ALBERTA SECURITIES COMMISSION

DECISION

Citation: Harris operating as Harris Agencies, Re, 2011 ABASC 138 Date: 20110317

Robert John Harris operating as Harris Agencies

Panel:	Kenneth B. Potter, QC Glenda A. Campbell, QC Neil W. Murphy
Appearing:	Carla A. Murray for Commission Staff
	Derek Lovatt for Robert John Harris operating as Harris Agencies
Dates of Hearing:	1-2 February 2011
Date of Decision:	17 March 2011

I. INTRODUCTION

[1] This is a proceeding before the Alberta Securities Commission (the "Commission") to consider whether it is in the public interest or appropriate to make orders under sections 198, 199 and 202 of the *Securities Act*, R.S.A. 2000, c. S-4 (the "Act") against Robert John Harris operating as Harris Agencies (the "Respondent") arising from allegations made by Commission staff ("Staff") set out in a notice of hearing dated 1 October 2010 (the "Notice of Hearing").

[2] Staff alleged in the Notice of Hearing that the Respondent breached Alberta securities laws and engaged in conduct contrary to the public interest by trading and dealing in securities in Alberta without being registered to do so or having an applicable exemption, engaging in illegal distributions of securities in Alberta, making misleading and untrue statements to Alberta investors and perpetrating a fraud on Alberta investors.

[3] During the hearing of the allegations against the Respondent, which commenced on 1 February 2011, Staff tendered documentary evidence (including a 25 January 2011 Statement of Admissions (the "Harris Admissions") signed by Robert John Harris ("Harris")) and elicited testimony from a Staff investigator and two investors (for privacy reasons, we identify investor witnesses by their initials). In the Harris Admissions, Harris acknowledged that he had received independent legal advice throughout this proceeding, including advice relative to the Harris Admissions, and that he had made the admissions therein voluntarily.

[4] The Respondent, who was represented by counsel, was not personally present at the hearing. No evidence was tendered or witnesses called by counsel for the Respondent.

[5] Only Staff elected to make submissions on the merits of the allegations against the Respondent. Staff and counsel for the Respondent agreed to make submissions as to what sanctioning and costs orders would be in the public interest or appropriate were the panel to uphold the allegations, and we heard those submissions on 2 February 2011.

[6] Our decision and reasons on the merits of the allegations against the Respondent follow. Stated briefly, we find that the Respondent:

- contravened section 75(1) of the Act by illegally trading and dealing in securities in Alberta;
- contravened section 110 by illegally distributing securities in Alberta;
- contravened section 92(4.1) by making misleading and untrue statements to Alberta investors;
- contravened section 93(b) by perpetrating a fraud on Alberta investors; and
- in so doing, engaged in conduct contrary to the public interest.

[7] Our decision and reasons as to sanctioning and costs orders also follow. In summary, we find it is in the public interest to order that the Respondent:

- cease trading in securities and is denied the use of exemptions under Alberta securities laws, permanently;
- is prohibited from acting as a director or officer (or both) of any issuer, permanently;
- is prohibited from acting in a management or consultative capacity in connection with securities market activities, permanently; and
- pay an administrative penalty of $500 000.

[8] We also consider it appropriate that the Respondent pay $13 000 towards the costs of the investigation and hearing.

II. FACTUAL BACKGROUND

[9] We summarize below the factual background relevant to our decision, derived from the testimony heard and the documentary evidence (including the Harris Admissions) received.

A. The Respondent

[10] Harris resided from 2000 until April 2010 in Calgary, Alberta but currently resides in Wasa, British Columbia. Harris was, from 2000 until 31 December 2009, licensed to sell life insurance and other insurance products in Alberta. Harris Agencies ("Harris Agencies") was an unincorporated and otherwise unregistered business that Harris owned and operated at all material times in Calgary.

[11] Neither Harris nor Harris Agencies has ever been registered under the Act. No prospectus has ever been filed or receipted in accordance with the Act, and no reports of exempt distribution have been filed with the Commission, in respect of a distribution of securities of Harris or Harris Agencies (or both). While the certified statement issued under section 218 of the Act does not refer to the Respondent per se, we infer from the evidence as a whole, and find, that the Respondent has never been registered under the Act and that no prospectus has ever been filed or receipted in accordance with the Act, and no reports of exempt distribution have been filed with the Commission, in respect of a distribution of securities of the Respondent.

[12] Harris was convicted in Calgary in 1983 on 42 charges of fraud over $200 contrary to the *Criminal Code* (Canada) and received a sentence of four years' imprisonment on each charge concurrent. According to the Harris Admissions, this conviction resulted from Harris's "illegally raising money from investors by making false statements to them about what he planned to do with the monies invested and instead operating a [P]onzi scheme".

B. Solicitations

[13] In order to promote the sale of insurance products to current and prospective insurance clients, Harris controlled and operated a real estate investment club (the "Club"), in which, he stipulated, only his current clients were eligible to participate.

[14] Approximately 200 of Harris's insurance clients, primarily Albertans, invested in the Club (the "Club Investors").

[15] Harris told the Club Investors that the investment money was being used to purchase real estate and second mortgages which would then be resold.

[16] After advancing the investment money, the Club Investors received promissory notes issued by "Robert Harris/Harris Agencies" (the "Promissory Notes"). It seems, from the evidence as a whole including the Promissory Notes in evidence, that the Promissory Notes set out the amount owed to the Club Investor (consisting of the amount advanced plus a profit component sometimes calculated using a rate greater than the minimum rate of return stipulated), the due date and the minimum rate of return (the Promissory Notes in evidence stipulated 15%). It also seems from the evidence as a whole that the Promissory Notes included handwritten notations made by Harris, such as notations about the working capital (the amount advanced), the calculated profit component, the start-up date, the projected cycle and the purported product invested in. The Promissory Notes contained three different signatures – represented to be one for Harris, one for Harris Agencies and one for a witness – all of which signatures were, Harris admitted, executed by Harris. Harris admitted that the handwritten notations provided false information and that he falsified signatures on the Promissory Notes so that the Promissory Notes would seem more legitimate to the Club Investors.

[17] By issuing the Promissory Notes to the Club Investors, Harris raised, he admitted, at least $5-6 million from about 2000 to 2010. The last investment in the Club was made in March or April 2010.

[18] Harris admitted that, contrary to what he told the Club Investors, he did not purchase any real estate or second mortgages with the investment money but, instead, the majority of the investment money was paid to certain of the Club Investors "in the manner of a [P]onzi scheme". Thus, certain of the Club Investors were periodically paid a high rate of interest (ranging between 15% and 23%), while others were not paid. Harris admitted to convincing certain of the Club Investors to reinvest any profits earned back into the Club by telling them that their prior investments had earned 23% even if their Promissory Notes only stipulated a 15% rate of return.

[19] Harris also admitted to making expenditures from the investment money for himself and the promotion and operation of his insurance business, including monthly payments totalling almost $2300 and periodic payments totalling approximately $3500. In the Harris Admissions, Harris recalled that he periodically comingled the investment money with money earned from the sales of insurance and related products to the Club Investors and others.

[20] Harris further admitted that he made statements to the Club Investors that he knew were misleading and untrue, including that he was purchasing real estate and second mortgages with

the investment money when he was not and that their investments in the Club were "safe" and "secure".

C. Investor Evidence

1. JD

[21] JD, an Alberta resident, testified that he was introduced to Harris in the fall of 2006 by friends who were apparently long-time clients of Harris. JD had no involvement with Harris prior to that time. JD understood, from Harris, that the Club pooled money from investors, which was to be used to purchase distressed properties or mortgages. Harris claimed to have advance knowledge of distressed properties from his insurance business and people with whom he was involved such as bankers. Harris told JD that the investment was "virtually risk free", "very low risk" and "secured against the properties". Harris also told JD that Harris did not make any money from the Club and suggested it was done as a benefit to his clients.

[22] JD and his wife invested approximately $181 000 in the Club during the period October 2006 to April 2008, for which they received Promissory Notes. This money was sourced from a line of credit secured against the equity in their home. JD and his wife also reinvested in the Club amounts owing on certain of the Promissory Notes issued to them, for which they received new Promissory Notes. The last Promissory Note issued to them was dated 30 March 2009.

[23] Many times JD requested a list of the properties in which he and his wife were investing, but Harris refused, saying that it would be a breach of confidence for him to provide such a list.

[24] At the time of JD's initial investment in the Club, there was no discussion as to whether JD qualified as an accredited investor or eligible investor and JD was not a close friend or business associate of Harris. JD was never provided with an offering memorandum or risk acknowledgement form.

[25] In 2008 JD received cheques from Harris Agencies totalling $83 069. Taking this into account, JD estimated that he and his wife have lost approximately $100 000 of the principal they invested. JD described the impact of this loss as "quite substantial" and "very large". JD testified that he is now "very leery" about investing and that he is not sure he and his wife would ever do it again. JD, who had been encouraged to and did trust Harris, also testified that Harris "didn't just hurt me and my family, he very much scarred us".

2. JH

[26] JH and her husband CH are Alberta residents. According to JH, CH first met Harris in 2000, and JH first met Harris probably in 2001.

[27] After CH purchased a life insurance policy from Harris in 2000, Harris told CH about the Club, which Harris described as an opportunity or "perk" offered only to clients. Harris also told CH about another investment club involving individuals meeting to learn about the stock market. Harris subsequently provided JH and CH with "real estate books". JH and CH met with Harris to ask him about a point mentioned in these books that caused JH concern – high rates of return being indicative of a Ponzi scheme. JH told us that Harris laughed and said, "Why would I provide you with these books and do something like this to you." Then, seeking a mortgage for

their home in 2002, JH and CH met, on Harris's recommendation, with bank personnel, who said that the Club was "a great opportunity". This gave JH and CH "some information to move forward with our investments with [Harris]" and shortly thereafter they invested in the Club. Harris also encouraged JH and CH to refer family and friends to Harris, which they did.

[28] JH and CH invested approximately $100 000 in the Club during the period 2002 to August 2008, for which they received Promissory Notes. The majority of this money was inherited, with the remainder drawn on a line of credit. JH and CH also reinvested in the Club amounts owing on certain of the Promissory Notes issued to them, for which they received new Promissory Notes.

[29] On a number of occasions JH and CH requested a list of the properties in which they were investing, but one was never provided. Harris told JH and CH that their principal investment was "safe".

[30] JH and CH received back the principal they invested (with $6000 to $10 000 of this being redirected into insurance investments). JH and CH continue to hold unpaid Promissory Notes with face amounts totalling $157 173.

[31] JH and CH were never provided with an offering memorandum or risk acknowledgement form. At the time of their initial investment in the Club, there was no discussion as to whether JH or CH qualified as an accredited investor or eligible investor and neither JH nor CH was a close friend or business associate of Harris. However, Harris subsequently became a fairly close friend of JH and CH – JH and CH cared for Harris during an illness, assisted Harris when his second wife died and were guests at Harris's third wedding.

[32] During the period 2008 and 2009 Harris provided numerous excuses to JH and CH for delays in transactions being completed and in payments being made, including that "FINTRAC was investigating his company" (which JH learned was not true). JH told us that she and CH tried to believe Harris and "looked for the best in him". However, following an April 2010 conversation with Commission personnel about Harris, JH decided to confront Harris. JH told us that she waited for Harris outside his home and that, when he finally spoke with her, Harris admitted to JH that the Club was a Ponzi scheme. According to JH, during this confrontation and in a telephone conversation a few days later, Harris expressed no remorse or concern about the Club Investors but rather spoke primarily about himself and how he had been affected.

[33] JH and CH commenced a legal action against Harris and Harris carrying on business under the name and style of Harris Agencies. JH and CH were subsequently appointed as the representative plaintiffs for a group of 54 investors in a class action brought against Harris and Harris carrying on business under the name and style of Harris Agencies. On 22 June 2010 consent judgment was obtained in the amount of $4 007 518 – the total of the face amounts of the Promissory Notes held by the 54 investors – but, according to JH, no money has been recovered as a result and any recovery of money is unlikely.

[34] JH testified that she felt betrayed, noting her and CH's personal relationship with Harris. She said that she was devastated when she finally learned that Harris, having been previously

jailed for something very similar, was nevertheless licensed to sell insurance products. JH also stated: "I don't know who I would trust making an investment now."

III. ANALYSIS AND FINDINGS ON MERITS

A. Illegal Trading and Dealing

[35] Staff alleged that the Respondent breached section 75(1) of the Act by trading and dealing in securities in Alberta without being registered to do so or having an applicable exemption.

[36] Section 75(1) of the Act (or its predecessor in the *Securities Act*, S.A. 1981, c. S-6.1) as it read during the period 2000 to 27 September 2009 prohibited a person or company from trading in a security if not registered to do so with the Executive Director of the Commission (the "Executive Director"), unless an exemption applied. Effective 28 September 2009, section 75(1) was revised to prohibit a person from acting as a dealer unless registered to do so in accordance with Alberta securities laws, unless an exemption applied. A person or company acts as a dealer within the meaning of the Act when engaging in or holding out as engaging in the business of trading in securities as principal or agent.

[37] Section 1(ggg)(v) of the Act defines "security" as including "any bond, debenture, note or other evidence of indebtedness". We find, consistent with the Harris Admissions, that the Promissory Notes issued in Alberta by Robert Harris/Harris Agencies – the Respondent – were notes or other evidences of indebtedness and thus "securities" under section 1(ggg)(v).

[38] We also find the arrangements between the Respondent and the Club Investors with respect to purchasing and reselling real estate and second mortgages to be "investment contracts" and thus "securities" under section 1(ggg)(xiv) of the Act. An investment contract is an investment of money in a common enterprise with expected profits derived significantly from the efforts of others (*Pacific Coast Coin Exchange of Canada Limited v. Ontario (Securities Commission)*, [1978] 2 S.C.R. 112, affirming (1975), 8 O.R. (2d) 257 (C.A.), affirming (1975), 7 O.R. (2d) 395 (Div. Ct.)). Here, the Club Investors were invited to, and did, make investments of money when they advanced money to the Respondent for investment in the Club, specifically, for the purchase of real estate and second mortgages by the Respondent. There was the required commonality between the Respondent who sought risk capital to invest and from which to profit and the Club Investors who paid money to the Respondent in search of profit. Once they paid their money to the Respondent, the Club Investors were not required to do anything further to earn their promised returns. Rather, the Club Investors were passive investors, wholly dependent on the efforts of the Respondent in purchasing and reselling real estate and second mortgages. This characterization of the arrangements between the Respondent and the Club Investors – what the Club Investors were led to believe and did believe they invested in – is in no way altered by the Respondent's intent to operate a Ponzi scheme.

[39] In sum, we find that the Promissory Notes issued in Alberta and the arrangements between the Respondent and the Club Investors with respect to purchasing and reselling real estate and second mortgages were securities under sections 1(ggg)(v) and (xiv) of the Act, respectively (and we will refer to them as the "Club Securities").

[40] A "trade" is defined in section 1(jjj) of the Act to include "any sale or disposition of a security for valuable consideration", including any act in furtherance of such sale. The Respondent solicited the purchase of the Club Securities in Alberta, and sold the Club Securities for money in Alberta. We find, consistent with the Harris Admissions, that the sales of the Club Securities by the Respondent, as well as the solicitations of such sales, were trades in Alberta within the meaning of section 1(jjj). The Respondent was clearly in the business of selling – trading in – securities as well as insurance products, and as part of that business offered clients the opportunity to purchase the Club Securities. The Respondent apparently hoped that clients who invested in the Club would be more motivated to purchase insurance and other investment products from the Respondent, resulting in increased sales and associated commissions. We find, consistent with the Harris Admissions, that the Respondent was also dealing in the Club Securities in Alberta.

[41] We found that the Respondent has never been registered under the Act. In the Harris Admissions, Harris admitted, consistent with the evidence as a whole, that he traded and dealt in securities in Alberta without being registered and without there being an applicable exemption to the registration requirement of the Act.

[42] We accordingly find, consistent with the Harris Admissions, that prior to 28 September 2009 the Respondent traded in securities in Alberta without being registered to do so or having an applicable registration exemption, and that from 28 September 2009 the Respondent acted as a dealer in Alberta without being registered to do so or having an applicable registration exemption, all in contravention of section 75(1) of the Act.

B. Illegal Distributions

[43] Staff alleged that the Respondent breached section 110 of the Act by distributing securities in Alberta without a prospectus having been filed or receipted for same or having an applicable exemption.

[44] Section 110 of the Act prohibits the distribution of a security if no prospectus has been filed with the Commission and receipted by the Executive Director, unless an exemption applied.

[45] Section 1(p) of the Act defines "distribution" to include "a trade in securities of an issuer that have not been previously issued". None of the Club Securities issued by the Respondent had been previously issued by the Respondent. Thus, we find that all of Respondent's trades in the Club Securities were distributions in Alberta within the meaning of section 1(p).

[46] We found that no prospectus has ever been filed or receipted in accordance with the Act in respect of a distribution of securities of the Respondent. In the Harris Admissions, Harris admitted, consistent with the evidence as a whole, that he distributed securities in Alberta without filing a prospectus and without there being an applicable exemption to the prospectus requirement of the Act.

[47] We accordingly find, consistent with the Harris Admissions, that the Respondent distributed securities in Alberta without a prospectus or an applicable prospectus exemption, in contravention of section 110 of the Act.

C. Misleading and Untrue Statements

[48] Staff alleged that the Respondent breached section 92(4.1) of the Act by making misleading and untrue statements to Alberta investors, including that the Respondent was purchasing real estate and second mortgages with their investment money and that their investments in the Club were "safe".

[49] Section 92(4.1) of the Act, which came into effect 8 June 2005, states:

> (4.1) No person or company shall make a statement that the person or company knows or reasonably ought to know
>
> (a) in any material respect . . .
>
> (i) is misleading or untrue, . . .
>
> and
>
> (b) would reasonably be expected to have a significant effect on the market price or value of a security[.]

[50] During the period 2000 to 7 June 2005, each governing section was worded somewhat differently; however, for purposes of our analysis, there are no substantive or material differences among the sections.

[51] As noted, Harris admitted that he made statements to the Club Investors, primarily Albertans, that he was purchasing real estate and second mortgages with the investment money and that their investments in the Club were "safe" and "secure". This admission is consistent with the evidence as a whole, including the investor witness testimony.

[52] We find, consistent with the Harris Admissions, that these statements by the Respondent were clearly misleading and untrue, and materially so, and the Respondent knew this. We further find that these statements would reasonably be expected to have a significant effect on the market price or value of the Club Securities, and the Respondent knew, or reasonably ought to have known, this.

[53] We therefore find, consistent with the Harris Admissions, that the Respondent contravened section 92(4.1) of the Act by making misleading and untrue statements to Alberta investors.

D. Fraud

[54] Staff alleged that the Respondent breached section 93(b) of the Act by perpetrating a fraud on Alberta investors. In particular, Staff alleged: "Contrary to what was told to the Investors, the Respondent did not purchase any real estate or second mortgages. Instead, monies raised through the Club went to paying a high rate of interest, ranging between 15% and 23%, to prior Investors in the Club in the manner of [P]onzi scheme."

[55] Section 93 of the Act, which came into effect 8 June 2005, states:

> 93 No person or company shall, directly or indirectly, engage or participate in any act, practice or course of conduct relating to a security . . . that the person or company knows or reasonably ought to know will . . .
>
> (b) perpetrate a fraud on any person or company.

[56] During the period 2000 to 7 June 2005, each governing section was worded somewhat differently; however, for purposes of our analysis, there are no substantive or material differences among the sections.

[57] The Act provides no definition of "fraud" in the securities regulation context. However, construing the term "fraud" in section 93 of the Act, this Commission said at para. 309 of *Re Capital Alternatives Inc*., 2007 ABASC 79 (affirmed 2008 ABCA 326):

> The term "fraud" is not defined in the Act. The gist of the meaning is not, however, difficult to discern. Johnston and Rockwell [in D. Johnston & K.D. Rockwell, *Canadian Securities Regulation*, 4th ed. (Markham: LexisNexis, 2007)] point to the elements of fraud as enunciated at common law by the Supreme Court of Canada in *R. v. Théroux*, [1993] 2 S.C.R. 5 at 27, which has been adopted in the context of securities regulation (for example, in *Anderson v. British Columbia (Securities Commission)*, 2004 BCCA 7 at para. 27):
>
> . . . the actus reus of the offence of fraud will be established by proof of:
>
> 1. the prohibited act, be it an act of deceit, a falsehood or some other fraudulent means; and
>
> 2. deprivation caused by the prohibited act, which may consist in actual loss or the placing of the victim's pecuniary interests at risk.
>
> Correspondingly, the *mens rea* of fraud 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 in knowledge that the victim's pecuniary interests are put at risk).

[58] In this case, it is clear that the Respondent committed "prohibited acts" as described in *Théroux*. The Respondent made misleading and untrue statements to the Club Investors, primarily Albertans: the Club Investors were told that the Respondent was purchasing real estate and second mortgages with the investment money, which was not done. Rather, the Respondent used the investment money to pay high rates of interest to certain of the Club Investors in a manner characteristic of a Ponzi scheme and to pay personal and business expenditures. Thus, the Club Investors were misled as to how the investment money would be used.

[59] It is also clear that there is "deprivation" as described in *Théroux*. In failing to use the investment money as represented, the Respondent caused deprivation to the Club Investors, primarily Albertans, consisting of actual financial loss or the risk thereof. While certain of the Club Investors were paid high rates of interest, others were not paid. It appears that many Club

Investors have lost some or all of the principal they invested and have failed to receive any or all of the promised returns.

[60] Further, it is clear that the Respondent had the requisite subjective knowledge of the prohibited acts and deprivation caused. That the Respondent had subjective knowledge of the prohibited acts is consistent with Harris's admissions that he knew the investment money was not being used to purchase real estate or second mortgages as represented but was being used to pay high rates of interest to certain of the Club Investors and to pay personal and business expenditures. Moreover, the Respondent had to know – especially given his previous conviction in Alberta for fraud relating to his operating a Ponzi scheme – that his misuse of investment money in a manner characteristic of a Ponzi scheme was not sustainable and could or would cause financial deprivation to the Club Investors.

[61] Thus, we find that the Respondent engaged in prohibited acts which caused deprivation to Alberta investors, had subjective knowledge of those prohibited acts and had subjective knowledge that those prohibited acts could or would have such deprivation as a consequence.

[62] Accordingly, we find, consistent with the Harris Admissions, that the Respondent contravened section 93(b) of the Act by perpetrating a fraud on Alberta investors.

E. Conduct Contrary to the Public Interest

[63] The Respondent promoted investment, through the Club, in real estate and mortgages. In fact, the Respondent did not use any of the money invested in the Club for this purpose. Instead, the Respondent operated a fraudulent Ponzi scheme, in which certain of the Club Investors were paid high rates of return using money invested by other of the Club Investors. Such activity encouraged continuing and wider participation in the scheme by giving it a legitimate appearance. However, because there was no legitimate underlying business to sustain the returns promised, there came a time when the inflow of new investment money so diminished that those remaining invested in the Club received little or nothing in the way of expected returns and lost some or all of the principal they had invested. Harris, having been previously convicted in Alberta for fraud relating to his operating a Ponzi scheme, knew that this was the inevitable result.

[64] The Respondent clearly knew that the scheme was fraudulent but nevertheless encouraged the Club Investors not only to invest but also to source investment money through leveraging. Moreover, although cognizant of the fraudulent nature of the scheme, the Respondent exhibited no compunction in encouraging and cultivating a relationship of trust or a personal relationship with at least some of the Club Investors. Such conduct was reprehensible and completely inconsistent with the public interest.

[65] The Respondent's capital market activities were conducted with complete disregard for Alberta securities laws, and, in the result, the Club Investors were denied the protections that come from dealing with registered salespersons and from receiving a prospectus with full, true and plain disclosure of all material facts in respect of the Club Securities.

[66] The Respondent's contraventions of Alberta securities laws caused direct financial harm to Alberta investors and threaten the integrity of, and investor confidence in, the Alberta capital market. Fraudulent capital market behaviour – the most serious of securities regulatory misconduct – can be especially damaging to the fairness and efficiency of our capital market. When investors lose their money through deceit, they and those who learn of their plight lose confidence in our capital market and look elsewhere for investment opportunities.

[67] It follows, and we find, that the Respondent's contraventions of Alberta securities laws were also contrary to the public interest.

F. Merits Decision

[68] We find that the Respondent:

- traded and acted as a dealer in securities in Alberta without being registered to do so or having an applicable registration exemption, in contravention of section 75(1) of the Act;
- distributed securities in Alberta without a prospectus or an applicable prospectus exemption, in contravention of section 110;
- contravened section 92(4.1) by making misleading and untrue statements to Alberta investors;
- contravened section 93(b) by perpetrating a fraud on Alberta investors; and
- in so doing, acted contrary to the public interest.

IV. ANALYSIS AND FINDINGS ON SANCTIONS AND COSTS

A. Introduction

[69] After conclusion of submissions on the merits of the allegations against the Respondent, Staff and counsel for the Respondent made submissions as to what sanctioning and costs orders would be in the public interest or appropriate were the panel to uphold the allegations.

[70] At the commencement of the hearing, the panel reiterated a concern raised in pre-hearing sessions that the Notice of Hearing named as respondent "Robert John Harris operating as Harris Agencies" and not Harris in his broader personal capacity. It was suggested that an amendment to the Notice of Hearing be considered. Staff commented that they saw no need to seek an amendment and subsequently commented that they would be satisfied if any orders made were issued against "Robert John Harris" or "Robert John Harris operating as Harris Agencies". On this point, counsel for the Respondent said only that he appreciated the difficulty Staff was contemplating when deciding who to name as respondent and that he also considered the panel's concerns valid. Because we are only able to issue orders against a respondent as named in a notice of hearing, we will proceed on that basis.

B. Sanctions

1. Parties' Submissions

(a) Staff

[71] Staff contended that the public interest would be served by: permanently banning the Respondent from trading in securities, using exemptions, acting as a director or officer of any issuer, and acting in a management or consultative capacity in connection with securities market activities; and having the Respondent pay an administrative penalty of $500 000.

[72] In so contending, Staff submitted that the Respondent admitted to numerous breaches of the Act, that investors were persuaded to invest in the Club through lies and deceit and that the Respondent's conduct demonstrated an egregious flouting of Alberta securities laws. Staff contended that the Respondent's past conduct included a 1983 conviction in Alberta for fraud relating to his operating a Ponzi scheme, which demonstrates that he is likely to re-offend. Staff also contended that there is no evidence or circumstance to suggest that the Respondent recognizes the seriousness of his improper activity. Staff noted that the Respondent has some prior experience in the capital market. Staff argued that the harm done to the Club Investors has been considerable. However, she submitted that, because Harris failed to retain a proper accounting of the bank account containing the investment money, it is not clear how much money the Club Investors have lost. Staff pointed to the evidence of investor witness JH that a group of 54 Club Investors have obtained judgment against Harris for more than $4 million and that any recovery under this judgment is unlikely; Staff also noted that this judgment does not include the claims of the approximately 146 Club Investors who did not participate in the lawsuit. Staff contended that the Respondent benefitted from his misconduct, as was admitted by him, but that the evidence does not disclose how much in additional commissions the Respondent earned from the sales of insurance products to the Club Investors. Staff argued that the seriousness of the Respondent's misconduct and the harm it caused to Alberta investors and the Alberta capital market call for sanctions, including a substantial administrative penalty, that would provide the necessary specific and general deterrence.

(b) The Respondent

[73] Counsel for the Respondent advised that, given Harris's age (approximately 70) and other factors, the Respondent takes no issue with the making of the permanent market-access bans sought by Staff, were the panel to find that the evidence justifies their imposition. Counsel also conceded that there should be a large administrative penalty imposed; however, he submitted that in the circumstances the quantum ordered should be much lower than the $500 000 proposed by Staff. Counsel contended that the Respondent did not operate the Club to make money, as was the case with most Ponzi schemes, but rather did so to increase his insurance business, to help people or as a means to gain client affection or adulation. Counsel stated it was apparent to him that Harris has "a pathological lack of insight" regarding his conduct, given his operation of another Ponzi scheme in 1983, for which he was convicted of fraud. Counsel suggested that the Respondent may have lost money from September 2008 to April 2010 because, during this time, Harris essentially mortgaged his own home to make payments of approximately $300 000 to Club Investors. This, counsel argued, is evidence of the Respondent's recognition of the seriousness of his misconduct. Counsel submitted that a much lower quantum of administrative penalty will provide the necessary specific deterrence in that the Respondent has no money, he did not make any money but rather lost money in the scheme and he essentially ruined his

personal and business life. Finally, counsel contended that there is very little evidence that the Respondent has any knowledge of the capital market, arguing that he did not run a sophisticated scheme.

2. Sanctioning Principles and Factors

[74] The Commission, which is responsible for the administration of Alberta securities laws, has jurisdiction in the public interest over the trading and dealing in and distributing of securities in Alberta. The protection of Alberta investors and the Alberta capital market from misconduct by capital market participants is an integral aspect of the Commission's public interest jurisdiction. In exercising our authority to order sanctions in the public interest under sections 198 and 199 of the Act, we do not punish or remedy capital market misconduct. Rather, we act prospectively to protect against and prevent future harm to Alberta investors and our capital market (*Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission)*, 2001 SCC 37 at paras. 39-45). The need for specific and general deterrence is an important consideration in determining what, if any, protective and preventative orders to make (*Re Cartaway Resources Corp*., 2004 SCC 26 at paras. 52-62).

[75] Several factors may be relevant in determining whether, or what, sanctions are in the public interest in respect of a particular respondent in the circumstances of a particular case. In our analysis, we are guided by a consideration of the factors identified at para. 11 of *Re Lamoureux*, [2002] A.S.C.D. No. 125 (affirmed on other grounds 2002 ABCA 253), as restated at para. 43 of *Re Workum and Hennig*, 2008 ABASC 719 (affirmed 2010 ABCA 405):

- the seriousness of the findings against the respondent and the respondent's recognition of that seriousness;
- characteristics of the respondent, including capital market experience and activity and any prior sanctions;
- any benefits received by the respondent and any harm to which investors or the capital market generally were exposed by the misconduct found;
- the risk to investors and the capital market if the respondent were to continue to operate unimpeded in the capital market or if others were to emulate the respondent's conduct;
- decisions or outcomes in other matters; and
- any mitigating considerations.

3. Application of Principles and Factors

[76] In applying the sanctioning principles and factors in light of the circumstances of this case and of the Respondent, we are of the view that, for the following reasons, the public interest requires the Respondent be made subject to very significant sanctions that will ensure he is never again able to participate in any role in the Alberta capital market.

(a) Seriousness, and Recognition of Seriousness, of Misconduct

[77] This case involved several contraventions by the Respondent of Alberta securities laws – the illegal trading and dealing in and distributing of securities in Alberta, the making of misleading and untrue statements to Alberta investors and the perpetration of a fraud on Alberta investors by operating a Ponzi scheme. All of these contraventions were serious contraventions, and, as noted, fraudulent capital market behaviour is the most serious of securities regulatory misconduct. The Respondent's misconduct denied Club Investors protections mandated by

Alberta securities laws – including the fundamental protections afforded by the advice of a qualified registrant and by the full, true and plain disclosure of material facts provided by a prospectus – and caused Club Investors financial harm or at least exposed them thereto. The Respondent's misconduct also poses a threat to the integrity of the Alberta capital market. The occurrence of any fraudulent activity in our capital market, in particular, can incite a rapid erosion of public confidence in that market. The seriousness of the Respondent's misconduct calls for very significant sanction against the Respondent.

[78] Staff argued that the Respondent's failure to appear personally at the hearing was indicative of a failure to recognize the seriousness of his misconduct. Counsel for the Respondent countered that the Respondent would have attended the hearing had he been required to do so, but that he feared for his safety and was too embarrassed and ashamed to attend. A respondent is not required to appear personally at a hearing and may appear by counsel or agent. As the Respondent was represented by counsel at the hearing, the Respondent's failure to be personally present at the hearing was not indicative of a failure to recognize the seriousness of his misconduct.

[79] That said, we do not believe that the evidence before us establishes anything remotely approaching a full recognition by the Respondent of the seriousness of his misconduct. This is so even if we were to accept, as indicative of some such recognition, that from September 2008 to April 2010 Harris essentially mortgaged his own home to make payments of approximately $300 000 to Club Investors. Indeed, given the payment period, is seems as likely that any such payments to Club Investors, or those of them earlier in time, were made primarily with a view to ensuring the continuation of the Ponzi scheme, which would be indicative of no recognition of seriousness by the Respondent. Further, that Harris was convicted in Alberta in 1983 for fraud as a result of his operating another Ponzi scheme strongly suggests to us that the Respondent has very little or no appreciation for the nature or seriousness of the misconduct at issue here. Moreover, according to investor witness JH, when she confronted Harris in April 2010 and spoke to him via telephone a few days later, Harris expressed no remorse or concern about the Club Investors but rather spoke primarily about himself and how he had been affected. This also strongly suggests to us that the Respondent has very little or no insight into the seriousness of his misconduct or its effects on the Club Investors. In sum, the evidence as a whole leads us to conclude that the Respondent fails to recognize in any meaningful way the seriousness of his misconduct and cannot be trusted to comply with Alberta securities laws or to act honestly in any future dealings in the Alberta capital market. This failure to recognize the seriousness of the misconduct also calls for very significant sanction against the Respondent.

(b) Capital Market Experience and Activity and Prior Sanctions

[80] Harris has never been registered under the Act. However, he was, from 2000 until 31 December 2009, licensed in Alberta to sell, and sold, insurance products that are similar to investment products, the sale of which is regulated by Alberta securities laws. Accordingly, the Respondent, with experience in a regulated industry, should have been alerted to the possibility of capital-raising regulatory requirements and that it was incumbent on him to learn of, and comply with, any such requirements. Further, the testimony of investor witness JH – to the effect that Harris told CH about another investment club involving individuals meeting to learn about the stock market and that Harris provided JH and CH with "real estate books" – suggests

an awareness by the Respondent of the capital market and the rules associated with that market, an awareness on which he did not – or chose not to – act.

[81] Moreover, as noted, Harris was convicted in Alberta in 1983 on 42 charges of criminal fraud over $200 for which he was imprisoned. This conviction resulted from Harris's raising money from investors by making false statements to them concerning his intentions for the money and instead operating a Ponzi scheme. Although this criminal prosecution was not a proceeding under Alberta securities laws, the Respondent had to know that the misconduct at issue here was illegal and thus knowingly flouted Alberta securities laws.

[82] This factor also argues for very significant sanction against the Respondent.

(c) Benefits Received and Harm to Investors and the Capital Market

[83] Counsel for the Respondent contended that the Respondent did not operate the Club to make money, as was the case with most Ponzi schemes, but rather did so to increase his insurance business, to help people or as a means to gain client affection or adulation. We find the latter two explanations difficult to understand given that Harris had to know, from prior experience, that Ponzi schemes are not sustainable. However, we are satisfied on the evidence that the Respondent operated the Club primarily to increase his insurance business and not to make money directly. To the extent that the Club was successful in attracting additional insurance-related business to the Respondent, the Respondent benefitted from such additional business. Harris admitted that, while the majority of the investment money was paid to certain of the Club Investors, he made expenditures from the investment money for himself and the promotion and operation of his insurance business, including monthly payments totalling almost $2300 and periodic payments totalling approximately $3500. To the extent expenditures were made for such purposes, the Respondent also benefitted, albeit modestly relative to the total amount raised. There is also evidence of Harris's transfer of approximately $300 000 of his own money to Harris Agencies for the purpose of making payments to Club Investors; however, it is unclear whether this transfer and any subsequent payments were motivated by a desire to help Club Investors or to keep the Ponzi scheme running.

[84] Harris admitted to raising at least $5-6 million from approximately 200 Club Investors, primarily Albertans, from about 2000 to 2010. The Staff investigator's review of bank statements for the Harris Agencies bank account for the period January 2004 to March 2010 indicated that slightly more than $9.1 million was paid into the account and a similar amount paid out. It is therefore possible that the total amount raised was in excess of the at least $5-6 million referenced in the Harris Admissions. However, the quality of the accounting records is such that it is impossible to quantify the amount raised or the total financial loss sustained by the Club Investors. Given the nature of a Ponzi scheme, some of those who participated – likely earlier participants – may have made money, while others will have received little or nothing in the way of expected returns and lost some or all of the principal they invested. For example, investor witness JD and his wife lost approximately $100 000 of their principal investment of $181 000 and have received none of the expected returns, whereas investor witness JH and her husband received back the principal they invested but continue to hold unpaid Promissory Notes with face amounts totalling $157 173. Further, JH told us that, in organizing for the class action against Harris and Harris carrying on business under the name and

style of Harris Agencies, she became aware of Club Investors who, having lost significant amounts of money, were unable to participate in the class action:

> . . . there were other people that contacted me that literally didn't have any money left, and they couldn't even pay the $130 towards a private investigator for a contribution. They had nothing left. There are people that had lost their retirement money, had leveraged so much on a line of credit that their homes are -- could be gone. There are some people that were considering bankruptcy and had. There was such a loss that people couldn't even move forward to this step with us as a class action.

[85] The 54 class action participants held unpaid Promissory Notes with face amounts totalling just over $4 million, although it is not known how much of those amounts constituted original principal. There are also approximately 146 additional Club Investors who did not participate in the class action, at least some of whom would hold unpaid Promissory Notes. Although the total financial loss sustained by the Club Investors cannot be quantified with exactitude, it is clear that the Respondent's misconduct caused significant financial loss to many Club Investors.

[86] The Respondent's misconduct also caused non-financial harm to Club Investors, such as investor witness JD, who had trusted Harris, and investor witness JH, who had developed a personal relationship with Harris. JD and JH were clearly devastated by the breach of that trust and abuse of that personal relationship.

[87] Further, the harm caused by the Respondent's misconduct is not limited to the financial and non-financial harm suffered by the Club Investors: the integrity of the Alberta capital market generally has also been damaged. Investor witness JD testified that this experience has made him "very leery" about investing, and investor witness JH testified that now she does not know who she would trust in making an investment. Club Investors have understandably lost confidence in our capital market, and others who learn of their plight may well experience a similar loss of confidence. In result, the ability of law-abiding issuers to raise money in our capital market may also suffer.

[88] These considerations, too, call for very significant sanction against the Respondent.

(d) Need for Specific and General Deterrence

[89] Harris's prior criminal conviction for conduct markedly similar to that which gave rise to this proceeding tells us that Harris's risk of re-offending is extremely high. This convinces us that, were the Respondent ever again to be allowed to operate in any role the Alberta capital market, the Respondent would pose a very significant risk to Alberta investors and our capital market.

[90] There is also considerable risk that others learning of the Respondent's success in raising a large amount of money through the operation of a Ponzi scheme might be tempted to engage in similar misconduct. Strong proactive steps are required to make it clear that such abuses of Alberta securities laws will not be tolerated and will result in severe consequences.

(e) Other Decisions

[91] Staff suggested to us that two Commission decisions – *Re Gold-Quest International Corp.*, 2010 ABASC 278; and *Re Smylski*, 2010 ABASC 449 – might assist us in our deliberations. Although previous decisions are typically of limited assistance because of differences in the underlying facts and misconduct, we find that *Gold-Quest*, which involved a Ponzi scheme, provides some guidance as to the type and extent of sanctions to order against the Respondent.

(f) Mitigating Factors

[92] There are no mitigating factors in the circumstances here.

4. Sanction Decision

[93] For the foregoing reasons, we find it is in the public interest to order that the Respondent be permanently removed from the Alberta capital market and from positions of authority with any issuers and be permanently prohibited from acting in management or consultative capacities connected with securities market activities.

[94] Further, we find it is in the public interest to order that the Respondent be required to pay, for his contraventions of Alberta securities laws, a substantial administrative penalty. In determining the appropriate quantum, we note that section 199 of the Act contemplates an administrative penalty of not more than $1 million per contravention. We also take into account that the Club was a fraud and operated as a Ponzi scheme, that the Respondent was solely responsible for this fraudulent scheme, that the Respondent made misleading and untrue statements to induce Alberta investors to invest in the Club and that Harris was convicted in Alberta in 1983 for fraudulently operating another Ponzi scheme. We thus find that it is in the public interest to require that the Respondent pay an administrative penalty of $500 000. In our view, such an administrative penalty in conjunction with the mentioned market-access bans will provide the protection and specific and general deterrence necessary in the circumstances of this case and of the Respondent.

[95] Accordingly, considering that it is in the public interest to do so, we order that:

- under sections 198(1)(b) and (c), the Respondent cease trading in securities, and all of the exemptions contained in Alberta securities laws do not apply to the Respondent, permanently;

- under sections 198(1)(d) and (e), the Respondent resign all positions he holds as a director or officer of any issuer, and the Respondent is prohibited from becoming or acting as a director or officer (or both) of any issuer, permanently;

- under section 198(1)(e.3), the Respondent is prohibited from acting in a management or consultative capacity in connection with activities in the securities market, permanently; and

- under section 199, the Respondent pay an administrative penalty of $500 000.

C. Costs

[96] Staff also sought an order under section 202 of the Act that the Respondent be required to pay all costs of the investigation and hearing totalling $15 818.55. To that end, Staff tendered a one-page itemization of the costs incurred, in addition to supporting documentation.

[97] Counsel for the Respondent submitted that any costs order should be determined having regard to the Respondent's cooperation in the investigation – including attending at the investigation, answering all questions and providing documentation within his power – and in the hearing. Counsel contended that the Respondent was as cooperative as possible, which caused the process to be abbreviated. Staff countered that, to the extent the Respondent's cooperation, including the Harris Admissions, resulted in a shorter investigation and hearing, the Respondent has received the benefit of the lesser costs incurred by Staff.

[98] An order for payment of costs under section 202 of the Act – which is not a sanction – is a means of recovering costs incurred by the Commission in conducting enforcement proceedings related to a market participant's contravention of Alberta securities laws or conduct contrary to the public interest. A costs order is also a means by which the Commission can promote procedural efficiency in the conduct of enforcement proceedings. It is generally appropriate that, when a respondent has been found to have contravened Alberta securities laws or acted contrary to the public interest, the respondent be required to pay at least a portion of the costs of the investigation and hearing that led to such a finding or findings. In determining the quantum of a costs order, one of the factors we consider is the extent to which a respondent facilitated or impeded an efficient investigation and hearing process.

[99] The current version of section 202 of the Act and the associated section 20 of the *Alberta Securities Commission Rules (General)* (the "Rules") came into force on 31 July 2010, so the former version of section 202 of the Act and the associated sections 191.1 and 191.2 of the Rules were in force during some of the investigation undertaken. Having reviewed Staff's itemization and supporting documentation, we are satisfied that the investigation and hearing costs totalling $15 818.55 are allowable costs under the former sections as well as the current ones. Further, the total amount of costs incurred does not appear unreasonable for the investigation and hearing that occurred here.

[100] That said, we accept that the Respondent was cooperative in the investigation of the allegations against him. We also acknowledge the Respondent's cooperation in the hearing through the provision of the Harris Admissions, which contributed to a shortened hearing. Having regard to this facilitation of an efficient investigation and hearing process, we will reduce the costs order made against the Respondent by $2818.55.

[101] Accordingly, we consider it appropriate that the Respondent pay $13 000 towards the costs of the investigation and hearing, and we so order under section 202 of the Act.

V. PROCEEDING CONCLUDED

[102] On 29 April 2010 the Commission issued a temporary pre-hearing order that all trading in securities issued by the Respondent cease, that the Respondent cease trading in all securities and

that all exemptions contained in Alberta securities laws do not apply to the Respondent. This temporary order expires, by its terms, with the issuance of this decision.

[103] This proceeding is concluded.

17 March 2011

For the Commission:

"original signed by"
Kenneth B. Potter, QC

"original signed by"
Glenda A. Campbell, QC

"original signed by"
Neil W. Murphy