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

AND

IN THE MATTER OF
LEHMAN COHORT GLOBAL GROUP INC., ANTON SCHNEDL,
RICHARD UNZER, ALEXANDER GRUNDMANN and HENRY HEHLSINGER

REASONS AND DECISION

Hearing:	January 25 and 26, 2010	
Decision:	July 28, 2010	
Panel:	James E. A. Turner	- Vice-Chair and Chair of the Panel
	Carol S. Perry	- Commissioner
	Sinan O. Akdeniz	- Commissioner
Counsel:	Hugh Craig	- For Staff of the Ontario Securities Commission
		- No one appeared for any of the Respondents.

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REASONS AND DECISION

I. OVERVIEW

[1] This was a hearing before the Ontario Securities Commission (the "**Commission**") to consider whether Lehman Cohort Global Group Inc. ("**Lehman**"), Anton Schnedl ("**Schnedl**"), Richard Unzer ("**Unzer**"), Alexander Grundmann ("**Grundmann**") and Heinrich "Henry" Hehlsinger ("**Hehlsinger**") (collectively referred to as the "**Respondents**") breached sections 25(1)(a) and 126.1(b) of the *Securities Act*, R.S.O. 1990, c. S.5, as amended (the "**Act**") and acted contrary to the public interest.

[2] A temporary cease trade order was issued in this matter on May 20, 2009 and a Notice of Hearing and Statement of Allegations were issued on August 14, 2009. Three Commission orders (dated June 4, 2009, July 21, 2009 and August 19, 2009) were issued that extended the temporary cease trade order until the completion of the hearing on the merits. A hearing on the merits was held on January 25 and 26, 2010.

[3] It is alleged by Staff of the Commission ("**Staff**") in the Statement of Allegations that the Respondents solicited European investors to invest in a fraudulent investment scheme offered by Lehman. By doing so, it is alleged that the Respondents breached Ontario securities law by:

(a) trading in securities without registration or an exemption from registration contrary to subsection 25(1) of the Act. Specifically, those breaches include:

(1) soliciting investors to purchase oil futures, a security within the meaning of clause (p) of the definition of "security" in subsection 1(1) of the Act;

(2) soliciting investors to purchase foreign treasury bonds, a security within the meaning of clause (e) of the definition of "security" in subsection 1(1) of the Act; and

(b) engaging in acts of fraud, contrary to section 126.1 of the Act.

It is also alleged that the Respondents' conduct was contrary to the public interest.

[4] On January 25 and 26, 2010, we heard evidence and submissions on the merits in this matter. None of the Respondents was present or represented by legal counsel. Five witnesses were called to testify: a husband and wife who are residents of Austria (the "**Austrian Investors**") whose testimony was given by video conference, Gale Solnik, the sole director of Lehman and a former employee of a Toronto law firm that advised Schnedl in connection with the incorporation of Lehman (the "**Canadian Director**"), and two Staff investigators, Donald Panchuk and Joanne Ramirez. Staff submitted to us a hearing brief and seven evidence summaries based on the hearing brief. The Austrian Investors retained a private investigator to investigate Lehman and Schnedl and that investigator travelled to Toronto and Hong Kong in connection with the investigation. Some of the testimony of the Austrian Investors was based on the report of the private investigator.

[5] These are our reasons and decision in this matter.

II. THE RESPONDENTS

[6] Lehman was incorporated under the *Business Corporations Act* (Ontario), R.S.O. 1990, c. B.16 on August 16, 2007. The address of Lehman's registered office and address for service is 100 Upper Madison Avenue, Suite 1907, Toronto, Ontario. That is the address of the law firm that formerly employed the Canadian Director.

[7] Lehman has an Internet Web site at http://www.lehmangroup.net (the "**Lehman Web site**"). The Lehman Web site describes the investment services Lehman provides and refers to its office locations in Toronto, Los Angeles and the Commonwealth of Dominica.

[8] The Lehman Web site identifies Lehman's head office as being located at 100 King Street West, 37th Floor, Toronto, Ontario. Staff submitted evidence showing that Lehman's head office is a business services centre that provides "virtual offices" to customers (see paragraphs 53 and 54 of these reasons). We will refer to Lehman's head office in these reasons as the "**Toronto Virtual Office**".

[9] Through the Lehman Web site, Lehman purports to offer capital markets and investment advisory services, wealth management, investment management and related products and services on a global basis, including securities origination, brokerage, and dealer and related activities in equities, futures, fixed income, mutual funds, commodities, swaps, currencies, options, and other derivatives.

[10] Evidence was submitted that also referred to "Lehman Advocate & Co." and "Lehman Limited". It is not clear whether these are mistaken references to Lehman, whether they are separate entities or whether, in fact, they exist.

[11] Schnedl arranged for the incorporation of Lehman and is Lehman's President, Treasurer and Secretary and appears to be Lehman's only shareholder. Schnedl signed an indemnity in favour of the Canadian Director for acting as a director of Lehman. The Austrian Investors testified that, based on the investigation report referred to in paragraph 4 of these reasons, they believe that Schnedl and Unzer were "in charge" of Lehman.

[12] Schnedl opened bank accounts in Toronto on behalf of Lehman and is the sole signing officer for those accounts. Schnedl also signed the services agreement for the Toronto Virtual Office and he is listed as the administrative contact for the Lehman Web site with an address in Spain. Schnedl appears to reside in Spain.

[13] There is evidence that Unzer and Grundmann held themselves out as representatives of Lehman.

[14] Hehlsinger also appears to be a representative of Lehman. One of the Austrian Investors testified that Hehlsinger informed her that he was really Schnedl and that "Hehlsinger" is an alias used by him. For purposes of these reasons, we will treat Hehlsinger as being the same person as Schnedl.

[15] None of the Respondents is, or has ever been, registered in any capacity with the Commission.

[16] None of the individual Respondents appears to reside in Canada. Based on the evidence submitted to us, none of them, other than Schnedl, appears to have ever been in Ontario in connection with the conduct that is the subject matter of this proceeding. Schnedl came to Toronto in 2007 to arrange the incorporation of Lehman, to establish the Toronto Virtual Office and to open the Lehman Toronto bank accounts.

III. PRELIMINARY ISSUES

A. The Failure of the Respondents to Appear at the Hearing

[17] As noted above, none of the Respondents appeared or was represented at the hearing on the merits. Subsection 7(1) of the *Statutory Powers Procedure Act*, R.S.O. 1990, c. S.22, as amended (the "**SPPA**") provides that a tribunal may proceed in the absence of a party when that party has been given adequate notice. That section provides as follows:

> Where notice of an oral hearing has been given to a party to a proceeding in accordance with this Act and the party does not attend at the hearing; the tribunal may proceed in the absence of the party and the party is not entitled to any further notice in the proceeding.

[18] We note the following passage from *Administrative Law in Canada*:

> Where a party who has been given proper notice fails to respond or attend, the tribunal may proceed in the party's absence and the party is not entitled to further notice. All that the tribunal need establish, before proceeding in the absence of the party, is that the party was given notice of the date and place of the hearing. The tribunal need not investigate the reasons for the party's absence.
>
> (Sara Blake, *Administrative Law in Canada*, 4th ed. (Markham, Ont.: LexisNexis Butterworths, 2006) at p. 35)

[19] Staff submitted evidence in the form of an Affidavit of Service dated January 25, 2010 of Kathleen McMillan, an employee of the Commission, to establish that Staff took reasonable steps to give the Respondents notice of this proceeding and to serve the Respondents with the order dated August 19, 2009 setting this proceeding down for a hearing on January 25, 2010. Staff received no response from the Respondents using the known e-mail addresses for them and documents sent to the Toronto Virtual Office were returned to Staff. One of the Austrian Investors testified that Schnedl stated in a telephone conversation that he was aware of this proceeding.

[20] We are satisfied that Staff gave adequate notice of this proceeding to the Respondents and that we are entitled to proceed in their absence in accordance with subsection 7(1) of the SPPA.

B. The Use of Hearsay Evidence

[21] A significant portion of the evidence relied on by Staff in this proceeding is hearsay evidence.

[22] Subsection 15(1) of the SPPA provides as follows:

> Subject to subsections (2) and (3), a tribunal may admit as evidence at a hearing, whether or not given or proven under oath or affirmation or admissible as evidence in a court,
>
> (a) any oral testimony; and
>
> (b) any document or other thing,
>
> relevant to the subject-matter of the proceeding and may act on such evidence, but the tribunal may exclude anything unduly repetitious.

[23] In *The Law of Evidence in Canada*, it is stated that:

> In proceedings before most administrative tribunals and labour arbitration boards, hearsay evidence is freely admissible and its weight is a matter for the tribunal or board to decide, unless its receipt would amount to a clear denial of natural justice. So long as such hearsay evidence is relevant it can serve as the basis for the decision, whether or not it is supported by other evidence which would be admissible in a court of law.
>
> (John Sopinka, Sidney N. Lederman & Alan W. Bryant, *The Law of Evidence in Canada*, 2d ed. (Markham, Ont.: LexisNexis Butterworths, 1999) at p. 308)

[24] Although hearsay evidence is admissible under the SPPA, the weight to be given to that evidence must be determined by the panel. Care must be taken to avoid placing undue reliance on uncorroborated evidence that lacks sufficient indicia of reliability (*Starson v. Swayze*, [2003] 1 S.C.R. 722 at para. 115).

[25] There was documentary evidence introduced by Staff that corroborated or was consistent with the hearsay evidence given by the Austrian Investors and the Staff investigators. That documentary evidence included copies of e-mails and faxes that appear to have been sent by investors to the Respondents, account statements made available to investors, bank records and evidence of wire transfers of funds and legal documents to which Lehman appeared to be a party. The totality of the evidence presented in this matter is corroborative and consistent.

[26] One of the concerns with respect to the introduction of hearsay evidence is that it may infringe on the rights of a party to cross-examine a witness or to introduce contradictory evidence. This engages the requirement for procedural fairness. In this case, none of the Respondents appeared, was represented or present to object to the use of the hearsay evidence, to cross-examine on it or to introduce contradictory evidence of their own. As a result, the

Respondents have waived their right to do so. In this respect, it was stated in *Violette v. New Brunswick Dental Society*, [2004] 267 N.B.R. (2d) 205 (C.A.) at paragraph 80 that:

> […] I am of the view that the appellant's informed decision not to participate in the hearing before the Discipline Committee constitutes abandonment, leading to waiver of possible breaches of the rules of procedural fairness. This conclusion is hardly surprising. He who seeks fairness must act fairly by raising timely objections. This necessarily requires the affected party's participation.

While that case did not involve an unrepresented respondent, in our view, the same principle applies here.

[27] Accordingly, we concluded that we would admit the hearsay evidence tendered by Staff, subject to our consideration of the weight to be given that evidence.

C. The Appropriate Standard of Proof

[28] We must also consider the appropriate standard of proof applicable in a Commission proceeding.

[29] In *F.H. v. McDougall*, [2008] 3 S.C.R. 41, the Supreme Court of Canada stated at paragraph 49 that:

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

At paragraph 46, the Court stated that:

> […] evidence must always be sufficiently clear, convincing and cogent to satisfy the balance of probabilities test. But again, there is no objective standard to measure sufficiency… If a responsible judge finds for the plaintiff, it must be accepted that the evidence was sufficiently clear, convincing and cogent to that judge that the plaintiff satisfied the balance of probabilities test.

[30] Accordingly, we will decide this matter on the balance of probabilities. In doing so, we must be satisfied that there is sufficient clear, convincing and cogent evidence to support our findings. While a significant portion of the evidence before us is hearsay evidence, that evidence is corroborated by and consistent with the other evidence submitted to us. Overall, we believe that the evidence before us is clear, convincing and cogent and provides a sufficient basis for our conclusions set out below. We are satisfied that the acts, events and conduct described in these reasons are more likely than not to have occurred.

IV. ISSUES AND EVIDENCE

A. Issues

[31] The issues we must decide in this matter are:

(a) Did the Respondents trade in securities in breach of subsection 25(1)(a) of the Act?

(b) Did the Respondents breach section 126.1(b) of the Act?

(c) Did the Respondents act in a manner that was contrary to the public interest?

B. Investors

[32] The only investors Staff called as witnesses were the Austrian Investors. The Staff investigators stated, however, that they were aware of other investors solicited with respect to the investment scheme and Staff introduced some evidence of the investments made by those other investors. To protect the privacy of the investors, we will not use their names in these reasons.

C. The Investment Scheme

[33] This proceeding involves an investment scheme that was offered by Lehman to potential investors through telephone solicitations. Individuals were contacted by telephone by representatives of Lehman. It appears that the phone calls were "cold" calls made to individuals who had no prior knowledge of or relationship with Lehman. During the telephone conversations, representatives of Lehman would propose investments in oil futures and/or foreign treasury bonds.

[34] If an investor agreed to invest, he or she would fill out an application form and Lehman would purport to open a managed account for the investor. The actual trading and the form of the investments to be purchased on behalf of investors were to be at the sole discretion of Lehman. Investors were told, however, that the investments would be made in oil futures and/or foreign treasury bonds.

[35] The Austrian Investors were solicited by telephone by Schnedl, Unzer and Grundmann to invest in the scheme. After they had done so, and after they had purportedly lost all of their investment, they were harassed by Schnedl in sometimes abusive telephone calls. All of the communications with the Austrian Investors were in the German language.

[36] In order to fund their investments, investors were given international wire instructions for Lehman's Toronto bank accounts. Lehman had three bank accounts at TD Canada Trust in Toronto, one denominated in each of Canadian dollars (the "**Lehman CAD account**"), U.S. dollars (the "**Lehman USD account**") and Euros (the **"Lehman Euro account**"). The accounts were opened by Schnedl on behalf of Lehman on November 13, 2007. Schnedl had sole signing authority and control over each of the bank accounts, although the account opening documentation for the Lehman Euro account could not be produced by the bank.

[37] The Staff investigators testified that the Austrian Investors, and other individuals who appeared to be investors participating in the investment scheme, wired funds as follows:

(a) Investor 1 wired (from a bank account in Germany) an amount in Euros that was credited as $9,496 to the Lehman CAD account;

(b) Investor 2 wired (from a bank account in Germany) an amount in Euros that was credited as $6,418 to the Lehman CAD account;

(c) Investor 3 wired (from a bank account in Germany) US $2,561 to the Lehman USD account; Investor 3 also wired an additional US $966 to the Lehman USD account from the same bank account in Germany;

(d) Investor 4 wired (from a bank account in Germany) US $84,990 to the Lehman USD account; Investor 4 also wired an additional €4,993 to the Lehman Euro account from the same bank account in Germany;

(e) Investor 5 wired (from a bank account in Italy) US $4,961 to the Lehman USD account;

(f) Investor 6 wired (from a bank account in Germany) €24,993 to the Lehman Euro account;

(g) Investor 7 wired (from a bank account in Switzerland) €4,983 to the Lehman Euro account;

(h) Investor 8 wired (from a bank account in Germany) €5,393 to the Lehman Euro account;

(i) Investor 9 wired (from a bank account in Germany) €4,266 to the Lehman Euro account;

(j) Investor 10 wired (from a bank account in Germany) €4,993 to the Lehman Euro account; and

(k) The Austrian Investors wired (from a bank account in Austria) €10,543 to the Lehman Euro account and subsequently sent additional wires in the amounts of €149,592, €25,923 and €34,903 from the same bank account in Austria.

All of these amounts are net of banking fees and rounded down.

[38] Lehman prepared client account statements that purported to show for each client all account activity and account balances. The statements were made available to clients on a password-protected section of the Lehman Web site. It appears that the account statements were a sham and did not reflect actual investments or returns.

[39] The Austrian Investors testified that their account statements initially showed significant profits but, beginning in July 2008, the account began to show losses. As of August 2, 2008, the account statements showed that the Austrian Investors had lost all of their invested money and owed Lehman US $11,198. At that time, Schnedl (using the Hehlsinger alias) contacted the Austrian Investors and suggested that if they sent the money "owed," their losses could be recouped.

[40] No trade confirmations were ever sent to investors. Notwithstanding the investments shown in the client accounts, it appears that no oil futures, treasury bonds or any other securities were ever purchased by Lehman on behalf of investors.

[41] Evidence was presented to us showing wire transfers from Lehman's Toronto bank accounts to bank accounts in Schnedl's name at Spanish banks. Amounts of $8,265, US $37,757, and €251,654 were transferred from the Lehman accounts to those accounts at banks in the Province of Málaga, Spain. The Austrian Investors testified that they believe that Schnedl resides there.

[42] In a number of cases, wire transfers to Schnedl's personal bank accounts were made within days of the receipt of wire transfers by investors to Lehman's bank accounts. A number of the amounts transferred to Schnedl's personal bank accounts were very close to the amounts wired by investors to Lehman. For example, Lehman received €24,993 from Investor 6 on December 12, 2007 and Schnedl transferred €24,920 to one of his personal bank accounts on December 18, 2007. In another case, Lehman received €4,266 from Investor 9 on February 12, 2008 and Schnedl transferred €4,180 to one of his personal bank accounts on February 20, 2008.

[43] Two transfers in the amounts of US $10,039 and €20,000 were made from Lehman's bank accounts to an Emilie Tunzer in Vienna, Austria. The Austrian Investors believe that Emilie Tunzer is Schnedl's mother.

[44] Based on the evidence, we conclude that Schnedl was the ultimate recipient or beneficiary of a substantial portion of the funds wired by investors to Lehman.

[45] It appears that no money was ever returned to investors. The Austrian Investors made a total investment of approximately €221,000 and have made repeated demands for the return of their funds but have received no response. The Austrian Investors testified that they have been left almost destitute as a result.

[46] Staff submitted a copy of the Austrian Investors' managed account application, which contains a choice of law clause stating that the agreement is governed by the laws of Toronto, Canada. The clause reads as follows (translated from the German):

> This contract, the associated rights and obligations of the parties, and any legal and administrative act or procedure directly or indirectly related to the transactions considered hereunder, whether initiated and/or caused by the Client or Lehman, shall be governed, interpreted and asserted in reference to the laws of Toronto, Canada.

One can certainly argue that, by including that provision in the application, Lehman made itself subject to the jurisdiction of Ontario law.

[47] It was not submitted by Staff, nor was there any evidence before us, that indicated that the Canadian Director was ever personally involved in the investment scheme.

D. The MediTerra Investment Scheme

[48] In a letter dated August 24, 2009, provided to Staff by the Swiss Financial Market Supervisory Authority ("**FINMA**"), Investor 7 stated that in April 2007 he invested CHF 20,000 with "MediTerra Investments Inc." ("**MediTerra**") in Germany. Shortly after making that investment, he received a call from Unzer, who claimed to be the chairman of MediTerra. Unzer solicited a subscription for securities of MediTerra.

[49] The material provided to Staff by FINMA included a copy of a subscription agreement purported to have been signed by Investor 7 on December 3, 2007 for the purchase of 5,000 Class A common shares of MediTerra, with a value of €1 each. MediTerra's office was shown on the subscription agreement to be 391 N.W. 179th Avenue, Aloha, Oregon 87006, USA. Investor 7 wired €4,983 to the Lehman Euro account to pay for his investment in MediTerra. The agreement entered into by Investor 7 was stated to be between Investor 7 and "Lehman Advocate & Co.," which showed its Head Office as 100 King Street West, 37th Floor, Toronto, Ontario, (the address of the Toronto Virtual Office).

[50] Unzer represented to Investor 7 that "Leman Advocats" in Toronto was the trustee of MediTerra. Investor 7 had never previously heard of Lehman, "Leman Advocats," or "Lehman Advocate & Co.". Investor 7 stated in the letter that "[it] was always a mystery to me why I suddenly was in contact with a company [called] Leman Advocats. I was told that Leman represented the interests of MediTerra."

[51] Investor 7 also stated in the letter that shortly after submitting the subscription agreement, Unzer called him and solicited a further investment in MediTerra, claiming that it would be a good time to invest since MediTerra would soon be listed on a stock exchange. Investor 7 declined to invest more funds as he wanted to wait for the listing of the shares on the exchange to ensure that "everything was going smoothly" before increasing his investment. Shortly afterwards, Unzer again called Investor 7 explaining that difficulties had arisen in the share subscription and that the shares could not be issued. Investor 7 then asked for his money back. In response, Unzer solicited Investor 7 to invest in other different investments. Investor 7 declined, and as of the date of the letter, he had not heard from Unzer or Lehman or received his money back.

[52] The MediTerra investment scheme is connected to Lehman through the use of the Lehman Euro account, the Toronto Virtual Office, Lehman's logo on the subscription form and the involvement of Unzer.

E. The Toronto Virtual Office

[53] The Austrian Investors understood that Lehman was carrying on business in Toronto and they thought they were dealing with a company and individuals located in Canada. The Toronto

Virtual Office appears to have been established for the sole purpose of misleading investors into believing that was the case.

[54] The Toronto Virtual Office provided Lehman with a telephone answering service, a mailing address and, if requested, conference facilities for meetings. A person calling a representative of Lehman would call the telephone number of the Toronto Virtual Office, which would be answered using Lehman's name, and a message could be left. The Austrian Investors would fax documents and correspondence to Lehman at the address of the Toronto Virtual Office. Those documents would then be forwarded to Lehman. The various documents prepared by Lehman and sent to investors identified Lehman using the Toronto Virtual Office address or referred to Lehman in Toronto. It was not apparent to investors that they were dealing with a virtual office.

[55] The Toronto Virtual Office was arranged by Schnedl who paid the service fees for the office by wire transfers from the Lehman CAD account and Lehman USD account.

[56] There was evidence that Lehman also has virtual offices or mail drops in Los Angeles, California and the Commonwealth of Dominica.

V. ANALYSIS

A. Did the Respondents Breach Subsection 25(1)(a) of the Act?

i. The Applicable Law

[57] As of the date of the conduct that is the subject matter of this proceeding, subsection 25(1)(a)[1] of the Act provided as follows:

> **Registration for trading** - 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…
>
> and the registration has been made in accordance with Ontario securities law and the person or company has received written notice of the registration from the Director and, where the registration is subject to terms and conditions, the person or company complies with such terms and conditions.

[58] Subsection 1(1) of the Act defines a "trade" as including:

> > (a) any sale or disposition of a security for valuable consideration, whether the terms of payment be on margin, instalment or otherwise, but does not include a purchase of a security or, except as provided in clause (d), a

[1] In September 2009, subsection 25(1)(a) of the Act was repealed and replaced by the current subsection, which contains a similar prohibition.

> transfer, pledge or encumbrance of securities for the purpose of giving collateral for a debt made in good faith,
>
> …
>
> (e) any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of any of the foregoing.

[59] We must determine whether the Respondents traded in securities for purposes of subsection 25(1)(a) of the Act. The only real issue is whether the Respondents traded in a security in Ontario. It is sufficient for that purpose if a person engages in Ontario in any acts in furtherance of a trade in a security.

[60] In *Gregory & Co.*, the Supreme Court of Canada concluded that the accused was subject to the securities law of Quebec, noting several factors that indicated a nexus to Quebec: the address and telephone number of the Montreal office were provided in the bulletin distributed to customers (and customers were invited to contact that office), purchasers of securities were solicited by telephone from the head office in Montreal, customers mailed their payments to that office and a bank account was maintained in Montreal (*Gregory & Co. v. Quebec (Securities Commission)*, [1961] S.C.R. 584 ("***Gregory***") at 589-590).

[61] In *Re Allen* (2005), 28 O.S.C.B. 8541 ("***Allen***"), the Commission concluded that sales of securities were made to investors primarily in Alberta but that a "substantial portion of the activities surrounding the sales took place in Ontario." The connecting factors to Ontario included that the issuer and its offices and operations were located in Ontario; the promotional materials and telephone calls originated in Ontario; and the cheques in payment for the securities were sent to Ontario. The Commission cited *Gregory* and held that the Commission "has jurisdiction over a trade in securities, notwithstanding that the purchaser is in a different province, provided that some substantial aspect of the transaction occurred within Ontario" (*Allen, supra,* at paras. 20-21).

[62] In *Re Lett* (2004), 27 O.S.C.B. 3215 ("***Lett***"), the Commission found that the respondents acted in furtherance of trades in securities and that those acts occurred in Ontario, although the trades were not made to investors in Ontario. The Commission stated that:

> [t]he Respondents were all based in the Toronto area, had bank accounts in the Toronto area, carried on business in the Toronto area. Most, if not all, of the documents referred to in the Agreed Statement of Facts and in the six volumes of documents composing the Joint Hearing Brief consist of documents that were either sent by the Respondents from the Toronto area or addressed to them in the Toronto area.
>
> (*Lett, supra,* at para. 66).

[63] The Commission also held in *Lett* that an act in furtherance of a trade is itself a trade for purposes of the Act. Accordingly, if an act in furtherance of a trade in a security occurs in Ontario, even if the actual trade occurs outside Ontario, that act constitutes trading in securities in Ontario for purposes of the Act *(Lett, supra,* at para. 69).

[64] In *Re Sunwide Finance Inc.* (2009), 32 O.S.C.B. 4671 ("***Sunwide***"), the Commission exercised its public interest jurisdiction with respect to certain respondents where the only connection to Ontario was the use of a virtual office in Toronto. *Sunwide* involved an investment scheme designed to lure European investors into wiring money to banks in New York, Hong Kong and Panama. Sunwide was not incorporated under the laws of Ontario, investors did not send their money to Ontario banks and there was no evidence that any of the respondents had been physically in Ontario. The Commission found that the virtual office in Toronto was established for the sole purpose of misleading investors into believing that they were dealing with persons located in Canada. The virtual office provided phone answering services and a mailing address and was used in correspondence with investors to give them the impression they were dealing with a legitimate company in Ontario (*Sunwide, supra,* at paras. 38-42).

[65] In *Re XI Biofuels Inc. et al* (2010), 33 O.S.C.B. 3077, the Commission found that the respondents traded in securities in Ontario where investors were made to believe that they were investing in an Ontario company and investor funds were deposited into a bank account in Ontario (and were almost immediately transferred offshore).

[66] It is not necessary for there to be a completed trade in order for a person to be trading in a security for purposes of the Act (see *Re First Federal Capital (Canada) Corp.* (2004), 27 O.S.C.B. 1603 ("***First Federal***") at paras. 46 and 51 and *Sunwide, supra,* at para. 45). For a particular act to be an act in furtherance of a trade, however, there must be sufficient proximity between the act and an actual or potential trade (see *Re Costello* (2003), 26 O.S.C.B. 1617 at para. 47; *First Federal, supra,* at para. 49; and *Sunwide, supra,* at para. 45).

ii. Analysis

[67] In this case, the Respondents were soliciting and Lehman was purporting to enter into transactions that would have constituted trading in securities for purposes of the Act if they had occurred in Ontario. In analysing the investment scheme from a securities law perspective we recognize that the scheme was a sham and that the Respondents never intended to complete the issue of a security as represented to investors. That does not mean, however, that no trading in a security occurred in Ontario for purposes of the Act.

[68] The acts in furtherance of the investment scheme that occurred in Ontario include the incorporation of Lehman in Ontario for the purpose of carrying out the investment scheme and the establishment of the Toronto Virtual Office and use of that office in dealing with investors. The establishment and use of the Toronto Virtual Office was an integral part of the investment scheme intended to mislead investors into believing they were dealing with a company and individuals located in Ontario. In our view, the establishment and use of the Toronto Virtual Office in this manner had sufficient proximity to the purported trades in securities with investors so as to constitute acts in furtherance of trades in securities that occurred in Ontario. The Commission came to a similar conclusion in *Sunwide*. We note that Lehman's head office was shown as the address of the Toronto Virtual Office and that its registered office was shown as the Toronto address of the law firm that incorporated Lehman.

[69] In addition, and perhaps most important, Lehman established bank accounts in Toronto to which investors wired funds in making their investments. Accordingly, investors completed their

investments and the purported trades in securities by wiring funds to Toronto bank accounts and Lehman received those investor funds in Toronto.

[70] It is also clear that Lehman through its representatives solicited investors to purchase oil futures and foreign treasury bonds, both securities for purposes of the Act.

iii. Conclusions as to Subsection 25(1)(a) of the Act

Lehman

[71] In the circumstances, we have concluded that Lehman engaged in acts in furtherance of trades in securities in Ontario within the meaning of the Act. There is evidence that Lehman:

(a) used the Lehman Web site to advertise its services in furtherance of trading in securities; that Web site referred to Lehman's Toronto Virtual Office address;

(b) established and paid for the services of the Toronto Virtual Office;

(c) communicated with investors using the Toronto Virtual Office;

(d) established Toronto bank accounts that received funds from investors;

(e) solicited trades in securities by telephone through its representatives (although those representatives probably were not in Ontario and those calls probably were not made from Ontario);

(f) entered into account agreements with investors governed by "the laws of Toronto, Canada;" and

(g) used the Lehman Web site to disseminate false account information to investors.

[72] Accordingly, we find that Lehman traded in securities in Ontario within the meaning of the Act. Lehman was not registered in any capacity with the Commission. The onus is on Lehman to prove that an exemption from registration was available. No evidence was submitted to us indicating that any such registration exemption was available. Lehman therefore contravened subsection 25(1)(a) of the Act.

Schnedl

[73] Based on the information and circumstances referred to in paragraphs 11 and 12 of these reasons, we have concluded that Schnedl was a directing mind of Lehman. There is evidence that Schnedl engaged in acts in furtherance of trades in securities in Ontario in that he:

(a) came to Toronto and caused Lehman to be incorporated under the laws of Ontario for purposes of carrying out the investment scheme;

(b) established the Toronto Virtual Office, signed on behalf of Lehman the services agreement establishing that office and paid for those services on behalf of Lehman;

(c) established the Toronto bank accounts used by Lehman to receive investor funds and was sole signing officer on those accounts;

(d) solicited the Austrian Investors by telephone, as a representative of Lehman, to participate in the investment scheme (although those calls were probably not made from Ontario);

(e) acted as the administrative and technical contact for the Lehman Web site used to advertise and solicit trades and to disseminate false account information to investors; and

(f) caused funds to be wired from Lehman's Toronto bank accounts to his personal bank accounts in Spain.

Some of those acts in furtherance of trades were engaged in by Schnedl using the Hehlsinger alias.

[74] Accordingly, we find that Schnedl traded in securities in Ontario within the meaning of the Act. Schnedl was not registered in any capacity with the Commission. The onus is on Schnedl to prove that an exemption from registration was available. No evidence was submitted to us indicating that any such registration exemption was available. Schnedl therefore contravened subsection 25(1)(a) of the Act.

Unzer

[75] Unzer participated in the investment scheme as a representative of Lehman by soliciting investors by telephone to invest in that scheme.

[76] Unzer called the Austrian Investors on numerous occasions to solicit investments in treasury bonds. The phone calls led to the Austrian Investors investing in April and May, 2008. Communications with Unzer included faxes to him at the Toronto Virtual Office.

[77] There is no evidence that Unzer was ever in Ontario or that he telephoned the Austrian Investors from Ontario. There is evidence, however, that he made use of the Toronto Virtual Office in his communications with investors and that he directed investors to make payments to Lehman's Toronto bank accounts. The acts in furtherance of trades carried out by Unzer may have occurred outside Ontario, but those acts in furtherance related to trading in securities that occurred in Ontario for purposes of the Act (see our conclusions in paragraphs 72 and 74 of these reasons). Accordingly, we find that Unzer traded in securities within the meaning of the Act. Unzer was not registered in any capacity with the Commission. The onus is on Unzer to prove that an exemption from registration was available. No evidence was submitted to us indicating that any such registration exemption was available. Unzer therefore contravened subsection 25(1)(a) of the Act.

Grundmann

[78] Grundmann participated in the investment scheme as a representative of Lehman by soliciting investors by telephone to invest in that scheme.

[79] Grundmann first starting calling the Austrian Investors in February 2008. He proposed that the Austrian Investors invest in oil futures because the price of oil was increasing rapidly at the time and because a "5% stop loss" would minimize the risk of such an investment. Grundmann told the Austrian Investors that it would be easy to make up their unrelated prior losses in the stock market by investing in oil futures. The Austrian Investors purported to invest in oil futures with Grundmann in February and May, 2008. Grundmann gave the Austrian Investors international wire instructions and bank account information for the Lehman Toronto bank accounts, a Lehman account application, and a user ID and password for the password-protected section of the Lehman Web site where the Austrian Investors could access their account statements. Communications with Grundmann included faxes to him at the Toronto Virtual Office.

[80] There is no evidence that Grundmann was ever in Ontario or that he telephoned the Austrian Investors from Ontario. There is evidence, however, that he made use of the Toronto Virtual Office in his communications with investors and that he directed the Austrian Investors to make payments to Lehman's Toronto bank accounts. The acts in furtherance of trades carried out by Grundmann may have occurred outside Ontario, but those acts in furtherance related to trading in securities that occurred in Ontario for purposes of the Act (see our conclusions in paragraphs 72 and 74 of these reasons). Accordingly, we find that Grundmann traded in securities within the meaning of the Act. Grundmann was not registered in any capacity with the Commission. The onus is on Grundmann to prove that an exemption from registration was available. No evidence was submitted to us indicating that any such registration exemption was available. Grundmann therefore contravened subsection 25(1)(a) of the Act.

B. Did the Respondents Breach Section 126.1(b) of the Act?

i. Section 126.1(b) of the Act

[81] Section 126.1(b) of the Act provides as follows:

> 126.1 Fraud and market manipulation - A person or company shall not, directly or indirectly, engage or participate in any act, practice or course of conduct relating to securities or derivatives of securities that the person or company knows or reasonably ought to know,
>
> …
>
> (b) perpetrates a fraud on any person or company.

ii. Staff submissions

[82] Staff has alleged that the Respondents engaged or participated in a course of conduct relating to securities that the Respondents knew or reasonably ought to have known perpetrated a fraud on the investors who invested in the investment scheme within the meaning of section 126.1(b) of the Act.

[83] Staff submitted that the evidence of fraudulent conduct by the Respondents meets the legal test for fraud. In particular, Staff submitted that the following evidence supports the conclusion that a fraud occurred here:

(a) the communications by Schnedl, Unzer and Grundmann with the Austrian Investors including the deceitful and false statements made in those communications with respect to the investment scheme;

(b) the wire transfer by investors of funds to the Lehman bank accounts in response to the representations made;

(c) the fact that a substantial portion of investor funds, including a portion of the funds forwarded by the Austrian Investors, were transferred from the Lehman Toronto bank accounts to accounts in Spain in the name of Schnedl;

(d) that €20,000 and US $10,039 were wired from the Lehman Euro account and Lehman USD account, respectively, to Emilie Tunzer, a person who the Austrian Investors believe is the mother of Schnedl;

(e) the Respondents created and distributed through the Lehman Web site account statements reflecting what appear to be fictitious trades in oil futures and fictitious investment returns;

(f) that the initial purchases of securities purportedly made by Lehman for the Austrian Investors and shown in the account statements were made on March 28, 2008 and March 31, 2008, both dates that are prior to the Austrian Investors' funds being credited to the Lehman Euro account;

(g) the Austrian Investors requested trade confirmations from Lehman, but their requests have never been responded to;

(h) there is no evidence (other than the account statements) that investor funds were ever used to invest in oil futures, foreign treasury bonds or other securities; and

(i) requests by the Austrian Investors for withdrawal of funds from their client accounts and for the return of their money have been ignored.

[84] The Austrian Investors' account statements showed an initial profit of $50,735 in one month, followed by the purported complete loss of all the funds. The Austrian Investors were then told that they owed Lehman US $11,198. Staff submits that those circumstances have attributes consistent with a potential fraud.

iii. Analysis

[85] We have concluded above that the Respondents engaged in acts in furtherance of trades in securities in Ontario. Given the nature of those acts, we find that each of the Respondents engaged or participated in an act, practice or course of conduct relating to securities within the

meaning of section 126.1(b) of the Act. We will now address whether those acts and the course of conduct perpetrated a fraud for purposes of section 126.1(b).

a. Fraud

[86] Fraud is "one of the most egregious securities regulatory violations" and is both "an affront to the individual investors directly targeted" and something that "decreases confidence in the fairness and efficiency of the entire capital market system" *(Re Capital Alternatives Inc.*, 2007 ABASC 79 at para. 308, citing D. Johnston & K. D. Rockwell, *Canadian Securities Regulation*, 4th ed., Markham: LexisNexis, 2007 at 420) ("***Capital Alternatives***").

[87] The term fraud is not defined in the Act. Section 126.1(b) was a relatively recent addition to the Act and there has been only one decision of the Commission that has addressed the application of that section (see *Al-Tar Energy Corp. et al* (2010), 33 O.S.C.B. 5535 ("***Al-Tar***"). We can, however, also draw guidance in interpreting section 126.1(b) from the criminal law and decisions of other securities commissions in Canada.

[88] The Supreme Court of Canada discussed the elements necessary to establish fraud in *R. v. Théroux*, [1993] 2 S.C.R. 5 ("***Théroux***"). Justice McLachlin (as she then was) stated that fraud will be established upon proof of a dishonest act, proof of deprivation caused by the dishonest act and proof of the mental element required (*mens rea*).

[89] The first element, the dishonest act, is established by proof of deceit, falsehood or other fraudulent means. As to deceit and falsehood, the Court stated that "all that need be determined is whether the accused, as a matter of fact, represented that a situation was of a certain character, when, in reality, it was not" (*Théroux*, *supra,* at para. 18).

[90] As to "other fraudulent means," the Supreme Court of Canada held that the issue is "determined objectively, by reference to what a reasonable person would consider to be a dishonest act" (*Théroux, supra,* at paras. 17 and 18). The concept is intended to encompass all other means, other than deceit or falsehood, which can be properly characterized as dishonest. "Other fraudulent means" include the non-disclosure of important facts, the unauthorized diversion of funds and the unauthorized arrogation of funds or property (*Théroux, supra*, at para. 18).

[91] The second element of fraud, deprivation, is established by proof of detriment, prejudice or risk of prejudice to the economic interests of the victim caused by the dishonest act (*Théroux, supra*, at paras. 16 and 27). In establishing deprivation, it is not necessary to prove that an accused ultimately profited or received an economic benefit or gain from the conduct or that actual deprivation occurred (*Théroux*, *supra,* at para. 19).

[92] In order to establish fraud, there must also be proof of the necessary mental element (*mens rea*) on the part of the accused. The necessary mental element for establishing fraud was also discussed by the Supreme Court of Canada in *Théroux*. The Court held that the mental element required is established by proof of:

1. subjective knowledge of the prohibited act; and

2. subjective knowledge that the prohibited act could have as a consequence the deprivation of another (which deprivation may consist of knowledge that the victim's pecuniary interests are put at risk).

(*Théroux*, *supra,* at para. 27.)

[93] The Court in *Théroux* observed that subjective intention may be inferred from the acts themselves (*Théroux*, *supra,* at para. 23) and that it is not necessary to show precisely what was in the mind of the accused at the time of the fraudulent acts. The Court stated in *Théroux* that:

> [t]he accused must have subjective awareness, at the very least, that his or her conduct will put the property or economic expectations of others at risk. As noted above, this does not mean that the Crown must provide the trier of fact with a mental snapshot proving exactly what was in the accused's mind at the moment the dishonest act was committed. In certain cases, the inference of subjective knowledge of the risk may be drawn from the facts as the accused believed them to be… [W]here the accused tells a lie knowing others will act on it and thereby puts their property at risk, the inference of subjective knowledge that the property of another would be put at risk is clear.
>
> (*Théroux*, *supra,* at para. 29.)

[94] The Alberta Court of Appeal has held that one can draw an inference as to the requisite mental element for fraud from the totality of the evidence (*Alberta (Securities Commission) v. Brost*, 2008 ABCA 326 ("***Brost C.A.***") at para. 48).

[95] The operative language of section 126.1(b) of the Act is identical to the language of section 57(b) of the British Columbia *Securities Act*, R.S.B.C. 1996, c. 418, as amended (the "**BC Act**"). The British Columbia Court of Appeal addressed the application of section 57(b) of the BC Act in *Anderson v. British Columbia (Securities Commission)*, 2004 BCCA 7 ("***Anderson***"). (The Supreme Court of Canada denied leave to appeal the *Anderson* decision ([2004] S.C.C.A. No. 81).) The Court in *Anderson* applied the legal test for fraud established in *Théroux*.

[96] In interpreting section 57(b) of the BC Act, the British Columbia Court of Appeal stated in *Anderson* that:

> … s. 57(b) does not dispense with proof of fraud, including proof of a guilty mind … Section 57(b) simply widens the prohibition against participation in transactions to include participants who know or ought to know that a fraud is being perpetrated by others, as well as those who participate in perpetrating the fraud. It does not eliminate proof of fraud, including proof of subjective knowledge of the facts constituting the dishonest act, by someone involved in the transactions. [emphasis in original]
>
> (*Anderson*, *supra,* at para. 26.)

[97] The Court in *Anderson* also stated that:

> [f]raud is a very serious allegation which carries a stigma and requires a high standard of proof. While proof in a civil or regulatory case does not have to meet the criminal law standard of proof beyond a reasonable doubt, it does require evidence that is clear and convincing proof of the elements of fraud, including the mental element.
>
> (*Anderson*, *supra*, at para. 29.)

[98] The legal test for fraud applied by the Court in *Anderson* was adopted in *Capital Alternatives*, which was affirmed in *Brost C.A.*

[99] In order for a corporation to commit fraud under section 126.1(b) of the Act, it is sufficient to show that the directing mind of the corporation knew that a fraud was being perpetrated.

[100] Our interpretation of section 126.1(b) of the Act discussed below is consistent with the foregoing decisions including the conclusions of the Commission in *Al-Tar*.

b. Lehman and Schnedl Committed Fraud

[101] Lehman committed dishonest acts by making numerous deceitful and false statements to investors including, in particular, that their funds would be invested in oil futures and/or foreign treasury bonds. We have no evidence that the investors' funds were ever used for that purpose. It also appears that the Austrian Investors' account statements falsely showed fictitious investments and purported investment returns. There is no doubt based on the evidence that Lehman committed acts of deceit and falsehood through its representations in soliciting investors to invest in the scheme. The Supreme Court of Canada has stated that "other fraudulent means" include the non-disclosure of important facts, the unauthorized diversion of funds and the arrogation of funds or property. Lehman and Schnedl did each of those things.

[102] As noted above, we found that Schnedl was a directing mind of Lehman and participated personally in the fraudulent activity.

[103] The second element required to establish fraud is deprivation caused by the dishonest acts. In this case, as a result of the deceitful and false statements made by Lehman, investors wired substantial amounts of money to Lehman bank accounts in Toronto. A substantial portion of those funds were misappropriated by Schnedl for his personal benefit. The Austrian Investors have demanded the repayment of the amounts they wired to Lehman and have received no response. Accordingly, the Austrian Investors have been deprived of those funds as a result of the dishonest acts of Lehman and Schnedl. The second element of fraud, deprivation, is therefore established against Lehman and Schnedl.

[104] Finally, in order to commit fraud, a person must have the necessary mental element (*mens rea*). As discussed in *Théroux*, the person must have subjective knowledge of the prohibited conduct and that a consequence of that conduct will be the deprivation of another. Based on our conclusions in paragraphs 101 to 103, 123 and 125 of these reasons, we find that Lehman and Schnedl *knowingly* committed fraud by depriving the Austrian Investors of the funds that they were induced by deceit to forward to Lehman.

[105] Accordingly, we find that Lehman and Schnedl *knowingly* perpetrated a fraud and, subject to the discussion below, contravened section 126.1(b) of the Act.

c. Was the Fraud Committed in Ontario?

[106] In order for a person to contravene section 126.1(b) of the Act, a fraud must have been perpetrated. The section does not expressly address whether it applies to any fraud or only to a fraud that occurs in Ontario. In our view, the section should be interpreted broadly to apply to any fraud. If a person has engaged or participated in "any act, practice or course of conduct relating to securities" that occurs in Ontario and that conduct perpetrates a fraud, wherever that fraud may have occurred, there is a public interest in not permitting that conduct in Ontario. This conclusion is particularly important because of the interjurisdictional nature of many securities frauds. This interpretation of section 126.1(b) is consistent with the legislative history of section 57(b) of the BC Act. A previous iteration of section 57(b) expressly applied to a fraud that occurred outside British Columbia (see paragraph 22 of *Anderson, supra,* for the earlier provision). Accordingly, in our view, section 126.1(b) is engaged where there is any act, practice or course of conduct relating to securities that occurs in Ontario and a fraud is perpetrated; it is not necessary that the fraud occur in Ontario.

[107] In any event, we believe that in this case the fraud perpetrated by Lehman and Schnedl occurred in Ontario because of the real and substantial link between the fraud and Ontario.

[108] The Supreme Court of Canada discussed in *Regina v. Libman,* [1985] 2 S.C.R. 178 ("***Libman***") the jurisdiction to prosecute a fraud under the *Criminal Code of Canada,* R.S.C. 1985, c. C-46 (the "***Code***") where the elements of the offence were carried out in more than one jurisdiction. The Court held that for an offence to be subject to its jurisdiction "a real and substantial link" must exist between the offence and Canada (*Libman, supra,* at para. 74).

[109] The accused in *Libman* was committed to stand trial on seven counts of fraud under the *Code,* and one count of conspiracy to commit fraud, for a fraudulent telephone sales solicitation scheme (i.e., a "boiler room operation") that operated out of Toronto. That fraud involved selling shares to United States residents who were directed to send their subscription monies to Central America. Some of the proceeds, however, were ultimately wired to the accused in Toronto (*Libman, supra,* at paras. 3-5).

[110] Writing for the Supreme Court of Canada, La Forest J. held that there were "ample links" to Toronto sufficient to ground jurisdiction and stated, "… the preparatory activities to perpetrate the fraudulent scheme were in themselves sufficient to warrant a holding that the offence took place in Canada" (*Libman, supra,* at paras. 72-76).

[111] Further, the fact that the person affected by the fraudulent activity may reside outside of Canada does not limit the court's jurisdiction over the fraudulent conduct (*Libman, supra,* at paras. 57 and 58).

[112] Recently, the Ontario Court of Appeal followed the *Libman* analysis in *R. v. Stucky,* 2009 ONCA 151 ("***Stucky***") in finding that the meaning of "the public" in a section of the *Competition Act,* R.S.C. 1985, c. C-34 was not restricted to the Canadian public where there was a real and substantial link or connection between the offence and Canada. The Court also stated in *Stucky*

that "[…] the "real and substantial link" or connection test articulated in *Libman* has been applied outside the *Criminal Code* context and is part of our general law concerning jurisdiction" (*Stucky, supra,* at para. 33).

[113] We note that the Ontario Superior Court of Justice in *R v. Drakes*, [2005] O.J. No. 2863 (Sup. Ct.) ("***Drakes***") did not find a "real and substantial link" where the evidence did not show any connection between the fraud and Canada other than funds being sent to bank accounts in Canada. In that case, Epstein J. applied the "real and substantial link" test to a fraudulent letter scheme involving the transfer of monies from Antigua to bank accounts in Canada. In considering *Libman,* Epstein J. stated:

> … [t]he fact that there is evidence that the money ultimately found its way to Canada is a relevant consideration in determining whether there was a real and substantial link between the offence and Canada.
>
> However, this finding does not, by itself, lead to a conclusion that there is a 'substantial link' between the alleged fraud and Canada. What remains to be determined is whether the delivery of the funds was an "integral" part of a scheme initiated in Canada.
>
> (*Drakes, supra,* at paras. 56-57).

d. Staff Submissions

[114] Staff submitted that Lehman is a corporation incorporated under the laws of Ontario. Given the illegal acts of Lehman and Schnedl and the public interest mandate of the Commission, Staff submitted that this fact alone should be enough to give the Commission jurisdiction over the Respondents for purposes of section 126.1(b) of the Act. That fact is reinforced by the fact that Schnedl came to Toronto for the express purpose of incorporating Lehman.

[115] Staff also pointed to the fact that Lehman opened bank accounts in Ontario, that Lehman established the Toronto Virtual Office and used that office as part of the fraudulent scheme, that telephone numbers with the Toronto area code were given to investors, and that the Lehman Web site and the administrative forms used by Lehman referred to the Toronto Virtual Office.

e. Real and Substantial Link to Ontario

[116] In our view, there is a real and substantial link between the fraud committed by Lehman and Schnedl and Ontario, even though the fraud was not planned or initiated by persons in Ontario. We were particularly influenced in coming to this conclusion by the fact that Lehman was incorporated in Ontario, Lehman was held out as carrying on business in and from Ontario, the Virtual Office was located in Ontario and was used in carrying out the investment scheme, and investor funds were wired to Lehman bank accounts established in Toronto. These elements of the investment scheme were an integral part of the fraud. We also find that the incorporation of Lehman, the establishment of the Toronto Virtual Office and the opening of the bank accounts were preparatory activities to perpetrate the fraudulent scheme (see paragraph 110 of these

reasons). Accordingly, we find that Lehman and Schnedl knowingly perpetrated a fraud in Ontario for purposes of section 126.1(b) of the Act.

[117] Based on our conclusions in paragraphs 85 and 116 of these reasons, we find that Lehman and Schnedl engaged or participated in an act, practice or course of conduct relating to securities that they knew perpetrated a fraud. Accordingly, Lehman and Schnedl contravened section 126.1(b) of the Act.

f. Knowledge of the Fraud by Unzer and Grundmann

[118] Section 126.1 of the Act applies by its terms to persons that knew or who "reasonably ought to [have] known" that a fraud was being perpetrated by others. We have no evidence that Unzer or Grundmann had subjective knowledge (i.e., knew) that a fraud was being perpetrated. Accordingly, in order for us to find that they contravened section 126.1(b), we must conclude that they *reasonably ought to have known* that a fraud was being committed by Lehman and Schnedl. Those words impose an objective test.

[119] As noted above, the operative language of section 126.1(b) of the Act is identical to section 57(b) of the BC Act. The British Columbia Court of Appeal found in *Anderson* at paragraph 24 that:

> [Section 57] creates a statutory prohibition which may extend to persons who ought to be aware of the fraud even though they may not be participants in it… Section 57(b) simply widens the prohibition against participation in transactions to include participants who know or ought to know that a fraud is being perpetrated by others, as well as those who participate in perpetrating the fraud.

[120] The British Columbia Court of Appeal in *Anderson* also held that while the fraud provision extends to those who "ought to know that fraud is being perpetrated by others," it "does not eliminate…proof of subjective knowledge of the facts constituting the dishonest act, by someone involved in the transaction" (*Anderson, supra,* at para. 26).

[121] We have concluded above that Lehman and Schnedl knowingly perpetrated a fraud for purposes of section 126.1(b) of the Act. We heard evidence that Unzer and Grundmann participated in the fraud by contacting the Austrian Investors to sell the investment scheme to them on behalf of Lehman and that they made use of the Toronto Virtual Office in doing so. We do not have any evidence, however, that Unzer or Grundmann knew or reasonably ought to have known that the investment scheme was a fraud, that the investor account statements were a sham, or that investor funds were being diverted to and misappropriated by Schnedl. While we can speculate that Unzer and Grundmann probably did know that the investment scheme was a fraud, that is not enough.

[122] In our view, we have insufficient evidence to determine whether Unzer and Grundmann knew or reasonably ought to have known that Lehman and Schnedl were perpetrating a fraud. Accordingly, we dismiss the allegations against Unzer and Grundmann that they contravened section 126.1(b) of the Act.

iv. Conclusions as to Section 126.1(b) of the Act

Lehman

[123] Based on the evidence, we have concluded that Lehman, among other things:

(a) promoted a fraudulent investment scheme and sold that scheme to investors in Europe;

(b) made deceitful and false statements to the Austrian Investors about the investment scheme through its representatives;

(c) used the Lehman Web site to make available to the Austrian Investors and other investors fictitious account statements showing investments that were never made by Lehman;

(d) established and used bank accounts in Toronto to receive investor funds in connection with the investment scheme;

(e) established the Toronto Virtual Office and used it to mislead investors in connection with the investment scheme; and

(f) misappropriated investors' funds.

[124] Accordingly, we concluded that Lehman knowingly perpetrated a fraud and contravened section 126.1(b) of the Act.

Schnedl

[125] Based on the evidence, we have concluded that Schnedl, among other things:

(a) caused the incorporation of Lehman in Ontario for purposes of carrying out the investment scheme and was a directing mind of Lehman;

(b) promoted a fraudulent investment scheme and sold that scheme to investors in Europe;

(c) made deceitful and false statements to the Austrian Investors about the investment scheme;

(d) arranged for the maintenance of the Lehman Web site and used it to make available to the Austrian Investors and other investors fictitious account statements showing investments that were never made by Lehman;

(e) established Lehman's Toronto bank accounts, acted as sole signing authority for those accounts and used them to receive investor funds in connection with the investment scheme;

(f) established the Toronto Virtual Office on behalf of Lehman and used it to mislead investors in connection with the investment scheme; and

(g) misappropriated investors' funds.

[126] Accordingly, we concluded that Schnedl knowingly perpetrated a fraud and contravened section 126.1(b) of the Act.

Unzer and Grundmann

[127] We have concluded that there is insufficient evidence that Unzer or Grundmann knew or reasonably ought to have known that Lehman and Schnedl were perpetrating a fraud. We therefore dismissed the allegations that Unzer and Grundmann contravened section 126.1(b) of the Act.

C. Was the Conduct of the Respondents Contrary to the Public Interest?

i. The Applicable Law

[128] Under section 1.1 of the Act, the Commission's mandate is:

(a) to provide protection to investors from unfair, improper or fraudulent practices; and

(b) to foster fair and efficient capital markets and confidence in those capital markets.

[129] Subsection 127(1) of the Act permits the Commission to make a wide range of orders sanctioning conduct if it concludes that doing so is in the public interest. The Commission's public interest jurisdiction permits it to take action to prevent future harm to Ontario investors and Ontario capital markets and to deter others from conduct giving rise to such harm.

ii. Analysis and Conclusion

[130] We have a public interest in ensuring that Ontario capital markets are not used to perpetrate a fraud and to misappropriate investor funds, wherever those investors may be located. It appears clear that the sole reason Lehman was incorporated in Ontario, the Toronto Virtual Office was established, and bank accounts were opened in Toronto was to mislead investors located outside Canada into believing that they were dealing with a reputable company and individuals resident and carrying on business in Ontario. That behaviour undermines the integrity of Ontario capital markets and their reputation in the rest of the world for fairness and integrity. The Commission came to a similar conclusion in *Sunwide* (*Sunwide*, *supra*, at para. 75).

[131] Accordingly, in our view, each of Lehman, Schnedl, Unzer and Grundmann, by making use of the Toronto Virtual Office and the Lehman Toronto bank accounts in connection with the investment scheme, has acted contrary to the public interest within the meaning of the Act. We have also concluded that each of Lehman, Schnedl, Unzer and Grundmann has acted contrary to the public interest as a result of our findings in paragraphs 72, 74, 77, 80 and 117 of these reasons (to the extent that any such finding applies to a particular Respondent).

VI. CONCLUSION

[132] For the reasons discussed above, we have concluded that:

(a) each of Lehman, Schnedl, Unzer and Grundmann contravened subsection 25(1)(a) of the Act;

(b) each of Lehman and Schnedl knowingly perpetrated a fraud and contravened section 126.1(b) of the Act; and

(c) each of Lehman, Schnedl, Unzer and Grundmann acted contrary to the public interest.

[133] As noted above, it appears from the testimony of the Austrian Investors that "Hehlsinger" is an alias used by Schnedl. Accordingly, each of our findings in these reasons that relate to Schnedl also apply to Schnedl using the Hehlsinger alias.

[134] Staff should contact the Office of the Secretary to the Commission to schedule a hearing to determine the appropriate sanctions, and any cost order, to be imposed in light of our findings.

Dated at Toronto this 28th day of July, 2010.

"James E. A. Turner"

James E. A. Turner

"Carol S. Perry"

Carol S. Perry

"Sinan O. Akdeniz"

Sinan O. Akdeniz