we would be concerned to learn that this information was given with the informed consent of those institutions.

[77] Where disreputable securities-related activities have occurred in the past, and there is reason to believe, based on past conduct, that a respondent might attempt to pursue highly questionable securities-related activities in the future, there is no reason why there should be any carve-outs from a cease trade order. To this effect, we note that investors (including Ontario investors) suffered loss as the result of securities-related fraud evidenced in Friesner's past convictions.

[78] Accordingly, we determine that it is in the public interest to order that:

1. First Federal and Friesner cease trading in securities permanently;

2. Friesner resign all positions that he holds as officer or director of an issuer; and

3. Friesner be prohibited from becoming or acting as an officer or director of an issuer in the future.

[79] We have not specifically ordered a reprimand of the respondents. In our view, the severity of the sanctions we are ordering speak for themselves and express the view of the Commission that the conduct of the respondents was reprehensible.

XI. Costs

[80] We are satisfied that First Federal and Friesner have not complied with Ontario securities law in that the provisions of section 25 of the Act requiring registration to advise and to trade securities, and section 63 with respect to prospectuses have not been complied with. In addition, we are satisfied that Friesner authorized, permitted and acquiesced in the non-compliance by First Federal with Ontario securities law. Indeed, it was Friesner's conduct that caused the non-compliance.

[81] Accordingly, we determine that it is in the public interest to order that the respondents pay the costs of the Commission's investigation and hearing with respect to this matter.

[82] Staff presented us with a bill of costs from April 1, 2000 to May 26, 2003. No claim for costs was made from the period starting September 6, 1999, when investigating staff of the Commission opened the file in this matter and up to April 1, 2000. The bill of costs only runs to May 26, 2003 and does not include any costs incurred for the days leading up to and the day of this hearing. Those three days would have been intense with respect to time and effort and expense on the part of staff in the preparation and conduct of the hearing.

[83] Staff applied to the calculation of costs, the methodology applied by staff in *Re Donnini* (2002), 25 O.S.C.B. 6225. While the Ontario Divisional Court sent the question of costs in *Donnini* back for consideration by the Commission, it did not criticize the methodology adopted in *Donnini.* There is a suggestion that additional evidence and procedures should be available to clarify the amount of costs in that case.

[84] We were not provided with a detailed breakdown of the time of the three Staff lawyers who had carriage of this case. We believe that such information would be helpful in satisfying ourselves as to the proper amount of costs incurred by the Commission in this matter.

[85] We were advised that three lawyers worked on the file individually and sequentially and there was not much double-teaming other than some hand-off instructions when a new person came on the file. Further information on this would be helpful.

[86] The file passed from Ms. Oseni, who left the litigation branch of the Commission, to Mr. Guttensohn, to Ms. Wootton, who left on maternity leave, and then to Ms. Clark, who joined the staff of the Commission in 2002. There is no claim for Mr. Guttensohn's time as he maintained a "watching brief" on the file.

[87] Subsequent to the hearing, counsel for the respondent requested that, if the hearing panel is inclined to make an order for costs against one or more of the respondents pursuant to section 127.1 of the Act, counsel be given the opportunity to obtain further information and make further submissions in light of *Donnini*.

[88] We agree with the request. Accordingly, we invite the parties to arrange for the exchange of information and invite counsel to arrange a costs hearing through the Secretary.

Dated at Toronto this 3rd day of February, 2004.

"Paul M. Moore"
_____
Paul M. Moore, Vice-Chair

"M. Theresa McLeod"
_____
M. Theresa McLeod, Commissioner

"Harold P. Hands"

_____
Harold P. Hands, Commissioner