Ontario Securities Commission
Commission des valeurs mobilières de l'Ontario
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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
BLACKWOOD & ROSE INC., STEVEN ZETCHUS and JUSTIN KRELLER (also known as JUSTIN KAY)

REASONS AND DECISION ON SANCTIONS AND COSTS
(Section 127 of the *Securities Act*)

Hearing:	March 12, 2014	
Decision:	April 30, 2014	
Panel:	James E. A. Turner	- Vice-Chair
Submissions:	Carlo Rossi	- For Staff of the Ontario Securities Commission
		- No one appeared for any of the Respondents

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REASONS AND DECISION
ON SANCTIONS AND COSTS

I. BACKGROUND

[1] This was a hearing before the Ontario Securities Commission (the "**Commission**") to consider pursuant to sections 127 and 127.1 of the *Securities Act*, R.S.O. 1990, c. S.5, as amended (the "**Act**") whether it is in the public interest to make an order with respect to sanctions and costs against Blackwood & Rose Inc. ("**Blackwood**"), Steven Zetchus ("**Zetchus**") and Justin Kreller ("**Kreller**") (collectively, the "**Respondents**").

[2] The hearing on the merits was heard in writing and the decision on the merits was issued on December 17, 2013 (the "**Merits Decision**").

[3] Following the release of the Merits Decision, we held a separate hearing on March 12, 2014 to consider submissions from Staff of the Commission ("**Staff**") regarding sanctions and costs (the "**Sanctions and Costs Hearing**"). No one appeared for the Respondents at the Sanctions and Costs Hearing.

[4] I am satisfied that the Notice of Hearing of the Sanctions and Costs Hearing and the submissions of Staff were served on the Respondents and that Staff took reasonable steps to provide notice of this proceeding to the Respondents. Therefore, I am entitled to proceed in their absence in accordance with section 7 of the *Statutory Power Procedures Act*, R.S.O. 1990, c. S.22 and Rule 7.1 of the Commission's *Rules of Procedure*.

[5] These are my reasons and decision as to the appropriate sanctions and costs to be ordered against the Respondents. A Sanctions and Costs Order is attached as "Schedule A" to these reasons.

II. THE MERITS DECISION

[6] In a Statement of Allegations dated January 29, 2013, Staff alleged that the Respondents held themselves out as engaging in the business of trading in securities and through misrepresentations, deceit and other fraudulent means solicited members of the public in the United States to transfer funds to Blackwood purportedly in furtherance of transactions involving the purchase and/or sale of securities.

[7] I concluded in the Merits Decision that each of the Respondents engaged in and held themselves out as engaging in the business of trading in securities without registration in circumstances in which no exemption from registration was available, contrary to section 25 of the Act and each of the Respondents directly or indirectly engaged in or participated in an act, practice or course of conduct relating to securities which they knew, or reasonably ought to have known, perpetrated a fraud on investors, contrary to subsection 126.1(b) of the Act. Further, I concluded that Zetchus authorized, permitted or acquiesced in Blackwood's non-compliance with Ontario securities law and was therefore deemed under section 129.2 of the Act to also have not complied with Ontario securities law. Finally, I held that the conduct of each of the

Respondents was contrary to the public interest and harmful to the integrity of the Ontario capital markets.

[8] My reasons for reaching these conclusions are summarized in the Merits Decision as follows:

> [64] There is ample evidence in the Vanderlaan Affidavit demonstrating that the Respondents engaged in conduct relating to securities that they knew or reasonably ought to have known would perpetrate a fraud on the Gigapix Shareholders in connection with the Gigapix Scheme.
>
> [65] The Respondents deceived investors with respect to the nature of the Gigapix Scheme and the Gigapix Shareholders suffered actual loss of all amounts they sent to Blackwood.
>
> [66] Zetchus represented Blackwood to be an established firm with a broad and reputable client base. The Blackwood Website described Blackwood as a "specialized boutique firm, serving Venture Capital Companies, Corporate & Institutional Clients, as well as Individual Consumers, Small and Middle Market Businesses and Large Corporations with a full range of Market Data & Trending Metrics Research". The Blackwood Website also indicated, among other things, that Blackwood:
>
> - [serves] more than 2000 consumer and small business relationships;
> - offers industry leading support through a suite of innovative services;
> - serves clients in more than 20 countries;
> - has relationships with U.S. Fortune 500 companies and Fortune Global 500; and
> - has a team of analysts that provide specialized data research and trending metrics.
>
> [67] In reality, the evidence shows that Blackwood had only been established in August 2012, had no clients, no business relationships, no analysts, no innovative services and the only deposits, other than those from the Gigapix Shareholders, into the Blackwood bank accounts came from Zetchus's mother and from the sale of a list of potential investors to an individual that Zetchus declined to name in his compelled interview.
>
> [68] The Gigapix Shareholders were all solicited by Blackwood on the basis that Blackwood could arrange for the sale of their shares. The Individual Respondents' own admissions in the compelled testimony acknowledge that the solicitations were based on deceitful representations about Blackwood's business and about its role in the fictitious acquisition of Gigapix shares.

[69] Kreller lied about his name and made representations to the Gigapix Shareholders that he knew or ought to have known were false and misleading. Kreller knew that the salespersons at Blackwood used aliases; he saw the information on the Blackwood website and acknowledged that he knew it was inaccurate. He knew he was not working for an established firm and he knew or ought to have known that by soliciting two of the Gigapix Shareholders on the basis of these fraudulent representations that a deprivation would likely result.

[70] Kreller attempted to mislead the Examiner and others by telling them that Blackwood had acquired shares from a distressed brokerage and offered to sell shares that Blackwood did not in fact own. Kreller also suggested to one potential investor that Blackwood had "insider information" with respect to Barrick and Dundee, when it in fact did not.

[71] Kreller was reckless as to the consequences of his actions, including the risk that perpetuating Zetchus's misrepresentations would result in a deprivation of two of the Gigapix Shareholders.

…

[76] Based on the foregoing, Staff has established dishonest acts on the part of Blackwood, Zetchus and Kreller and a deprivation to the Gigapix Shareholders. The evidence establishes subjective awareness and subjective intent on the part of Blackwood, Zetchus and Kreller to perpetrate a fraud.

[84] The evidence in this case overwhelmingly establishes that the Respondents engaged in and held themselves and itself out as engaging in the business of trading in securities.

[85] I find that the evidence establishes that:

(a) Blackwood was held out, through the Blackwood Website and the representations to members of the public by Zetchus and Kreller, as an established firm engaged in the business of trading in securities;

(b) the Gigapix Shareholders were solicited by the Respondents to: (i) send funds to purportedly open trading accounts with Blackwood; (ii) purchase shares in two publicly listed companies: Barrick and Dundee, and one private company; and (iii) sell shares they held in Gigapix, on the basis of deceitful representations made by the Respondents in connection with that solicitation;

(c) the Respondents sent emails and other documents to the Gigapix Shareholders in support of their solicitations that purported to, among other things, confirm the terms of transactions involving the purchase or sale of securities, provide deposit instructions to the investors, record the investors' investment preferences, provide Blackwood with authority to undertake trades on the investors' behalf, and promote transactions involving the sale of securities;

(d) Blackwood received funds from the Gigapix Shareholders in connection with the purported transactions involving the sale of their Gigapix shares and Zetchus and Kreller profited from their conduct; and

(e) Kreller worked on a commission basis and received a commission for one of the transactions.

…

[93] Zetchus was the sole director and directing mind of Blackwood during the Material Time and he authorized, permitted and acquiesced in all the conduct undertaken on behalf of Blackwood. Among other things, the evidence shows that Zetchus:

(a) incorporated Blackwood;

(b) rented the office space on behalf of Blackwood and hired salespersons;

(c) supervised Kreller;

(d) created the Blackwood Website;

(e) opened the Blackwood bank accounts and was the sole signatory on those accounts;

(f) solicited the Examiner; and

(g) misappropriated the funds that the Gigapix Shareholders sent to Blackwood.

[94] Zetchus was a director and officer of Blackwood and I find that he authorized, permitted and acquiesced in Blackwood's non-compliance with Ontario securities law described in these reasons. Accordingly, he is deemed pursuant to section 129.2 of the Act to have also failed to comply with Ontario securities law.

(Merits Decision at paras. 64 to 71, 76, 84, 85, 93 and 94)

[9] I will consider my findings and conclusions in the Merits Decision in determining the appropriate sanctions and costs order in this matter.

III. SANCTIONS AND COSTS REQUESTED BY STAFF

[10] Staff requests the following sanctions and costs orders:

(a) with respect to Blackwood that:

(i) pursuant to clause 2 of subsection 127(1) of the Act, trading in any securities by Blackwood cease permanently;

(ii) pursuant to clause 2.1 of subsection 127(1) of the Act, the acquisition of any securities by Blackwood be prohibited permanently;

(iii) pursuant to clause 3 of subsection 127(1) of the Act, any exemptions contained in Ontario securities law not apply to Blackwood permanently; and

(iv) pursuant to clause 10 of subsection 127(1) of the Act, Blackwood disgorge to the Commission, on a joint and several basis with Zetchus, the amount of $15,634 obtained as a result of its non-compliance with Ontario securities law, such amount to be designated for allocation or use by the Commission pursuant to subsection 3.4(2)(b)(i) or (ii) of the Act;

(b) with respect to Zetchus that:

(i) pursuant to clause 2 of subsection 127(1) of the Act, trading in any securities by Zetchus cease permanently;

(ii) pursuant to clause 2.1 of subsection 127(1) of the Act, the acquisition of any securities by Zetchus be prohibited permanently;

(iii) pursuant to clause 3 of subsection 127(1) of the Act, any exemptions contained in Ontario securities law not apply to Zetchus permanently;

(iv) pursuant to clause 6 of subsection 127(1) of the Act, Zetchus be reprimanded;

(v) pursuant to clauses 8, 8.2, and 8.4 of subsection 127(1) of the Act, Zetchus be prohibited permanently from becoming or acting as a director or officer of any issuer, registrant, or investment fund manager;

(vi) pursuant to clause 8.5 of subsection 127(1) of the Act, Zetchus be prohibited permanently from becoming or acting as a registrant, as an investment fund manager or as a promoter;

(vii) pursuant to clause 9 of subsection 127(1) of the Act, Zetchus pay an administrative penalty in the amount of $100,000 for his failure to comply with Ontario securities law, such amount to be designated for allocation or use by the Commission pursuant to subsection 3.4(2)(b)(i) or (ii) of the Act;

(viii) pursuant to clause 10 of subsection 127(1) of the Act, Zetchus disgorge to the Commission, on a joint and several basis with Blackwood, the amount of $15,634 obtained as a result of his non-compliance with Ontario securities law, such amount to be designated for allocation or use by the Commission pursuant to subsection 3.4(2)(b)(i) or (ii) of the Act; and

(ix) pursuant to subsection 37(1) of the Act, Zetchus be prohibited permanently from telephoning from within Ontario to any residence within or outside Ontario for the purpose of trading in any security or derivative or in any class of securities or derivatives;

(c) with respect to Kreller that:

(i) pursuant to clause 2 of subsection 127(1) of the Act, trading in any securities by Kreller cease permanently;

(ii) pursuant to clause 2.1 of subsection 127(1) of the Act, the acquisition of any securities by Kreller be prohibited permanently;

(iii) pursuant to clause 3 of subsection 127(1) of the Act, any exemptions contained in Ontario securities law not apply to Kreller permanently;

(iv) pursuant to clause 6 of subsection 127(1) of the Act, Kreller be reprimanded;

(v) pursuant to clauses 8, 8.2, and 8.4 of subsection 127(1) of the Act, Kreller be prohibited permanently from becoming or acting as a director or officer of any reporting issuer, registrant, investment fund manager or any issuer that engages in a distribution of securities to the public;

(vi) pursuant to clause 8.5 of subsection 127(1) of the Act, Kreller be prohibited permanently from becoming or acting as a registrant, as an investment fund manager or as a promoter;

(vii) pursuant to clause 9 of subsection 127(1) of the Act, Kreller pay an administrative penalty in the amount of $25,000 for his failure to comply with Ontario securities law, such amount to be designated for allocation or use by the Commission pursuant to subsection 3.4(2)(b)(i) or (ii) of the Act;

(viii) pursuant to clause 10 of subsection 127(1) of the Act, Kreller disgorge to the Commission the amount of $1,000 obtained as a result of his non-compliance with Ontario securities law, such amount to be designated for allocation or use by the Commission pursuant to subsection 3.4(2)(b)(i) or (ii) of the Act; and

(ix) pursuant to subsection 37(1) of the Act, Kreller be prohibited permanently from telephoning from within Ontario to any residence within or outside Ontario for the purpose of trading in any security or derivative or in any class of securities or derivatives.

IV. STAFF SUBMISSIONS

Administrative Penalties

[11] Staff seeks orders that Zetchus pay an administrative penalty in the amount of $100,000 and that Kreller pay an administrative penalty in the amount of $25,000.

[12] The Commission has held that an administrative penalty should be of a magnitude sufficient to ensure effective specific and general deterrence. Factors to be considered in determining an appropriate administrative penalty include: the scope and seriousness of a respondent's misconduct; whether there were multiple and/or repeated breaches of the Act; whether the respondent realized any profit as a result of his or her misconduct; the amount of money raised from investors; the harm caused to investors; and the level of administrative penalties imposed in other cases. (*Limelight Entertainment Inc. (Re)* (2008) 31 OSCB 12030 ("***Limelight Sanctions***"), at paras. 67 and 71)

[13] Applying these principles, and considering the amount of disgorgement sought, together with the totality of the sanctions requested, Staff submits that the administrative penalties sought are appropriate and proportionate to the respective conduct of the Respondents.

Disgorgement

[14] Staff seeks an order, pursuant to clause 10 of subsection 127(1) of the Act, requiring each of the Respondents to disgorge to the Commission all amounts obtained as a result of their non-compliance with Ontario securities law.

[15] Staff seeks a disgorgement order that Blackwood and Zetchus jointly and severally disgorge $15,634 to the Commission, being the total amount obtained by them as a result of their non-compliance with Ontario securities law. Staff submits that Kreller should be required to disgorge $ 1,000, the amount Staff estimates that Kreller made in cash and other compensation while at Blackwood.

[16] Pursuant to clause 10 of subsection 127(1) of the Act, the Commission has the power to order disgorgement of "any amounts obtained as a result of the non-compliance" with Ontario securities law. The Commission has previously held that "all money illegally obtained from investors can be ordered to be disgorged, not just the 'profit' made as a result of the activity" *(Act, supra* at subsection 127(1)10, *Limelight Sanctions, supra,* at para. 49).

[17] In *Limelight Sanctions,* the Commission held that it should consider the following factors when contemplating a disgorgement order:

(a) whether an amount was obtained by a respondent as a result of non-compliance with the Act;

(b) the seriousness of the misconduct and the breaches of the Act and whether investors were seriously harmed;

(c) whether the amount that a respondent obtained as a result of noncompliance with

the Act is reasonably ascertainable;

(d) whether the individuals who suffered losses are likely to be able to obtain redress; and

(e) the deterrent effect of a disgorgement order on the respondents and other market participants.

(Limelight Sanctions, supra, at para. 52)

[18] Staff submits that the following factors support the disgorgement orders requested:

(a) the amounts requested were obtained as a result of the Respondents' fraudulent conduct in breach of Ontario securities law;

(b) the misconduct was serious and investors were harmed by the fraud; and

(c) the amount obtained has been ascertained.

[19] Staff submits that an order for disgorgement of the entire amount obtained from investors would achieve the objectives of general and specific deterrence, would be proportionate to the Respondents' conduct and would be consistent with other Commission decisions.

Staff's Conclusions on Sanctions

[20] Staff submits that this matter involves egregious conduct by the Respondents involving significant contraventions of the Act in circumstances where the Respondents showed a complete disregard for investors and the integrity of the capital markets. The Respondents perpetrated a fraud on investors and the Commission found that both Zetchus and Kreller had subjective intent to perpetrate that fraud. The Respondents pose an on-going risk to Ontario investors and capital markets.

[21] In Staff's submission, the Respondents' intentional fraudulent conduct warrants their permanent removal from Ontario capital markets to protect investors and the integrity of those capital markets in the future.

[22] While the Respondents' fraudulent scheme was detected and restrained at an early stage, Staff submits that their conduct clearly shows that they were willing to lie and deceive investors in order to profit personally.

[23] The Respondents' conduct undermined the integrity of and confidence in the Ontario capital markets and caused significant harm to investors.

[24] Staff submits that the Respondents should also be ordered to disgorge all amounts obtained as a result of their non-compliance with Ontario securities law and be ordered to pay administrative penalties that are more than simply a cost of doing business.

[25] Staff submits that Zetchus and Kreller have demonstrated an utter lack of regard for the capital markets and the investors they deceived. There is a need to send a strong message to the Respondents and the public at large that involvement in these types of schemes will result in significant sanctions.

[26] Staff notes that neither Zetchus nor Kreller attended any of the hearings in connection with this matter, either personally or through a representative, nor did they present evidence, make submissions, otherwise acknowledge the seriousness of their improprieties or express remorse. At best, they demonstrated a casual indifference to the proceedings. Staff submits that such casual indifference ought to be interpreted as a lack of recognition of the seriousness of their improprieties.

Costs

[27] Staff also seeks an order for payment of Commission investigation and hearing costs pursuant to section 127.1 of the Act. Staff requests total costs of $49,692.50 to be apportioned as follows:

(a) Zetchus shall pay $37,269.38, representing 75% of the total costs sought; and

(b) Kreller shall pay $12,423.12, representing 25% of the total costs sought.

[28] Rule 18.2 of the Commission's *Rules of Procedure* provides that the Commission may consider the following factors in determining whether to order costs under section 127.1 of the Act:

(a) whether the respondent failed to comply with a procedural order or direction of the Panel;

(b) the complexity of the proceeding;

(c) the importance of the issues;

(d) the conduct of Staff during the investigation and during the proceeding, and how Staff's conduct contributed to the costs of the investigation and the proceeding;

(e) whether the respondent contributed to a shorter, more efficient, and more effective hearing, or whether the conduct of the respondent unnecessarily lengthened the duration of the proceeding;

(f) whether any step in the proceeding was taken in an improper, vexatious, unreasonable, or negligent fashion or in error;

(g) whether the respondent participated in the proceeding in a way that helped the Commission understand the issues before it;

(h) whether the respondent participated in a responsible, informed and well-prepared manner;

(i) whether the respondent co-operated with Staff and disclosed all relevant information;

(j) whether the respondent denied or refused to admit anything that should have been admitted; or

(k) any other factors the Panel considers relevant.

(Ontario Securities Commission *Rules of Procedure,* Rule 18.2)

[29] Staff submits that they used a conservative approach in preparing their bill of costs. The bill of costs reflects only the time spent by the primary investigator, Wayne Vanderlaan, Senior Investigator, and the primary litigator, Carlo Rossi, Litigation Counsel, involved in this matter.

[30] Staff submits that the amounts set out in paragraph [27] of these reasons are reasonable in the circumstances and that a costs order on the terms requested by Staff is in the public interest.

V. NO SUBMISSIONS BY THE RESPONDENTS

[31] None of the Respondents appeared or participated in the hearing on the merits or in the Sanctions and Costs Hearing.

VI. SANCTIONS

(i) The Law on Sanctions

[32] The Commission's dual 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 capital markets (*Act, supra* at section 1.1).

[33] The Commission's objective when imposing sanctions is not to punish past conduct but rather to restrain future conduct that may be harmful to Ontario investors or capital markets. This objective was described in *Re Mithras Management Ltd.* as follows:

> … the role of this Commission is to protect the public interest by removing from the capital markets – wholly or partially, permanently or temporarily, as the circumstances may warrant – those whose conduct in the past leads us to conclude that their conduct in the future may well be detrimental to the integrity of those capital markets. We are not here to punish past conduct; that is the role of the courts, particularly under section 118 [now 122] 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.
>
> (*Re Mithras Management Ltd.* (1990), 13 OSCB 1600 at pp. 1610-1611)

[34] Further, the Supreme Court of Canada has recognized general deterrence as an additional factor that the Commission may consider when imposing sanctions. In *Cartaway Resources Corp.*, [2004] 1 S.C.R. 672 at para. 60 the Supreme Court stated that: "…it is reasonable to view general deterrence as an appropriate and perhaps necessary consideration in making orders that are both protective and preventative".

[35] The Commission must ensure that the sanctions imposed in each case are proportionate to the circumstances and conduct of each respondent. The Commission has previously identified the following as some of the factors that a panel should consider when imposing sanctions:

> (a) the seriousness of the conduct and the breaches of the Act;
> (b) the respondent's experience in the marketplace;
> (c) the level of a respondent's activity in the marketplace;
> (d) whether or not there has been recognition by a respondent of the seriousness of the improprieties;
> (e) whether or not the sanctions imposed may serve to deter not only those involved in the matter being considered, but any like-minded people, from engaging in similar abuses of the capital markets;
> (f) the size of any profit obtained or loss avoided from the illegal conduct;
> (g) the size of any financial sanction or voluntary payment;
> (h) the effect any sanctions may have on the ability of a respondent to participate without check in the capital markets;
> (i) the reputation and prestige of the respondent;
> (j) the remorse of the respondent; and
> (k) any mitigating factors.
>
> (*Re Belteco Holdings Inc.* (1998), 21 OSCB 7743 at p. 7746 and *Re M.C.J.C. Holdings Inc. and Michael Cowpland* (2002), 25 OSCB 1133 at para. 26)

[36] Ultimately, the sanctions I impose must protect Ontario's capital markets and investors by restricting or barring the Respondents from participating in our markets and by deterring others from using our jurisdiction to perpetrate fraudulent schemes which are abusive of investors outside Ontario.

Relevant Commission Decisions

[37] In *Al-Tar Energy Corp.*, the Commission considered the appropriate sanctions to be imposed in the context of a fraudulent investment scheme. (*Al-Tar Energy Corp (Re)* (2011), 34 OSCB 447 ("***Al-Tar Sanctions***")

[38] The Panel summarized its approach to sanctions in that case:

> Overall, the sanctions that we impose must protect investors and Ontario capital markets by barring or restricting the Respondents from participating in those markets in the future and by sending a clear message to the Respondents and others participating in our capital markets that the type of misconduct identified in this matter will not be tolerated.

(*Al-Tar Sanctions, supra,* at para. 26)

[39] The Commission found that the public interest "require[d] that the Respondents be restrained permanently from any future participation in the capital markets". In addition to permanent market conduct prohibitions, the Panel ordered that the respondents disgorge all amounts illegally obtained and pay significant administrative penalties. (*Al-Tar Sanctions, supra,* at para. 82)

[40] The Panel emphasized that an administrative penalty "must be more than a fee for or cost of carrying out a fraudulent scheme":

> The Individual Respondents engaged in fraudulent conduct that warrants the imposition of substantial administrative penalties. We do not consider the amount of the administrative penalties requested by staff to be sufficient to deter similar conduct in the future. In our view, to be a deterrent, the amount of the administrative penalty must bear some reference to the amount raised from investors through the investment scheme. In addition, in cases where fraud and repetitive conduct over an extended period is involved, higher administrative penalties are necessary. In order to deter, an administrative penalty must be more than a fee for or a cost of carrying out a fraudulent scheme.
>
> (*Al-Tar Sanctions, supra,* at para. 47)

[41] The Commission's approach to sanctions in cases of fraudulent investment schemes was reflected in *Al-Tar* and has been applied in recent cases including *Global Partners Capital (Re)* (2011), 34 OSCB 10023, *Goldpoint Resources Corp. (Re)* (2013), 36 OSCB 1464 and *Global Energy Group, Ltd.* (Re) (2013), 36 OSCB 12153.

[42] This reasoning also underpins the Commission's decisions in cases involving "advance-fee" schemes. Those schemes are designed to extract an advance or upfront payment from investors on the basis of some fictitious transaction such as an offer to purchase shares held by an investor at inflated prices. In both *Sunwide Finance Inc.* (Re) (2009), 32 OSCB 4671 and *Lehman Brothers & Associates Corp.* (Re) (2012) 35 OSCB 5357 ("***Lehman Brothers***"), cases involving an advance fee scheme, the Commission concluded that the respondents should be permanently barred from the capital markets and, in the case of *Lehman Brothers*, that substantial financial sanctions were appropriate.

[43] There are no Commission decisions where a relatively small amount of money was raised fraudulently from investors. Staff submits that the amount raised is a factor to consider when ordering administrative penalties. However, Staff says that where the intent to defraud investors exists, significant sanctions are warranted, irrespective of the amount raised from investors. Further, Staff submits that an administrative penalty must be sufficient to ensure specific and general deterrence. An administrative penalty must not simply be a cost of doing business.

[44] Staff submits that all of the sanctions they have requested are reasonable and appropriate in the circumstances.

(ii) Findings and Conclusions as to Sanctions

Specific Factors Applicable in this Matter

[45] In considering the factors referred to in paragraph [35] of these reasons, I find the following factors and circumstances to be most relevant in this matter, based on the findings in the Merits Decision (set out in paragraph [8] of these reasons):

(a) the conduct of the Respondents was clearly egregious; as noted above, the Respondents solicited and sold investments they knew were a sham, lied to and misled investors and misappropriated USD $15,634 of investors' funds;

(b) all of the Respondents breached a number of key provisions of the Act which are intended to protect investors from the very conduct that occurred here; the Respondents actions caused damage to the integrity of Ontario's capital markets and were clearly contrary to the public interest;

(c) Zetchus and Kreller solicited shareholders in Gigapix Studios, Inc. ("**Gigapix**" and the "**Gigapix Shareholders**") to send funds to Blackwood purportedly to facilitate the sale of the Gigapix shares held by the Gigapix Shareholders (the "**Gigapix Scheme**"); that solicitation was made by telephone to investors located outside of Ontario;

(d) as part of the Gigapix Scheme, the Gigapix Shareholders were told by Zetchus and Kreller that Blackwood had buyers for their Gigapix shares but that various advance payments were required to be made in order to complete the sales. These representations were false and were designed to fraudulently extract money from the Gigapix Shareholders;

(e) Kreller's communications with investors included the use of an alias and deceitful and false statements;

(f) Zetchus and Kreller knew or ought to have known that they were selling securities in breach of the Act;

(g) the funds received from investors were misappropriated by Zetchus and were not used to further any transactions involving the purchase of Gigapix shares;

(h) the investors have received no consideration for their payments; and

(i) in addition to the Gigapix Scheme, Zetchus and Kreller, through Blackwood, solicited U.S. residents to send funds to Blackwood for the purported purpose of opening an account with Blackwood and to purchase shares Blackwood said it held in several companies; Zetchus and Kreller used deceit, falsehood and other fraudulent means to solicit these funds from the investors.

[46] While I recognise that a relatively small amount of money was obtained by the Respondents from investors, it is important that I impose significant sanctions in order to emphasize that we will not tolerate conduct in this jurisdiction intended to defraud investors located outside of Ontario. That conduct is unacceptable.

Trading and Other Prohibitions

[47] One of the Commission's objectives in imposing sanctions is to restrain future conduct that could be harmful to investors or Ontario's capital markets. In this case, I find that the public interest requires the Commission to restrain the Respondents from future participation in Ontario capital markets.

[48] Staff requested a permanent ban against each of the Respondents trading any securities, acquiring any securities, relying on any prospectus exemptions or acting as a registrant, an investment fund manager or a promoter. Staff also requested a permanent ban for Zetchus from becoming or acting as a director or officer of *any issuer*, registrant or investment fund manager. In respect of Kreller, Staff requested a permanent ban from becoming or acting as a director of *a reporting issuer*, registrant, investment fund manager or any issuer that engages in any distribution of securities to the public. In Staff's submission, the more limited restriction on being a director or officer for Kreller is appropriate given his relatively limited role and his young age. Staff submits that a ban on the terms requested does not unnecessarily restrict Kreller's ability to earn a living.

[49] Staff submits that, given the Panel's findings in the Merits Decision that the Respondents engaged in deceitful conduct by means of telephone calls to investors outside Canada, the individual respondents should be permanently prohibited from telephoning from within Ontario to any residence within or outside Ontario for the purpose of trading or acting in furtherance of a trade in securities, pursuant to subsection 37(1) of the Act. I agree with this submission and find that such prohibitions are in the public interest.

[50] In all of the circumstances, I have concluded that it is in the public interest to make the market conduct orders requested by Staff as they relate to Blackwood and Zetchus. Because of Kreller's young age and more limited involvement in the Gigapix Scheme, I have restricted certain of the prohibitions applicable to him to a 10-year period. Those prohibitions shall, however, continue to apply to Kreller after the 10-year period until such time as Kreller pays to the Commission the administrative penalty and costs award imposed on him. Accordingly, I impose the following sanctions:

(a) a permanent cease trade order against Blackwood and Zetchus and a 10-year cease trade order against Kreller;

(b) a permanent prohibition order against Blackwood and Zetchus acquiring any securities and a 10-year prohibition order against Kreller acquiring any securities;

(c) a permanent removal of exemptions order against Blackwood and Zetchus and a 10-year removal of exemptions order against Kreller;

(d) an order that Zetchus be prohibited permanently from becoming or acting as a director or officer of any issuer, registrant, or investment fund manager;

(e) an order that Kreller be prohibited for a period of 10 years from becoming or acting as a director or officer of any reporting issuer, registrant, investment fund manager or any issuer that engages in any distribution of securities to the public;

(f) an order that Zetchus be prohibited permanently from becoming or acting as a registrant, as an investment fund manager or as a promoter and an order that Kreller be prohibited for a period of 10 years from becoming or acting as a registrant, as an investment fund manager or as a promoter;

(g) an order that each of Zetchus and Kreller be prohibited permanently from telephoning from within Ontario to any residence within or outside Ontario for the purpose of trading in any security or derivative or in any class of securities or derivatives; and

(h) an order reprimanding each of Zetchus and Kreller.

Disgorgement

[51] Subsection 127(1)10 of the Act provides that a person or company that has not complied with Ontario securities law can be ordered to disgorge to the Commission "any amounts obtained" as a result of the non-compliance. The disgorgement remedy is intended to ensure that such persons do not obtain financial benefits from their breaches of the Act and to provide specific and general deterrence.

[52] In considering the issue of a disgorgement order, I have considered the factors referred to in paragraph [17] of these reasons.

[53] In my view, a disgorgement order against Blackwood and Zetchus for the full amount obtained from investors is appropriate in these circumstances. It was Zetchus who concocted, orchestrated and carried out the Gigapix Scheme and misappropriated investors' funds. I will order that Blackwood and Zetchus disgorge to the Commission US $15,634 on a joint and several basis. That amount represents the total amount that was obtained by Blackwood and Zetchus from investors. I impose joint and several liability on Blackwood and Zetchus because, as stated in the Merits Decision, Zetchus was the directing and controlling mind of Blackwood.

[54] Staff requested an order that Kreller disgorge to the Commission $1,000, being the amount he obtained from Zetchus for his participation in the Gigapix Scheme. Kreller estimated that of that $1,000, between $200 and $400 was for commissions, and the remainder was for a cell

phone which was given to him by Zetchus to facilitate his role at Blackwood. Staff submits that the $1,000 is compensation which Kreller received directly as a result of his conduct in breach of the Act. I am not satisfied that the full amount of $1,000 constitutes "an amount obtained" by Kreller within the meaning of subsection 127(1)10 of the Act. In all the circumstances, I will not make a disgorgement order against Kreller.

Administrative Penalties

[55] In my view, it is appropriate in this matter to impose administrative penalties against Zetchus and Kreller. I have considered the submissions made by Staff as to the appropriate administrative penalties in this case. Staff submits that, while the amount obtained by the Respondents is significantly less than any previous fraud case before the Commission, substantial administrative penalties are warranted. Staff submits that had the Respondents' conduct not been detected as early as it was, they would have continued to raise funds from investors through their fraudulent scheme.

[56] The $100,000 administrative penalty requested by Staff for Zetchus appears to be one of the lowest administrative penalties imposed by the Commission on the directing mind of a fraudulent scheme, and the $25,000 administrative penalty requested by Staff for Kreller appears to be the lowest such penalty that has been ordered by the Commission in a fraud case.

[57] In imposing the following administrative penalties, I have considered my findings in the Merits Decision and the respective roles and involvement of each Respondent in the illegal conduct involved in this matter.

[58] I will order that an administrative penalty of $100,000 be paid to the Commission by Blackwood and Zetchus on a joint and several basis, and that an administrative penalty of $25,000 be paid by Kreller. I note that Staff did not request that Blackwood and Zetchus pay the $100,000 penalty on a joint and several basis but in the circumstances I find that to be appropriate. Blackwood, Zetchus and Kreller committed multiple violations of the Act and committed a fraud that caused significant financial harm to investors. Zetchus was the directing and controlling mind of Blackwood and orchestrated the Gigapix Scheme and misappropriated investors' funds. Substantial administrative penalties are justified because the Respondents intentionally misled and defrauded investors.

VII. COSTS

[59] Staff seeks an order for the payment of $49,692.50 of the costs of the investigation and hearing in this matter, to be apportioned as follows:

(a) an order that Zetchus pay $37,269.38, representing 75% of the total costs sought: and

(b) an order that Kreller pay $12,423.12, representing 25% of the total costs sought.

[60] A costs order pursuant to section 127.1 of the Act is not a sanction. An order of costs is a way of recovering the costs of an investigation or hearing from the persons or companies who have breached Ontario securities law or acted contrary to the public interest. A costs order will not necessarily recover the entirety of the costs incurred by the Commission, but it is appropriate

that a respondent contribute to the costs of a hearing where there has been a finding that the respondent has contravened Ontario securities law or acted contrary to the public interest.

[61] Staff has submitted a bill of costs supporting the costs awards requested. The amount requested by Staff reflects only the time spent by the primary investigator and litigator in this matter. Staff submits that the amounts requested for costs are proportionate and reasonable in the circumstances. I agree with their submission.

[62] I order that costs in the amount of $37,000 shall be paid to the Commission by Zetchus and that costs in the amount of $12,000 shall be paid to the Commission by Kreller.

VIII. CONCLUSION

[63] For the reasons discussed above, I have concluded that the sanctions I impose in this matter are proportionate to the respective conduct and culpability of each Respondent in the circumstances and are in the public interest. I will issue a sanctions and costs order in the form appended to these reasons.

DATED at Toronto, this 30th day of April, 2014.

"*James E. A. Turner*"

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James E. A. Turner

Schedule "A"

Ontario Securities Commission | Commission des valeurs mobilières de l'Ontario | 22nd Floor 20 Queen Street West Toronto ON M5H 3S8 | 22e étage 20, rue queen ouest Toronto ON M5H 3S8

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

-AND-

IN THE MATTER OF
BLACKWOOD & ROSE INC., STEVEN ZETCHUS and JUSTIN KRELLER (also known as JUSTIN KAY)

ORDER
(Sections 127 and 127.1 of the *Securities Act*)

WHEREAS on January 29, 2013, a Statement of Allegations and a Notice of Hearing were issued pursuant to sections 127 and 127.1 of the *Securities Act*, R.S.O. 1990, c. S.5, as amended (the "**Act**") in respect of Blackwood & Rose Inc. ("**Blackwood**"), Steven Zetchus ("**Zetchus**") and Justin Kreller ("**Kreller**") (collectively, the "**Respondents**");

AND WHEREAS the Commission conducted a hearing in writing on the merits in this matter;

AND WHEREAS the Commission issued its Reasons and Decision on the merits on December 17, 2013 (the "**Merits Decision**");

AND WHEREAS the Commission concluded that the Respondents committed fraud and contravened Ontario securities law and acted contrary to the public interest, as described in the Merits Decision;

AND WHEREAS the Commission conducted a hearing on March 12, 2014 with respect to the sanctions and costs to be imposed in this matter;

AND WHEREAS the Commission is of the opinion that it is in the public interest to make this order;

IT IS HEREBY ORDERED THAT:

(a) pursuant to clause 2 of subsection 127(1) of the Act, each of Blackwood and Zetchus shall cease trading in any securities permanently and Kreller shall cease trading in securities for a period of 10 years from the date of this Order;

(b) pursuant to clause 2.1 of subsection 127(1) of the Act, the acquisition of any securities by Blackwood or Zetchus is prohibited permanently and the acquisition of any securities by Kreller is prohibited for a period of 10 years from the date of this Order;

(c) pursuant to clause 3 of subsection 127(1) of the Act, any exemptions in Ontario securities law not apply permanently to either Blackwood or Zetchus and that any exemptions in Ontario securities law not apply to Kreller for a period of 10 years from the date of this Order;

(d) pursuant to clause 6 of subsection 127(1) of the Act, each of Zetchus and Kreller are reprimanded;

(e) pursuant to clause 8, 8.2 and 8.4 of subsection 127(1) of the Act, Zetchus is prohibited permanently from becoming or acting as a director or officer of any issuer, registrant, or investment fund manager;

(f) pursuant to clause 8, 8.2 and 8.4 of subsection 127(1) of the Act, Kreller be prohibited for a period of 10 years from becoming or acting as a director or officer of any reporting issuer, registrant, investment fund manager or any issuer that engages in any distribution of securities to the public;

(g) pursuant to clause 8.5 of subsection 127(1) of the Act, Zetchus is prohibited permanently from becoming or acting as a registrant, an investment fund manager or as a promoter and Kreller is prohibited for a period of 10 years from becoming or acting as a registrant, an investment fund manager or as a promoter;

(h) pursuant to clause 9 of subsection 127(1) of the Act, Blackwood and Zetchus shall pay to the Commission on a joint and several basis an administrative penalty of $100,000, for their contraventions of Ontario securities law, such amount to be designated for allocation or use by the Commission pursuant to subsection 3.4(2)(b)(i) or (ii) of the Act;

(i) pursuant to clause 10 of subsection 127(1) of the Act, Blackwood and Zetchus shall disgorge to the Commission on a joint and several basis the amount of USD$15,634 obtained by them as a result of their non-compliance with Ontario securities law, such amount to be designated for allocation or use by the Commission pursuant to subsection 3.4(2)(b)(i) or (ii) of the Act;

(j) pursuant to clause 9 of subsection 127(1) of the Act, Kreller shall pay to the Commission an administrative penalty of $25,000 for his contraventions of Ontario securities law, such amount to be designated for allocation or use by the Commission pursuant to subsection 3.4(2)(b)(i) or (ii) of the Act;

(k) pursuant to subsection 37(1) of the Act, each of Zetchus and Kreller are prohibited permanently from telephoning from within Ontario to any

residence within or outside Ontario for the purpose of trading in any security or derivative or in any class of securities or derivatives; and

(l) pursuant to section 127.1 of the Act, Zetchus shall pay to the Commission costs of $37,000 and Kreller shall pay costs of $12,000;

(m) notwithstanding clauses (a), (b), (c), (f) and (g) of this Order, those prohibitions shall continue to apply to Kreller after the 10-year period from the date of this Order until such time as Kreller pays to the Commission the amounts referred to in clauses (j) and (l) of this Order.

DATED at Toronto, Ontario this 30th day of April, 2014.

"*James E. A. Turner*"

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James E. A. Turner