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A L B E R T A S E C U R I T I E S C O M M I S S I O N

In the Matter of the Securities Act (S.A. 1981, c. S-6.1, as amended)
(the 'Act")

and IN THE MATTER of

World Stock Exchange,
Thomas Kim Seto and Orest Rusnak
(the "Respondents")

REASONS FOR DECISION OF THE

ALBERTA SECURITIES COMMISSION

BEFORE: Eric T. Spink, Vice-Chair
Ian E.W. McConnan, FCA, Commission Member
Jerry A. Bennis, FCA, Commission Member

APPEARANCES: Lisa J. Rudan
for the Staff of the Alberta Securities Commission

Thomas Kim Seto
on his own behalf

HEARD: In Edmonton, Alberta
May 3-5, 1999
September 3, 1999

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1. INTRODUCTION

This is a hearing under sections 165 and 167.1 of the Act. It deals with allegations contained in a Notice of Hearing dated October 6, 1998.

The first appearance in this matter was on October 22, 1998. At that time, all three respondents were represented by the same counsel. That counsel subsequently ceased to act and, after several adjournments, the hearing of this matter was scheduled for May 3-7, 1999.

On April 20, 1999, the respondent Orest Rusnak brought an application to have the proceedings against him heard separately from the proceedings against the other respondents, and for an adjournment of the hearing scheduled for May 3-7. The Commission denied those applications. On April 22, 1999, the respondent Thomas Kim Seto ("Tom Seto") brought similar applications, which were also denied by the Commission.

When the hearing commenced on May 3, Tom Seto was the only respondent to appear. Tom Seto had been a director of the corporate respondent World Stock Exchange (or the "WSE") until he resigned sometime in March of 1999. Mr. Seto did not represent the WSE at the hearing.

Evidence was presented from May 3 through May 5, at which time proceedings were adjourned so that the parties could present written submissions. Written submissions were subsequently provided by staff and by Tom Seto, each of whom also appeared before the Commission on September 3, 1999 to elaborate on those submissions. The Commission then adjourned to consider its decision.

2. ISSUES

There are three basic issues to be decided in this matter:

- Was Orest Rusnak a director of the WSE, as defined by section 1(e.1) of the Act?
- Did the WSE "carry on business as an exchange in Alberta", contrary to section 52(1) of the Act?
- Did the respondents trade in securities, contrary to sections 54(1) and 81(1) of the Act?

3. FACTS

The facts were largely uncontested.

(A) Origins of the World Stock Exchange

At all relevant times, Orest Rusnak and Tom Seto both resided in Edmonton, Alberta. Tom Seto described himself as a salesman, business consultant and the founder of the WSE. Orest Rusnak, a former lawyer, is president of Academy Financial Planners & Consultants Inc. ("Academy Financial"). The letterhead of Academy Financial says, "International Business, Legal & Financial Consulting".

In September or October of 1997, Tom Seto came up with the idea of setting up an Internet stock exchange. He discussed the idea with Orest Rusnak, who prepared most of the written material relating to the WSE, with editorial input from Tom Seto. Mr. Rose, an Edmonton businessman, also provided some comments on the material.

At that time, there was no formal organization to the WSE. Tom Seto described Mr. Rose as an "extremely competent and conscientious type businessman" whose advice he respected. Tom Seto described Orest Rusnak's role with the WSE "basically as a consultant and advisor, and in some ways a friend and business cohort".

In late October of 1997, Tom Seto registered a domain name (worldstock.com) and opened a website under the name "World Stock Exchange on the Internet". A website is a collection of web pages stored on a single computer that is connected to, and accessible through, the Internet. The WSE website was stored on and accessible through an Internet service provider whose computer was located in Edmonton, Alberta.

At that time, the website was still under construction and, although it is clear that no companies were then listed, the website included information on how a company could become listed on the WSE. Not all the information on the website was consistent, but it appeared to include a requirement that the listing company purchase shares in the WSE. A printed copy of the website as it existed on November 5, 1997 was entered in evidence.

By November 5, 1997 Commission staff had learned of the website and issued an Investigation Order pursuant to section 28 of the Act. On November 10, 1997 a Commission investigator, Mr. Kimak, met with Tom Seto and advised him to "take the website down" pending further investigation. Tom Seto removed everything except the title page, and advised Mr. Kimak that he was going to the Cayman Islands the next day to set up the website there.

On November 11, 1997, Tom Seto, Orest Rusnak and Mr. Rose went to the Cayman Islands. On that trip, WSE was incorporated in the Cayman Islands, as were Valle Los Reyes Island Resort Ltd. ("Valle Los Reyes") and Canroc International Ltd. ("Canroc"), two of the companies to be listed on the WSE.

Tom Seto was named as a director of WSE. Mr. Rose was, as he described it, "a director and the nominal president". According to Mr. Rose, Orest Rusnak was essentially running the

show during their time in the Cayman Islands, while Mr. Rose Asort of toddled around behind everybody". Mr. Rose resigned his positions with the WSE in May 1998 because, as he described it:

> I was concerned that Orest Rusnak was doing some things, and even though I was nominal president and director I wanted to know what was going on. And I didn't know that our website had been shut down, I didn't know that our lawyer had ceased to act for us and things like that that had to do with this problem with the Cayman Stock Exchange and with the government getting on our case. And a month had gone by and Orest who had all of this information didn't pass it on to me. I thought there is no communication here and, therefore, I can't be left in a position where I am a director of a company and I don't know what is happening. So that is when I resigned.

The WSE website was stored on and accessible on the Internet through a computer located in the Cayman Islands for some time. The Cayman Island authorities had some problems with the WSE website and, as Mr. Rose described it, "the government, the police shut it down". The WSE website was then moved to a computer located in Antigua. Mr. Kimak downloaded a copy of the Antigua website as it existed on September 28, 1998 and the printed version of that was entered in evidence.

(B) Soliciting listings for the WSE and other activities of the respondents

Orest Rusnak and Tom Seto both solicited a number of Albertans and Alberta companies to raise money on the WSE. The Commission investigator, Mr. Kimak, testified that "somewhere between 30 and 40 people were engaged in conversations concerning the WSE and concerning the possibility of getting listed on the WSE", all of whom were Alberta residents. According to Mr. Kimak, every one of those people who discussed the WSE with either Orest Rusnak or Tom Seto was told about the WSE website.

Everyone understood that, in order to become listed on the WSE, companies had to be incorporated "offshore", which apparently meant in the Cayman Islands or another similar jurisdiction.

The November 1997 trip to the Cayman Islands was financed by Mr. Wall, a retired businessman residing in Edmonton. Mr. Wall paid $16,500 to Orest Rusnak, for which he expected to have Valle Los Reyes incorporated in the Cayman Islands and listed on the WSE. He also expected to receive shares in Valle Los Reyes and in the WSE. Mr. Wall understood that Tom Seto, Orest Rusnak and Mr. Rose were the directors of the WSE. Orest Rusnak passed the $16,500 to Tom Seto, who used it to obtain travelers cheques for himself and Orest Rusnak. All the money was spent during the trip to the Cayman Islands.

Mr. Ziegler, president of an Alberta company, was contacted by Tom Seto in March 1998. Tom Seto told him about the WSE website and offered to help him "raise capital in a public venue". They discussed the $5,000 listing fee for the "Speculative Trading Board" on the WSE, and were negotiating a "Management Agreement" whereby Tom Seto would, among other things, "prepare an Offering Memorandum...for listing on the WSE".

Mr. Ziegler wanted Tom Seto to raise $200,000 for the company. They discussed the possibility of listing Mr. Ziegler's company on other exchanges or the OTC Bulletin Board in the U.S., but "narrowed it down to the WSE because of the cost of the other exchanges". Mr. Ziegler was not asked to purchase shares in the WSE and he stopped dealing with Tom Seto after talking to Commission Staff.

Mr. Lalsin, principal of an Alberta company named Lombard Developments Inc., first met Orest Rusnak sometime late in 1997. Mr. Lalsin wanted to raise capital. Orest Rusnak suggested the WSE, and told Mr. Lalsin that he was a "partner in the WSE". Mr. Lalsin asked Orest Rusnak several times whether he was a director of the WSE, but never received an answer.

On January 21, 1998, Orest Rusnak sent a proposal to Lombard Developments Inc. through Mr. Lalsin's lawyer. The covering letter and proposal are both on Academy Financial letterhead. The covering letter describes the WSE, gives its website address, and advises that the WSE Ais currently setting up an information site that will be listed on all the search engines, which domain address is: worldstock.com".

The proposal is entitled "INTERNATIONAL FINANCING FOR LOMBARD WORLD HOUSING CORPORATION through the WORLD STOCK EXCHANGE". It says, in part:

> 1. That you will retain my services to incorporate LOMBARD WORLD HOUSING CORPORATION in the Cayman Islands and then to prepare and file the proper documents to list this company on the WSE in the Cayman Islands.
>
> 2. That in addition to the estimated disbursements of $10,000 to complete the above services, you have agreed to pay me compensation for my services in the amount of $5,000 plus 2% of the shares issued to the promoters in the above company….
>
> 5. That the Offering Memorandum to be filed with the WSE will be organized to raise a total of $15 million (U.S. Funds). It is proposed that these funds will be raised in three separate stages to enhance the promotional efforts for the company [$5 million in each stage, at issue prices of $1.00, $2.00 and $3.00 per share]….

> The time frame for completing the set-up of this program to the stage of having the shares listed on the World Stock Exchange and ready for trading would be approximately 2 weeks. During that time, the promotion of the company can be launched to arrange interested investors. It is my assessment that this project should proceed immediately as the circumstances are ideal to create the necessary excitement to generate the initial capital required in a short time frame.

Mr. Lalsin signed and accepted the proposal. On January 27, 1999 he paid $10,000 to Academy Financial, which he understood to be the listing fee for the WSE. The listing fee quoted on the WSE website was $15,000 (U.S.), but Mr. Lalsin told Orest Rusnak:

> I said like we are going in as a guinea pig on these things and I wasn't going to give him the $15,000, we would give him the ten. Plus, they were getting a piece of the company.

Lombard World Housing Corporation ("Lombard") was incorporated in the Cayman Islands on February 13, 1998, and listed on the WSE some time later. Mr. Lalsin understood that prospective investors would be able to locate the WSE through search engines, that investors could purchase shares through the WSE and that the WSE would take a percentage of the money coming to Lombard from investors. Mr. Lalsin said that The WSE initially wanted 10%, but he negotiated this down to about 5% with Orest Rusnak and Tom Seto.

Mr. Lalsin was not asked to purchase shares in the WSE. Tom Seto indicated that the WSE only received $5,000 of the $10,000 paid by Mr. Lalsin to Academy Financial.

(C) Contents of the WSE website

We have two snapshots of the contents of the WSE website: one from November 5, 1997, when the website was stored on a computer in Edmonton (the "Edmonton website"); and one from September 28, 1998, when the website was stored on a computer in Antigua (the "Antigua website"). Each website contained a large amount of information, not all of which was consistent. Some of that information is described below.

(i) general descriptions of the WSE

Under the heading "How the WSE Operates", the Antigua website says, in part:

What Security Regulations control the listing of companies?

The World Stock Exchange was incorporated and established in a manner that ensures that it does not fall under the Securities Regulations of any country. Only the regulations and policies of the World Stock Exchange control the listing of companies on the various Trading Boards of the World Stock Exchange.

The World Stock Exchange was established on the principle that its role is simply to provide a mechanism for full disclosure of relevant financial information for each company listed. It is up to the investors to review the information filed in the Company's web page and to decide whether to invest in the company. There are no standards or regulations that preclude any company from being listed, but companies are distinguished by the Administrator of Filings based on the length of business operations and assigned to specific Listing Boards. Furthermore, Warning Handles are attached to companies where there is relevant information which poses a risk to prospective investors.

Aside from requiring the listing companies to provide full disclosure, making the information easily accessible to interested investors, and requiring the company's directors, lawyer and accountant accessible [sic] for information on the company, the World Stock Exchange does not interfere with the rights of investors to invest in any company. The recourses of investors to sue the company and its directors for providing false or misleading information remains the only recourse of the investors (similar to all other jurisdictions).

Where is the World Stock Exchange Situated?

The World Stock Exchange is incorporated offshore in a tax free haven. The server for the web site of the World Stock Exchange is located offshore, and all financial transactions are finalized through offshore banks….

NOTE: The World Stock Exchange charges fees of between 3% and 10% on buy and sell orders. Of this amount, 1% in each case will be retained by the World Stock Exchange to pay for operational costs. The World Stock Exchange may charge fees for their services that they must provide in the course of serving their customers.

The Antigua website contained detailed information about how to apply for listing on the WSE. The "Procedures for Listing" include the requirement for "Confirmed arrangements for the payment of the Filing Fees, as required, together with the further investments for the purchase of shares in the World Stock Exchange." At some places in the Antigua website, only a "Listing Filing Fee" is mentioned, but another part of the website refers to both the Listing Filing Fee and a minimum or maximum WSE stock purchase.

There were four "trading boards" on the WSE:

- speculative ("for start up companies with no proven record of earnings");
- growth ("for companies that have a minimum of two years research or activity");
- established ("for companies with three years of profitable operations"); and
- blue chip ("for companies with five years of profitable operations").

The Antigua website shows three listed companies on the WSE, Valle Los Reyes and Canroc on the "growth" trading board and Lombard on the "established" trading board. Each of these companies was recently incorporated in the Cayman Islands, and the operations of each were apparently conducted through what are described as subsidiary or affiliate companies. Canroc had a subsidiary company in Alberta. Lombard had an affiliate company in Alberta. Valle Los Reyes had a subsidiary company incorporated in Costa Rica.

Each listed company had its own web page on the Antigua website containing information relating to the company. For Valle Los Reyes and Canroc, there was a certificate of incorporation, a "lawyer's letter", an "accountant's letter", an "offering memorandum", and each company's application for listing on the WSE. Lombard's web page contained everything except the accountant's letter, plus additional information on Lombard including its own website and the address of the company's president in Edmonton, Alberta.

(ii) buying and selling shares on the WSE

The Antigua website included "buttons" labeled "TO BUY/SELL SHARES CLICK HERE", and electronic forms to be filled in to buy or to sell. These forms included a "certificate" whereby the buyer or seller applied to become "registered" with the "ISBC", which is identified elsewhere on the website as the International Stock Brokerage Corporation. It appears that the ISBC would act as some type of designated agency for the WSE, and the website notes:

> There are NO stock certificates issued for any companies listed exclusively on the World Stock Exchange, and the records and letters of confirmation (which, if desired, include an electronically generated share certificate to be used for record purposes only) by the International Stock Brokerage Corporation will be the only proof of ownership.

Staff testified that the ISBC is not registered under the Act. In his evidence, Mr. Rose indicated that "the brokerage company that we had hadn't been incorporated". The only other evidence about the ISBC appears on the Edmonton website, where there are several pages of material under the title: ***"HOW TO BECOME AN INDEPENDENT STOCK BROKER".*** Some of that material says:

> ***This may seem impossible ... but it isn't:***
>
> Have you ever thought about becoming a Stock Broker? Perhaps in the area where you reside, it is too difficult because of the regulations. However, in the international financial market, this opportunity is now suddenly available to you if you meet the right qualifications. It's easier than you may imagine, so give this your careful consideration.
>
> ***Opportunity knocks…***
>
> With the appearance of the World Stock Exchange on the Internet, a new era in the financial markets of the World has started. We are entering the 21st Century with a feeling that anything is possible and that new ideas will create a better lifestyle for everyone. These new ideas and businesses require capital, which is becoming increasingly more difficult to find in the conventional marketplace. For that reason, the World Stock Exchange on the Internet is positioned to become the new leader in International Finance.
>
> Because the World Stock Exchange is simply a financial registry, the actual trading of stock must take place through a Brokerage House. The specific Brokerage Company that is licensed by contract to execute all the trades

(whether buy or sell) on the Four Trading Boards on the World Stock Exchange is: INTERNATIONAL STOCK BROKERAGE CORPORATION. This company is incorporated in the Cayman Islands and has its main office there.

The International Stock Brokerage Corporation is now licensing independent stock brokers who will have the exclusive authority to submit the buy and sell orders and to earn a commission for any trades executed on behalf of their clients….

What are the Qualifications for becoming licensed as an Independent Stock Broker:

The INTERNATIONAL STOCK BROKERAGE CORPORATION has the following qualifications for becoming an Independent Stock Broker, namely that every applicant must fall into one of the four following categories, either:

(a) The applicant was worked (either part time or full time) in the stock brokerage or investment field as either a broker or an investor, and therefore knows investors who regularly purchase stock on public stock exchanges;

(b) The applicant has the basic knowledge of the stock investment or financial investment field and has developed a list of potential investors who regularly purchase stock on public stock exchanges;

(c) The applicant has worked in the sales field exclusively for at least one year and has developed a list of potential investors who may wish to purchase stock on a public stock exchange;

(d) The applicant has unique qualities that would be ideal for this type of career and the applicant has developed a list of potential investors who may wish to purchase stock on a public stock exchange;

Qualified applicants were required to pay a "one-time licensing fee" of $1,000 and annual renewal fees of $100 (U.S.). Once licensed, Independent Stock Brokers could "earn as much money as you want based on the following commission structures". The commission fees could be set by the Independent Stock Broker anywhere from 3% to 10% of the buy or sell transaction, of which 1% must be paid to the WSE, the balance up to 7% would be split between the Independent Stock Broker and the ISBC, and any commission over 7% would go entirely to the Independent Stock Broker. Also, the Independent Stock Broker would "receive 10% of the listing fee for any new companies he introduces to the World Stock Exchange". Applicants were advised to courier the necessary documents and fee to ISBC in the Cayman Islands, whereupon:

> Your application will be processed within one week and you will be notified of your acceptance. ….You will receive an official and impressive certificate which should be framed and displayed in your place of business. You will then be licensed and ready to begin your career as an independent Stock Broker.

(iii) offering memorandums of listed companies

Although both websites appeared to contemplate secondary trading in the shares of WSE listed companies, it is clear that primary distributions were the immediate focus of the WSE. Each listed company's "offering memorandum" described how much money the company proposed to raise through the sale of shares. All figures are specified as U.S. funds.

Valle Los Reyes and Canroc (the two companies on the "growth" trading board) proposed to raise $2,000,000 and $500,000, respectively, by selling shares at "a discounted sale price of $0.50 per share". In addition, a further 600,000 and 400,000 shares already issued to the president of each company would also be sold at the same price "to repay the financial investment of [the president]". Each offering memorandum went on to say that the shares "will be listed for trading at an initial trading price of $1.00 per share".

Lombard (the company on the "established" trading board) proposed to raise a total of $38,000,000 in four issues from treasury priced at $1.00, $2.00, $3.00 and $4.00. Its offering memorandum said that "on the completion of this share offering, the Company's shares will be listed for trading at an initial trading price of $5.00 per share".

In each case, the company agreed to pay sales commission of 10% on the sales of shares from treasury.

(iv) disclosure of financial information

As noted above, the WSE said "its role is simply to provide a mechanism for full disclosure of relevant financial information for each company listed", yet there were no financial

statements available on the Antigua website. The website contained considerable narrative financial information, described below.

The "accountant's letter" for Valle Los Reyes says:

> Enclosed with this letter are the Financial Statements for the company, which includes the Balance Sheet and the projected Revenue Statement for this company. We have conducted a review of these Financial Statements and have satisfied ourselves that they have been prepared in a professional manner and in accordance with generally accepted accounting principles. Our concerns with these financial statements, if any are noted in our reports attached to the financial statements….
>
> Our Accounting department has further conducted an assessment of all pertinent risks for investors in the Company, and these risks are noted in the Financial Statements and are specifically summarized herein, namely:
>
> ***Valle Los Reyes Island Resort Ltd. having been recently incorporate,*** [sic] ***does not have an established record or earnings and financial performance against which the corporation can be evaluated.***

The "offering memorandum" for Valle Los Reyes says, under the heading "FINANCIAL STATEMENT FOR THE COMPANY":

> 1. The financial statements for the business Mar-Y-Sol Island Beach Resort have been developed from the estimations of the owner, and together with the projections of future revenues and profits, has been filed, and are available upon request of any shareholder or interested investor, by contacting the accountant of the Company.
>
> 2. The current Balance Sheet for the Company has been filed, and are available upon the request of any shareholder or interested investor, by contacting the accountant of the Company.
>
> 3. None of these financial statements are audited or in any way verified by the Accountant of the Company, and are simply based on the estimations

> provided by the previous owner. These financial statements have been provided simply for the information of any interested parties.

The application for listing of Valle Los Reyes includes the following question and answer:

> If [the company has operated its business] more than one year, does the company have financial statements?
>
> > No! These were destroyed in a recent fire of the facility. However, projected income statements for the future re-developed project, based on the former business, have been provided.

The "accountant's letter" for Canroc says:

> Enclosed with this letter are the Financial Statements for the company together with copies of the filed tax assessments for the period of N/A years.

The "offering memorandum" for Canroc says:

> There are no financial statements for the business of the subsidiary company, but projections of future revenues and profits have been prepared for the Corporate business planning [sic] and are available upon request of any shareholder or interested investor, by contacting the accountant of the Company.

Except for the differences in the sections quoted above, the "accountant's letters" for Valle Los Reyes and Canroc are otherwise very similar, and both are signed by Ralph Michael Gerndt. The evidence suggested that Mr. Gerndt was an employee of Peter Labant, the president of Canroc, and that Mr. Gerndt does not have a recognized accounting designation.

The "accountant's letter" for Lombard was a fill-in-the-blanks form letter addressed to the WSE at an address in Edmonton, Alberta to the attention of the "Administrator of Filings". The blanks on the form are not completed and it makes no mention of Lombard. Tom Seto testified that he was the WSE's "Administrator of Filings".

The Lombard "offering memorandum" says, under the heading "FINANCIAL

STATEMENT FOR THE COMPANY":

> 1. The financial statements for the business of the Affiliate company, which include projections of future revenues and profits, have been prepared for the Corporate business planning [sic] and are available upon request of any shareholder or interested investor, by contacting the accountant of the Company.
>
> 2. The current Balance Sheet for the Company has been filed, and are available upon the request of any shareholder or interested investor, by contacting the accountant of the Company.
>
> 3. None of these financial statements are audited or in any way verified by the Accountant of the Company, and are simply based on the records maintained by the Affiliate of the Company. These financial statements have been provided simply for the information of any interested parties.

(v) other promotional material on the WSE website

The Antigua website includes a section entitled "Companies being considered for listing on the WSE". This section has brief descriptions of eight companies, including Canroc. All the descriptions appear to be implausibly promotional.

For example, the "Cayman Islands Tax Free Mutual Fund" projects a 25% return to investors, with a guaranteed 10% annual dividend for investors "without fear of taxation in their resident jurisdiction". Canroc is described as having two mining claims with "proven reserve values" of approximately $800,000 and Canroc is said to be planning to "continue a testing program for gold and diamonds on these properties, which currently show favorable prospects". The description of "Golden Eagle International Inc." says:

> This company is to be a re-organized company to be incorporated offshore for raising capital to develop real estate in Canada. Because Canada is rated as the best country in the world to live and has a high standard of living, real estate developments have shown great opportunity in recent years. This company will focus on developments that will guarantee a spectacular return for its investors.

The "Offering Memorandum" for Valle Los Reyes includes a special incentive for "Founding Investors" who purchase shares in the amount of $10,000 or more. It says:

> Furthermore, each Founding Investor shall qualify to receive a FREE one-week timeshare to stay at the Hotel Resort of the Company, upon payment of a one-time administration fee of $500.00 (U.S. Funds). Each timeshare Unit is valued at $5,000.00 (U.S. Funds) or more and is a flexible booking timeshare which extends for a period of 25 years and is subject only to the time-share rules of the Company. The time-share Unit can also be used by the Founding Investor as a down-payment on any future villas or condominiums developed by the Company.

Presumably, this refers to the same "Hotel Resort" that was damaged by fire and which Valle Los Reyes proposes to redevelop using the proceeds of this offering.

(D) Accessibility of the WSE website

According to Mr. Kimak, the WSE website was accessible through Internet search engines for a "very brief moment" in July of 1998. Otherwise, it would be necessary to know the name in order to access the website. Anyone who knew the domain name had access to the website, which was apparently still running shortly before the hearing.

(E) Regulatory matters

The WSE was not recognized as an exchange by the Commission. Neither the WSE, nor any of its listed companies, filed a prospectus with the Commission. None of the respondents were registered under the Act. It was not suggested that any statutory exemptions applied.

4. ANALYSIS AND FINDINGS

(A) Was Orest Rusnak a director of the WSE, as defined by section 1(e.1) of the Act?

Orest Rusnak was not formally a director of the WSE. The issue is whether he meets the definition of "director" in section 1(e.1) of the Act, which "includes a person acting in a capacity similar to that of a director of a company."

(i) principles applicable to this issue

The principles applicable to this issue were addressed by the Commission in *Re Press* (1998), 7 A.S.C.S. 2178, where the Commission stated (at pp. 2182-3):

In our view, the purpose of the broad definition in the Act is the same as in corporate statutes. We agree with the discussion in *Canadian Business Organizations Law,* T. Haddon, R. Forbes and R. Simmonds (Toronto: Butterworths, 1984) at 196:

> In the *Canada Business Corporations Act* and similar statutes (including the Alberta Business Corporations Act), there is a provision stating that a director is "a person occupying the position of director by whatever name called". The purpose of this provision and of equivalent provisions in other jurisdictions is to prevent those who exercise the powers of a director from seeking to avoid their liabilities as such by arranging for others to fill the formal positions on the board of directors without diminishing their effective control over the affairs of the company. [footnotes omitted]

As described in s. 97(1) of the *Alberta Business Corporations Act*, the function of a director is to "manage the business and affairs of a corporation". A "de facto director" was defined in *Canadian Aero Services Ltd. v. O'Malley* (1969), 61 C.P.R. 1 (Ont. H.C.J.) at 15 as "...one who intermeddles and who assumes office without going through the legal formalities of appointment".

The British Columbia Securities Commission has considered this same issue several times, finding individuals to have been de facto directors in *Re Vancouver Stock Exchange Rules and Bylaws; "Atra Resources Ltd.*(1993), B.C.S.C. Weekly Summary 93:22, p37; *Re Metaxa Resources Ltd.* (1995) B.C.S.C. Weekly Summary 95:16, p. 115; and *Re Pinchin* (1996), 12 C.C.L.S. 24. In these cases, the B.C. Commission considered it relevant that the various de facto directors did one or more of the following:

- appointed nominees as directors;
- were responsible for the supervision, direction, control and operation of the company;

- ran the company from their office;
- had signing authority over the company's bank account;
- negotiated on behalf of the company;
- were the company's sole representative on a trip organized to solicit investments;
- substantially reorganized and managed the company;
- selected the name of the company;
- arranged a public offering;
- made all significant business decisions.

The Commission found that Mr. Press was a director because he was actively and directly involved in key aspects of the company's business. In each case, it is the entirety of the alleged director's involvement that must be considered in the context of the company's activities. No individual factors are necessarily determinative. The test is whether, under the particular circumstances, the alleged director is an integral part of the mind and management of the company.

(ii) evidence of Orest Rusnak's role with the WSE

In considering Orest Rusnak's role with the WSE, we must examine the evidence of his involvement in the context of the WSE's overall activities and the roles of its named directors.

At the time the WSE was incorporated in the Cayman Islands, Mr. Rose understood his own role as president and director to be nominal, not functional. He said there were no formal directors' meetings. Mr. Rose indicated that it was Tom Seto and Orest Rusnak who ran the business of the WSE. He eventually resigned his nominal positions with the WSE because he was concerned about things that Orest Rusnak was doing and about Orest Rusnak not keeping him informed of developments with the WSE's business and operations.

Tom Seto described the formal relationship between the WSE, himself, Orest Rusnak and Mr. Rose in the following terms: "we never came to anything totally definitive and it was kind of like, well, we'll see what happens". When asked specifically about Orest Rusnak's position with the WSE in the long run, Tom Seto said that it "was never really spelled out exactly as to how he was going to fit in". It is clear that the formal organization of the WSE had little connection with its actual operations, which were conducted on a remarkably informal basis.

Orest Rusnak made most of the corporate and business arrangements for the WSE in the Cayman Islands. Every listing on the WSE came through Orest Rusnak. He also wrote most of the content of the WSE website. Tom Seto and Mr. Rose provided editorial comments on that material but it is clear that Mr. Rose's involvement was negligible and Tom Seto admitted

having very limited experience with public companies. We find that it was Orest Rusnak who primarily determined how the WSE would be set up and how it would operate.

Although Tom Seto variously described Orest Rusnak as providing legal advice or consulting services, the evidence does not support the proposition that Orest Rusnak provided independent services to Tom Seto or the WSE. Orest Rusnak did not submit any invoices for his services. The WSE never had an operating bank account, nor was there any accounting for the money it received or spent, but the evidence shows that Orest Rusnak received money from Tom Seto in a manner that we find most consistent with some kind of partnership arrangement. As Tom Seto described it, "I believe it was kind of like, well, you know, I need some money and here it is and if I had it I gave it to him. This whole thing started pretty well on a shoestring." The evidence showed that the initial $16,500 received from Mr. Wall was divided between and spent by Tom Seto and Orest Rusnak on their trip to the Cayman Islands. Later, when Orest Rusnak received a $10,000 listing fee from Mr. Lalsin, he paid only $5,000 over to Tom Seto.

Mr. Lalsin said that Orest Rusnak told him that "he was acting on behalf of the WSE and he was a partner in the WSE", and all of Mr. Lalsin's extensive dealings with Orest Rusnak were consistent with that. It is significant that Orest Rusnak, by not answering Mr. Lalsin's several inquiries as to whether he was a director of the WSE, did not deny that he was a director. It is also significant that Orest Rusnak negotiated a reduced listing fee for Mr. Lalsin's company without consulting Tom Seto, and that Mr. Lalsin did not know of or meet Tom Seto until after the listing fee had been paid and the listing process was well underway.

Mr. Wall, who dealt directly with Orest Rusnak in relation to the listing of Valle Los Reyes on the WSE, testified that he understood that Orest Rusnak was a director of the WSE.

(iii) conclusion

We find that Orest Rusnak was a director of the WSE. In our view, he was clearly an integral part of the mind and management of the WSE. By normal standards the WSE did not have much in the way of formal management but what it did have certainly involved Orest Rusnak. We find that Orest Rusnak deliberately avoided any formal corporate role with the WSE and that he deliberately concealed that fact from Mr. Lalsin by telling him the colloquial truth: that he was a partner in the WSE.

(B) Did the WSE "carry on business as an exchange in Alberta", contrary to section 52(1) of the Act?

Section 52 of the Act says:

> **52**(1) No person or company shall carry on business as an exchange in Alberta unless the person or company is recognized by the Commission as an exchange.

> (2) The Commission may, on the application of a person or company proposing to carry on business as an exchange in Alberta, recognize the person or company as an exchange if the Commission considers that it would not be prejudicial to the public interest to do so.
>
> (3) The recognition of an exchange under this section shall be made in writing and is subject to any terms and conditions that the Commission may impose.

We were referred to no decisions interpreting section 52 or any of the similar provisions in other provinces' securities legislation.

Staff urged the Commission to adopt a broad interpretation of "carry on business as an exchange in Alberta" for enforcement purposes, suggesting that it might encompass any exchange activity occurring in Alberta. Such a broad interpretation of section 52(1) may, however, be inconsistent with the way these provisions have actually been applied to exchanges until now.

At the time of the hearing, the Alberta Stock Exchange ("ASE") was the only exchange recognized by the Commission under this section. During the hearing, a re-structuring of Canadian stock exchanges was announced and, recently, the ASE and the Vancouver Stock Exchange ("VSE") merged to form the Canadian Venture Exchange ("CDNX"). CDNX was recognized as an exchange by the commissions in both Alberta and British Columbia on November 26, 1999. In this decision, we generally refer to the ASE, VSE and other exchanges as they were prior to the restructuring.

It is an historical fact that section 52 has never been applied to exchanges, such as the VSE, that are recognized elsewhere or are otherwise subject to a regulatory scheme comparable to that in Alberta, but are not recognized in Alberta. We will call these "regulated exchanges". This category would clearly also include the Toronto Stock Exchange ("TSE"), the Montreal Exchange and a number of foreign exchanges such as the New York Stock Exchange. Regulated exchanges may be distinguished from those exchanges that are recognized in Alberta such as the ASE, and now CDNX, which we will refer to as "recognized exchanges".

It is easy to see why, historically, section 52 of our Act and the equivalent provisions in other provinces applied only to the "local" exchange. The ASE, like most other stock exchanges, existed long before the advent of the modern Canadian Securities Acts. In Alberta, a provision similar to section 52(1) first appeared in *The Securities Act*, 1967. At that time, the ASE and other exchanges each operated a physical trading floor. The location of the trading floor was an obvious indicator of where the exchange carried on business.

Since then, the exchange business has changed dramatically. Trading floors have disappeared and have been replaced by computer systems. As these proceedings demonstrate, modern technology gives almost anyone the operational capacity to set up a new type of exchange. That raises important issues about whether and how the law applies to such exchanges.

Tom Seto argued that the WSE's trading-floor equivalent is located either in "Cyberspace, or Antigua where the correspondence is received, or where the transaction is completed, the Cayman Islands". He argued that the WSE should be subject to regulation only by its incorporating jurisdiction, the Cayman Islands.

Tom Seto urged the Commission to compare the activities of the WSE to those of regulated exchanges like the VSE and TSE, which actively and successfully solicit listings in Alberta. Tom Seto argued that, since the Commission does not apply section 52(1) to the VSE and TSE, they are not carrying on business as an exchange in Alberta, so the less extensive activities of the WSE in Alberta cannot reasonably be construed as carrying on business here.

Tom Seto indicated that he intends to carry on with the WSE and, apparently, market it on the basis of the WSE's lack of regulation and low listing cost in relation to other exchanges. He suggested in argument that "the [Alberta Securities Commission] should not be held in greater esteem than myself in making regulations as a securities regulator".

The essence of Tom Seto's position is that the WSE is not subject to section 52(1) of the Act. As Tom Seto's arguments suggest, there is no question here about whether the WSE meets Alberta's regulatory standards. It does not. It falls far below the standards imposed on exchanges recognized by Alberta or by any other major commercial jurisdiction. The WSE appears to accept that, because it does not attempt to meet those standards and it freely admits taking deliberate steps to avoid such rigorous regulation. The WSE wants to be an "unregulated exchange", by which we mean an exchange that is not recognized or otherwise subject to a regulatory scheme comparable to that in Alberta. The fundamental question here is whether the WSE, as an unregulated exchange, is subject to section 52(1) of the Act.

Due to the lack of existing authority on this issue and the range of potential consequences that may flow from our interpretation of section 52(1), we must undertake a comprehensive analysis of this provision before attempting to apply it to the particular circumstances of the WSE.

(i) is the WSE an "exchange"?

Although Tom Seto did not dispute staff's allegation that the WSE was an exchange, it is useful to review current developments relating to this question. "Exchange" is not defined in the Act. It is clear that traditional exchanges like the ASE are examples of exchanges but that does not provide much guidance in determining whether less traditional organizations are exchanges.

The functional characteristics of exchanges are described in proposed National Instrument 21-101 *Marketplace Operation* ("NI 21-101") and Companion Policy 21-101CP. These were published for comment by the Commission on July 2, 1999 at (1999), 8 A.S.C.S. 1830. NI 21-101 and Companion Policy 21-101CP are intended to regulate all marketplaces operating within any Canadian jurisdiction including exchanges, quotation and trade reporting systems, and alternative trading systems ("ATSs"). Section 1.1 of NI 21-101 defines "marketplace" to mean:

> (a) an exchange,
>
> (b) a quotation and trade reporting system, and
>
> (c) any other person or company that
>
> > (i) constitutes, maintains or provides a market or facilities for bringing together purchasers and sellers of securities,
> >
> > (ii) brings together the orders for securities of multiple buyers and sellers, and
> >
> > (iii) uses established, non-discretionary methods under which the orders interact with each other, and the buyers and sellers entering the orders agree to the terms of a trade.

Section 3.1(2) of Companion Policy 21-101CP says, in part:

> The Canadian securities regulatory authorities generally consider a marketplace to be an exchange for purposes of securities legislation, if the marketplace
>
> (a) requires an issuer to enter into an agreement in order for the issuer's securities to trade on the marketplace, *i.e.*, the marketplace provides a listing function;

Although these provisions are not authoritative in this proceeding, we find that they accurately describe the defining functions of an exchange that are applicable regardless of the exchange's other physical, organizational or technological characteristics. It is not necessary for us to explore the limits of the definition because the WSE falls squarely within them.

The WSE actually provided a listing function and a market or facilities for bringing together purchasers and sellers of securities. It set non-discretionary methods for trading. The fact that no one actually bought or sold securities through the WSE means that we do not know

whether the WSE actually had the capacity to consolidate orders of multiple parties, but it clearly wanted to. We find that the WSE is an exchange within the meaning of the Act.

(ii) what is "carrying on business as an exchange in Alberta"?

The interpretation of this phrase is the most difficult issue raised by these proceedings. There is apparently no authority that deals directly with the question of what constitutes carrying on business as an exchange.

(a) case law interpreting the phrase "carrying on business"

The Commission was referred to a number of cases interpreting phrases similar to "carry on business", but none of those cases involved provisions that were directly comparable to section 52.

For example, we were referred to *Success International Inc. v. Environmental Export International of Canada Inc.* (1995), 23 O.R. (3d) 137 (Gen. Div.). That case dealt with the issue of whether a New York company carried on business in Ontario within the meaning of section 1(2) of the Ontario *Extra-Provincial Corporations Act*. The court held that the phrase should be broadly interpreted.

There are also a number of cases discussing this phrase and concept in the context of taxation. These are examined in an article by C. A. Kyres, "Carrying On Business in Canada" (1995), vol.43, no. 5 *Canadian Tax Journal*, p. 1629. These cases tend to adopt a more restrictive interpretation as exemplified by the House of Lords decision in *Grainger and Son v. Gough (Surveyor of Taxes)*, [1896] A.C. 325.

In our view, these cases demonstrate that the words "carry on business" are capable of either a broad or narrow interpretation depending upon the legislative context in which they appear, but these cases are not particularly useful to show the meaning of the phrase in the context of section 52(1).

We were also referred to a number of cases and articles dealing with the question of whether courts had personal jurisdiction over parties to deal with civil claims, including some involving claims arising out of Internet transactions or communications. The cases include: *Alteen v. Informix Corp.* (1998), 21 C.P.C. (4th) 228 (Nfld. S.C.T.D.); *Braintech, Inc. v. Kostiuk*, [1999] B.C.J. No. 622 (B.C.C.A.); *Zippo Manufacturing Company v. Zippo DotCom, Inc.* 952 F.Supp. 119 (W.D.Pa. 1997); *Bensusan Restaurant Corp. v. King*, 126 F.3d 25 (2d Cr. 1997); *Asahi Metal Industry, Inc. v. Superior Court of California, Solano County* (1987), 480 U.S. 102; and *Inset Systems, Inc. v. Instruction Set, Inc.*, 937 F.Supp. 161 (D.Conn. 1996). The articles include: B.A. Slutsky, "Jurisdiction Over Commerce On The Internet" (1997) http://www.kslaw.com/menu/jurisdic.htm; W.D. Facon, Jr., "A Nice Place to Visit, But I

Wouldn't Want to Litigate There: The Effects of *Cybersell v. Cybersell* on the Law of Personal Jurisdiction" (1999) 5 Rich. J.L. & Tech. 7; M.R. Kravitz, "Sum & Substance: A Virtual Presence" (1997) http://www.courttv.com/news/422f.html; and D.F. Hernandez and D. May, "Personal Jurisdiction and the Net: Does Your Website Subject You to the Laws of Every State in the Union? (1996) http://www.gseis.ucla.edu/iclp/dhdm.html.

In our view, these cases and articles are not relevant to the matter before us because the issues relating to personal jurisdiction over civil claims are fundamentally different than the issues here, where we are concerned with the question of whether or not a specific statutory provision, section 52(1), applies to the WSE.

(b) purposive analysis of section 52(1)

In order to properly interpret section 52, we follow the purposive approach to statutory interpretation as described in *Driedger on the Construction of Statutes*, 3rd ed. by R. Sullivan (Toronto and Vancouver: Butterworths, 1994) ("Driedger"). According to Driedger, the purposive approach may be summarized by the following propositions (at p. 35):

> (1) All legislation is presumed to have a purpose. It is possible for courts to discover, or to adequately reconstruct, this purpose through interpretation.
>
> (2) Legislative purpose should be taken into account in every case and at every stage of interpretation, including the determination of ordinary meaning.
>
> (3) Other things being equal, interpretations that are consistent with or promote legislative purpose should be preferred and interpretations that defeat or undermine legislative purpose should be avoided.
>
> (4) The ordinary meaning of a provision may be rejected in favour of an interpretation more consistent with the purpose if the preferred interpretation is one the words are capable of bearing.

Driedger describes how various factors have prompted the modern emphasis on purposive analysis, and that one factor deserving special attention is the growth of "program legislation". In our view, the Act is an example of such program legislation. Driedger describes program legislation as follows (at pp. 42-3):

> Program legislation is the type of legislation on which the modern administrative state is founded. It addresses a large social or economic problem by establishing a program of regulation...and creating a department

or other body to administer it. In program legislation the starting point is not existing law, but an area of human activity to be regulated….
Most program legislation takes the form of a single self-contained statute setting out the goals of the program and establishing a legal framework within which delegated powers are exercised and reviewed…

The delegation of power to the executive branch is the most striking feature of program legislation. In many programs, the executive is given both the legislative role of rule-making and the judicial role of rule-application. It often becomes the primary interpreter of its own legislation. However, its exercise of power is subject to supervision by the courts. Rule-making is supervised through judicial review of the validity of delegated legislation while rule-application is supervised through judicial review of the decisions of officials and administrative tribunals. In carrying out these supervisory functions, the courts may be required to interpret both the statute and the delegated legislation made pursuant to the statute. However, even though the courts have the final say, generally they are not the primary interpreters of this legislation and their role is limited to reviewing the interpretations of others.

These distinctive features of program legislation have affected its interpretation in a number of ways:

(a) by drawing the focus away from the meaning of rules and their relation to the common law:

(b) by emphasizing the *function* of rules, in relation to the scheme set out in the legislation and its ultimate goals:

(c) by enlarging the concept of purpose from the cure of discrete social mischiefs or defects in the common law to include broad social and economic policies and long-range goals; and

(d) by fostering the development of principles for reviewing the administration of programs, including the principles of fairness and natural justice and the doctrine of curial deference. [footnotes omitted]

(c) legislative context of section 52(1)

The purpose of section 52(1) should be considered by examining it within the context of the legislative scheme of the entire Act and, more particularly, Part 4 of the Act.

The general purpose of securities legislation has been described by the Supreme Court of Canada in *Barry v. Alberta (Securities Commission*), (sub nom. *Brosseau v. Alberta (Securities Commission*)), [1989] 1 S.C.R. 301, where L'Heureux-Dubé J. stated (at p. 314):

> Securities acts in general can be said to be aimed at regulating the market and protecting the general public. This role was recognized by this Court in Gregory & Co. v. Quebec Securities Commission, [1961] S.C.R. 584 where Fauteaux J. observed at p. 588:
>
> > "The paramount object of the Act is to ensure that persons who, in the province, carry on the business of trading in securities or acting as investment counsel, shall be honest and of good repute and, in this way, to protect the public, in the province or elsewhere, from being defrauded as a result of certain activities initiated in the province by persons therein carrying on such a business."
>
> This protective role, common to all securities commissions, gives a special character to such bodies which must be recognized when assessing the way in which their functions are carried out under their Acts.

The Supreme Court of Canada addressed the purpose of securities legislation again in *Pezim v. British Columbia (Superintendent of Brokers*), [1994] 2 S.C.R. 557 ("Pezim"), where Iacobucci J. stated (at p. 589):

> It is important to note from the outset that the Securities Act [B.C.] is regulatory in nature. In fact, it is part of a much larger framework which regulates the securities industry throughout Canada. Its primary goal is the protection of the investor but other goals include capital market efficiency and ensuring public confidence in the system: David L. Johnston, *Canadian Securities Regulation*, at p. 1.
>
> Within this large framework of securities regulation, there are various government administrative agencies which are responsible for the securities

> legislation within their respective jurisdictions. The British Columbia Securities Commission is one such agency. Also within this large framework are self-regulatory organizations which possess the power to admit and discipline members and issuers. The [Vancouver Stock Exchange] falls under this head. Having regard to this rather elaborate framework, it is not surprising that securities regulation is a highly specialized activity which requires specific knowledge and expertise in what have become complex and essential capital and financial markets.

The Supreme Court of Canada in *Pezim* describes the *Securities Act* in terms consistent with Driedger's description of "program legislation" referred to above. Iacobucci J. stated (at p.593):

> In National Corn Growers Assn. v. Canada (Canadian Import Tribunal), [1990] 2 S.C.R. 1324 at pp. 1369-70, Wilson J., in a concurring judgment, referred at p. 1336 to financial markets as a field where specialized tribunals have an important role to play:
>
> > Canadian courts have struggled over time to move away from the picture that Dicey painted toward a more sophisticated understanding of the role of administrative tribunals in the modern Canadian state. Part of this process has involved a growing recognition on the part of courts that they may simply not be as well equipped as administrative tribunals or agencies to deal with issues which Parliament has chosen to regulate through bodies exercising delegated power, e.g., labour relations, telecommunications, financial markets and international economic relations. Careful management of these sectors often requires the use of experts who have accumulated years of experience and a specialized understanding of the activities they supervise.
> >
> > Courts have also come to accept that they may not be as well qualified as a given agency to provide interpretations of that agency's constitutive statute that make sense given the broad

> policy context within which that agency must work. [Emphasis added by Iacobucci J.]

Although the comments in *Pezim* refer specifically to the British Columbia *Securities Act*, they apply equally to the Alberta Act.

We turn now to examine how Part 4 serves the general purpose of the Act by enabling the Commission to regulate "Exchanges, Self-Regulatory Organizations and Clearing Agencies".

Part 4 does not require that Self-Regulatory Organizations ("SROs") or clearing agencies be recognized by the Commission. There is no apparent need for a prohibition against unrecognized SROs or clearing agencies because there is little prospect of danger from such entities. They may apply for recognition or not, as they wish, but any SRO is naturally motivated to seek recognition in order to obtain delegated authority over its members.

Clearing agencies are highly-specialized institutions with links to many jurisdictions, performing a vital, utility-like, function in securities markets. The Canadian Depository For Securities, Inc. ("CDS") is the clearing agency for all trades executed on Canadian stock exchanges. CDS is recognized as a clearing agency by the Ontario Securities Commission, and as an SRO by the Commission des valeurs mobilières du Québec, but CDS has not applied for recognition as a clearing agency under section 53.4 of our Act because, at this time, there is no legal or practical need to do so.

Part 4 does require exchanges to be recognized by the Commission if they are to carry on business as an exchange in Alberta. Section 52(1), which does this, is the only prohibitive provision in Part 4. The rest of Part 4 is generally permissive, describing the complex relationship between the Commission and recognized entities.

Essentially, the provisions of Part 4 enable the Commission to work in a somewhat flexible partnership with recognized exchanges, SROs, and clearing agencies. Considered generically, these four components (securities regulators, exchanges, SROs, and clearing agencies) comprise the "large framework of securities regulation" described by Iacobucci J. in *Pezim*, above. They basically define the securities markets. The quality of these components and their ability to work together can be important factors in determining the size, strength, reputation and relative success or failure of the particular securities markets to which they relate.

The Commission delegates considerable authority to a recognized exchange, but it retains almost complete control in the sense that it has access to the exchange's books and records (section 53.7), approval over the exchange's councils and committees (section 53.2), and a broad public interest mandate to dictate virtually every aspect of the exchange's business under section 53(3). The Commission also acts as the primary appellate body for anyone directly affected by a decision, order, ruling, etc. of the recognized exchange. Appeals are not uncommon, but it would be unusual for the Commission to actually invoke the other provisions to dictate elements of the recognized exchange's business.

Part 4 provides a framework for what might be called "co-regulation" of the securities market. Sections 53(1) and 53.1(4) of the Act appear to contemplate that recognized exchanges and SROs have special expertise because they assign to them the responsibility to "regulate the operations and the standards of practice and business conduct" of their members, subject always to the ultimate authority and supervision of the Commission as senior regulator. Because exchanges, SROs and clearing agencies will normally have a common interest in the integrity and efficiency of the securities markets, they will normally work co-operatively with the Commission.

There is a significant political element in these relationships as well, with the parties attempting to persuade the Commission to take certain positions on regulatory issues. This political element may, and often does, involve regulators and regulated exchanges from other jurisdictions because of increasing pressures for harmonized regulation of securities markets.

(d) purposes of section 52(1)

In our view, the over-arching purpose of section 52(1) is to ensure that no exchange operates contrary to the public interest in Alberta. We note, however, that the application of section 52(1) to an exchange will trigger either of two distinctly different regulatory responses.

If an exchange applies for and receives recognition from the Commission, it becomes both a regulatee and a regulator. It is regulated by the Commission, and it regulates its members, as part of a comprehensive and co-operative framework of securities regulation intended to protect the public interest. The particular purpose of section 52(1) in this context is to provide a gateway to the more complex aspects of Part 4 which enable a close, ongoing relationship between the Commission and the recognized exchange. That relationship may be referred to as "small-r" regulation.

We distinguish that relationship from what may be referred to as "big-R" regulation, which is an essentially hostile response by the Commission meaning "stop right now". The particular purpose of section 52(1) in this context is simply to prohibit conduct by any exchange that is contrary to the public interest in Alberta.

Although big-R regulation is hypothetically applicable to any exchange, it may be seen as primarily directed at unregulated exchanges because their failure to comply with regulatory standards will generally trigger public interest concerns. There is almost never any need to apply big-R regulation to regulated exchanges because small-r regulation is designed to use co-operative methods to produce ongoing compliance with standards that protect the public interest. Big-R regulation is designed to deter non-compliance with those standards, using an array of intimidating enforcement tools.

This helps explain why section 52(1) has never been interpreted to apply to the activities in Alberta of regulated exchanges like the VSE or TSE. Their activities are not contrary to the public interest in Alberta precisely because they are already subject to small-r regulation in what

may be described as their "home" jurisdiction. It seems evident that it is not the purpose of section 52(1) to capture regulated exchanges, provided the small-r regulation in their home jurisdiction is satisfactory. That appears to be why each regulated exchange has traditionally been viewed as carrying on business only in its home jurisdiction. Functionally, this is similar to many situations where statutory or discretionary exemptions recognize the effectiveness of regulatory requirements imposed by other jurisdictions.

(e) public interest considerations relating to the WSE

The purpose and function of section 52 is directly related to public interest considerations. Section 52(2) provides that the Commission may recognize an exchange only if it "considers that it would not be prejudicial to the public interest to do so". The public interest considerations relating to the WSE may be seen by comparing the WSE to recognized and regulated exchanges.

Proposed NI 21-101 and Companion Policy 21-101CP describe the general requirements for recognition as an exchange, which include the filing of Form 21-101F1. As noted earlier, these provisions are not authoritative in this proceeding but we find that they accurately describe the factors to be considered in determining whether it would be prejudicial to the public interest to permit an exchange to carry on business in Alberta.

Section 5.1 of Companion Policy 21-101CP says:

> Recognition as an Exchange or Quotation and Trade Reporting System
>
> (1) In determining whether to recognize an exchange or quotation and trade reporting system, the Canadian securities regulatory authorities must determine whether it is in the public interest to do so.
>
> (2) In exercising this discretion the Canadian securities regulatory authorities will look at a number of factors, including
>
> (a) the manner in which the exchange or quotation and trade reporting system proposes to comply with the National Instrument 21-101;
>
> (b) whether the exchange or quotation and trade reporting system has fair and meaningful representation on its governing body, in the context of the nature and structure of the exchange or quotation and trade reporting system;
>
> (c) whether the exchange or quotation and trade reporting has sufficient financial resources for the proper performance of its functions; and

(d) whether the by-laws, rules, regulations, policies, procedures, practices, interpretations and other similar instruments of the exchange or quotation and trade reporting system ensure that its business is conducted in an orderly manner so as to afford protection to investors.

Form 21-101F1 requires an exchange to provide detailed information about its operations. This is intended to enable the Commission to consider all aspects of the exchange's operations and their combined effects in order to determine whether it is in the public interest for the Commission to recognize the exchange. Each exchange will normally have unique characteristics. Small-r regulation generally permits the Commission and the exchange to address the implications of the most complex and subtle combined effects of exchange operations.

We have incomplete information about the WSE and it would be speculative to consider the most complex and subtle combined effects its operations may have had. But this is unnecessary because the WSE raises so many fundamental concerns by failing to meet the most basic requirements of exchange operations. It is not financially responsible, its corporate structure is false, it has no clearance and settlement system, and so on. Any of these factors, alone, would present a significant public interest concern. In this case, however, these factors must be considered as part of the background to the two most striking characteristics of the WSE's operations: 1) its lack of credible listing and disclosure requirements; and 2) offering direct trading access to the public through the Internet.

1) listing and disclosure requirements

The requirement for listed companies (and other issuers) to provide full and accurate disclosure of financial and business information is central to our system of securities regulation and investor protection. Regulated exchanges generally play a significant role in setting and enforcing such requirements, so that a listing on a regulated exchange connotes compliance with certain listing and disclosure standards.

The WSE has no credible listing standards or disclosure requirements for its listed companies. A sophisticated investor who closely examined the WSE website would probably recognize this and shun the WSE. However, a less-sophisticated investor might think that a WSE listing connotes compliance with meaningful listing or disclosure standards, which would be a dangerous mistake. The overall presentation of information on the WSE website seems to be crafted to lure the unwary investor to make that mistake.

It is significant that, although the website says that the WSE's Arole is simply to provide a mechanism for full disclosure of relevant financial information for each company listed", there were no financial statements whatsoever on the website. Although financial statements could be requested from the companies, the companies' statements were mainly projections. We find that the apparent purpose and effect of this is to obscure the fact that there is no reliable financial information about the listed companies. Similar considerations apply to the excessively promotional descriptions of listed companies' business plans and prospects on the website. Together, these create a definite risk that prospective investors would be misled.

2) direct trading access

Perhaps the most unorthodox characteristic of the WSE is that it offers direct trading access to anyone through the Internet.

We are not aware of any regulated exchange that offers such access to anyone who is not a member of that or another regulated exchange. All members of regulated exchanges are normally registrants under the Act and members of SROs, subject to a wide range of regulatory requirements intended to protect the public interest. The transactions on regulated exchanges are trades by registrant/members (who will often be acting as agents for other persons). Regulated exchanges do not trade. Their members trade (exempted by section 54(1) of the Act) and their members' customers trade (exempted by section 65(1)(j) of the Act).

The WSE is radically different in that it has no members. The core of the WSE's intended business is the primary distribution of securities by direct sales through the Internet. Anyone with Internet access could buy shares through the WSE. By offering to sell securities directly through its website, the WSE trades in securities. Although the WSE website referred to the ISBC having some role in these transactions it is clear that the ISBC's role was in no way comparable to the function of registrant/members of regulated exchanges.

This aspect of the WSE's business violates one of the fundamental tenets of the Act, which is that no one may trade in securities unless they are registered or exempt from the registration requirement. In addition, since the securities of the companies listed on the WSE were not qualified for sale in Alberta, this trading by the WSE also constitutes an illegal distribution of securities, thereby violating another fundamental tenet of the Act. It is self-evident that these aspects of the WSE's business are contrary to the public interest because they could be the subject of enforcement action as violations of sections 54(1) and 81(1) of the Act. They are considered as public interest issues here in the context of section 52(1) because they are an integral part of the WSE's unique method of carrying on business as an exchange.

Almost every aspect of the WSE's structure and operations presents a substantial threat to prospective investors and we find that its overall business is utterly contrary to the public interest.

(f) territoriality of section 52(1)

The WSE is active in and has connections to many jurisdictions, including Alberta. Our jurisdiction under the *Securities Act* is basically territorial, and we must consider whether the WSE's activities fall within that jurisdiction.

We find that the same territoriality considerations apply in this case as discussed by the Supreme Court of Canada in *Libman v. The Queen*, [1985] 2 S.C.R. 178 ("*Libman*"). Libman involved a fraud charge under the Criminal Code where the accused conducted activities in several countries, including Canada. La Forest J. reviews the history of English and Canadian law in relation to transnational offences and distills it down to a concise rationale and conclusion which we find directly applicable to the case at hand.

La Forest J. describes the basic rationale for territoriality as follows (at p. 208):

> [T]he territorial principle in criminal law was developed by the courts to respond to two practical considerations, first, that a country has generally little direct concern for the actions of malefactors abroad, and secondly, that other states may legitimately take umbrage if a country attempts to regulate matters taking place wholly or substantially within their territories. For these reasons the courts adopted a presumption against the application of laws beyond the realm....

La Forest J. then describes how the courts never applied the doctrine rigidly but tried, sometimes crudely, to apply its underlying rationale. He describes part of the rationale as follows (at p. 209):

> This country has a legitimate interest in prosecuting persons for activities that take place abroad but have an unlawful consequence here.... The protection of the public in this country is widely acknowledged to be a legitimate purpose of criminal law, and one moreover that another nation could not easily say offended the dictates of comity.

LaForest J. applied the reasoning of the House of Lords in *Treacy v. Director of Public Prosecutions*, [1971] A.C. 537. That case involved a criminal charge of blackmail in England, where the accused posted a letter in England, to a woman in West Germany, demanding money upon certain threats. LaForest J. described Lord Diplock's decision as follows (at pp. 195-6):

> In his view, if the facts alleged and proved constitute the offence charged, the only reason (the technicalities of venue being jurisdictional and long ago abolished) for refusing to convict was to be found in the international rules of

comity which it must be presumed Parliament did not intend to break. But he interpreted comity narrowly to attempts to regulate conduct abroad and not in the United Kingdom. As he put it, at p. 561:

> It would be an unjustifiable interference with the sovereignty of other nations over the conduct of persons in their own territories if we were to punish persons for conduct which did not take place in the United Kingdom and had no harmful consequences there. But I see no reason in comity for requiring any wider limitation than that upon the exercise by Parliament of its legislative power in the field of criminal law.

In particular he noted that comity did not prevent Parliament from prohibiting conduct in England that has consequences abroad. Nor did it give immunity to persons abroad for conduct there that has harmful consequences in England. He continued at pp. 561-62:

> There is no rule of comity to prevent Parliament from prohibiting under pain of punishment persons who are present in the United Kingdom, and so owe local obedience to our law, from doing physical acts in England, notwithstanding that the consequences of those acts take effect outside the United Kingdom. Indeed, where the prohibited acts are of a kind calculated to cause harm to private individuals it would savour of chauvinism rather than comity to treat them as excusable merely on the ground that the victim was not in the United Kingdom itself but in some other state.
>
> Nor, as the converse of this, can I see any reason in comity to prevent Parliament from rendering liable to punishment, if they subsequently come to England, persons who have done outside the United Kingdom physical acts which have had harmful consequences upon victims in England. The state is under a correlative duty to those who owe obedience to its laws to protect their interests and one of the purposes of criminal law is to afford such protection by deterring by threat of punishment conduct by other persons which is calculated to harm those

> interests. Comity gives no right to a state to insist that any person may with impunity do physical acts in its own territory which have harmful consequences to persons within the territory of another state. It may be under no obligation in comity to punish those acts itself, but it has no ground for complaint in international law if the state in which the harmful consequences had their effect punishes, when they do enter its territories, persons who did such acts.

La Forest J. summarized his approach to the limits of territoriality as follows (at pp. 212-3):

> As I see it, all that is necessary to make an offence subject to the jurisdiction of our courts is that a significant portion of the activities constituting that offence took place in Canada. As it is put by modern academics, it is sufficient that there be a "real and substantial link" between an offence and this country, a test well known in public and private international law....

La Forest J. also described the need to adopt an evolving concept of comity, saying (at pp. 213- 4):

> Just what may constitute a real and substantial link in a particular case, I need not explore. There were ample links here. The outer limits of the test may, however, well be coterminous with the requirements of international comity.
>
> As I have already noted, in some of the early cases the English courts tended to express a narrow view of the territorial application of English law so as to ensure that they did not unduly infringe on the jurisdiction of other states. However, even as early as the late 19th century, following the invention and development of modern means of communication, they began to exercise criminal jurisdiction over transnational transactions as long as a significant part of the chain of action occurred in England. Since then means of communications have proliferated at an accelerating pace and the common interests of states have grown proportionately. Under these circumstances, the notion of comity, which means no more nor less than "kindly and considerate behaviour towards others", has also evolved. How considerate is it of the interests of the United States in this case to permit

> criminals based in this country to prey on its citizens? How does it conform to its interests or to ours for us to permit such activities when law enforcement agencies in both countries have developed cooperative schemes to prevent and prosecute those engaged in such activities? To ask these questions is to answer them. No issue of comity is involved here. In this regard, I make mine the words of Lord Diplock in Treacy v. Director of Public Prosecutions cited earlier. I also agree with the sentiments expressed by Lord Salmon in Director of Public Prosecutions v. Doot, supra, that we should not be indifferent to the protection of the public in other countries. In a shrinking world, we are all our brother's keepers. In the criminal arena this is underlined by the international cooperative schemes that have been developed among national law enforcement bodies.

Although the *Libman* decision addresses territoriality in the context of criminal law, in our view the same principles are applicable to the Act, including section 52(1).

(g) conclusion

We find that the WSE did carry on business as an exchange in Alberta, contrary to section 52(1) of the Act.

We find that any similarity between the activities in Alberta of the WSE and of regulated exchanges is entirely superficial. The most important distinguishing characteristic of the WSE is its general lack of regulation, manifested in business practices that are contrary to the public interest. We find that the purpose of section 52(1) is protect the public interest by prohibiting such practices.

We interpret the phrase "carry on business as an exchange in Alberta" to mean, in effect, "conduct any exchange activity in Alberta that requires the Commission to act to protect the public interest". Although this makes the application of section 52(1) somewhat nebulous, that is a natural consequence of the fact that it is impossible to precisely define the public interest in the context of innovative or evolving exchange activity. While the public interest remains relatively constant, and is quite clearly reflected in the regulatory requirements imposed upon the actual activities of recognized exchanges, exchange activities are almost infinitely variable. Every exchange must be assessed individually and it is the combined effect of all its activities that must be weighed against the public interest to determine whether section 52(1) should apply. It would be inappropriate to focus on particular operations or activities as determinative because these are easily manipulated (as this case shows), and to do so would enable such manipulation to succeed in avoiding public-interest regulation.

There is no inconsistency in our applying section 52(1) to the WSE but not to regulated exchanges because of the fundamental differences in the way they carry on business. Regulated

exchanges do not raise public interest concerns in Alberta because regulation is an integral part of the way they carry on business. A purposive interpretation of section 52(1) does not, in our view, allow us to impose Alberta's small-r regulation on an exchange that already has similar regulation in its home jurisdiction and which does not raise public interest concerns in Alberta.

Our interpretation does not preclude the possibility of big-R regulation against regulated exchanges, which might lead eventually to small-r regulation of such an exchange. That has never occurred to our knowledge and it would be an exceptional situation, presumably involving unusual activity by the exchange raising significant public interest concerns, with enforcement action taken as a last resort after the failure of the various mechanisms that permit harmonized small-r regulation between jurisdictions. In such a situation, it could be said that the exchange had fundamentally changed the way it carried on business and thereby become subject to section 52(1).

With the passage of physical trading floors and the evolution of technology, the location of exchange operations has become increasingly flexible and notional. That makes the location of exchange operations less significant, and the functional linkage between an exchange and its recognizing regulator more significant, in determining where that exchange carries on business. To some extent, exchanges may choose where they want to be regulated and so assert where they believe that they carry on business within the meaning of the Act, as CDNX did recently when it sought recognition from the Commissions in both Alberta and British Columbia. In our view, as long as the connection between a regulated exchange and its home jurisdiction is reasonable and substantial, and the exchange's activities do not raise public interest concerns in Alberta (generally, by the home jurisdiction maintaining regulatory standards comparable to ours), section 52(1) should be interpreted to say that the regulated exchange carries on business only in its home jurisdiction.

We see clear distinctions between the connection of a typical regulated exchange to its home jurisdiction and the situation of the WSE. The WSE tried to choose its regulator by deliberately seeking the minimum possible amount of regulation. When the authorities in the Cayman Islands shut down the WSE's operations there, it moved to Antigua. In our view, this flag-of-convenience approach demonstrates the lack of any substantial connection between the WSE and either of its purported home jurisdictions. Even if the WSE had much closer links to its purported home jurisdictions, the lack of significant regulation by those jurisdictions would, in our view, preclude them from being considered home jurisdictions comparable to those of regulated exchanges. In this sense, unregulated exchanges are homeless. They may therefore be seen as carrying on business wherever they set foot and subject to enforcement action by any jurisdiction with standards comparable to ours.

The WSE has real and substantial links to Alberta, more than sufficient to justify the application of Alberta law. The WSE was established in and run from Alberta. Tom Seto and Orest Rusnak were both Alberta residents who spent much of their time here promoting the WSE to Albertans. The real and substantial nature of these links is evident by comparing them to the

artificial and insignificant links between the WSE and the Cayman Islands (place of incorporation) or Antigua (location of computer).

We also find that the Commission has a legitimate interest in applying Alberta law to the WSE merely because its activities have unlawful consequences here. If the WSE had operated entirely "offshore", as it wanted to, we would still have jurisdiction to take enforcement action against anyone in Alberta with a sufficient connection to the WSE. Similar considerations would apply in every other jurisdiction with securities laws comparable to ours. As a practical issue, it may be necessary to wait until someone comes from offshore to such a jurisdiction before effective enforcement action can be taken. The prospect of such action by any of a number of major commercial jurisdictions should be a deterrent to anyone associated with offshore entities who conduct unlawful securities market activities through the Internet. Such deterrent is only effective if individual jurisdictions take action wherever possible, and we see no reason in comity to prevent that. There would be no purpose in having an elaborate framework of securities regulation to protect the public interest if the law permitted entities like the WSE to circumvent it all by using modern technology and communications to step beyond our jurisdiction.

The WSE's potential victims include anyone with Internet access so, in this situation, comity encourages us to apply Alberta law because the WSE's links to Alberta allow us to act and because we would want other jurisdictions to take a similar approach.

Quite different comity considerations might apply in a situation where section 52(1) was being used in an attempt to force an already-regulated exchange to apply for recognition in Alberta. In that situation, there would be a major issue of comity because, in effect, we would be trying to superimpose Alberta's small-r regulation over the existing (and, presumably, somewhat different) small-r regulation of another jurisdiction. No exchange can operate lawfully if it is subject to inconsistent small-r regulation from two or more jurisdictions, so the principles of comity militate strongly against interpreting section 52(1) to capture any exchange whose activities do not raise significant public interest concerns in Alberta.

(C) Did the respondents trade in securities, contrary to sections 54(1) and 81(1) of the Act?

The Notice of Hearing alleges that the respondents traded in securities of the WSE by requiring companies to purchase shares in the WSE as a condition of listing.

The requirement that listed companies buy shares in the WSE appears on both the Edmonton and Antigua websites. The evidence shows, however, that the WSE never sold or issued any shares. It appears that only Mr. Wall understood that he was purchasing shares in the WSE as part of the listing process. The requirement appears to have been waived or simply ignored in relation to the other listings.

Section 1(x)(v) of the Act defines trade to include "any act, advertisement, solicitation, conduct or negotiation made directly or indirectly in furtherance of [a trade]". This is a broad provision intended to regulate the activities that may lead to actual sales of securities.

We find that the information on the WSE websites constitutes a trade in WSE shares. We find that the information on the websites is clearly a solicitation in furtherance of a trade and it does not matter that no WSE shares were actually sold.

Tom Seto argued, in effect, that all trades in securities occur only in the jurisdiction of incorporation of the issuer. That is incorrect and it reflects a misguided approach to the question of where a trade occurs. It is therefore useful to review this question here.

The basic principles are described in *R. v. McKenzie Securities Limited* (1966), 55 W.W.R. 157 (Man. C.A.) *("McKenzie").* That case involved charges under the Manitoba *Securities Act* of unlawfully trading in securities under circumstances where the accused operated entirely from Toronto by letters and telephone calls. Freedman, J.A. said at p. 165-6:

> Although offences are local, the nature of some offences is such that they can properly be described as occurring in more than one place. This is peculiarly the case where a transaction is carried on by mail from one territorial jurisdiction to another, or indeed by telephone from one such jurisdiction to another. This has been recognized by the common law for centuries….
>
> I think it completely unrealistic to suggest that when the accused sent their letters by mail from Toronto, Ont., to Shilo, Man., that act of solicitation there represented took place only in Toronto or at most within the borders of Ontario. Such an approach ignores completely the nature and character both of a letter and of the postal service. The invitation put forward by the accused in their letters was a continuing one. It started when written in Toronto; it continued when deposited in the post box there; it did not cease to exist during the period when it was being transported through the postal service (the agency selected for that purpose by the accused); and it retained its vitality and spoke with special effectiveness to McCaffrey at the time when he opened and read the letter in Shilo in Manitoba. It was in this province that McCaffrey was solicited by the accused to purchase the shares in question, and it was in this province that McCaffrey responded favourably to such solicitation. I would agree with the learned magistrate and the learned county court judge that what took place in the present case

> constituted an act of trading in securities within the definition of The *Securities Act* of Manitoba.

The principles expressed in *McKenzie* were applied by the Commission to telephone solicitations in *Re Cromwell Financial Service Inc. et al* (1996, unreported) and, in our view, these same principles apply to solicitations by any method of communication, including the Internet. The Internet is revolutionary in the way it permits instantaneous communication and interactivity on a global scale, but its function in relation to securities trading remains essentially similar to the mail or the telephone. We agree with the statement in *"Securities Activity on the Internet"* (a Report of the Technical Committee of the International Organization of Securities Commissions published in September 1998), that the "fundamental principles of securities regulation do not change based on the medium".

These principles are also reflected in National Policy 47-201 *Distribution of Securities Using the Internet and other Electronic Means* ("NP 47-201"), which became effective January 1, 2000, Although its provisions are not authoritative in this proceeding, the following section of NP 47-201 is completely consistent with our view:

> **2.2 Trading in a Jurisdiction**
>
> (1) The securities regulatory authorities generally consider a person or company to be trading in securities in a local jurisdiction if that person or company posts on the Internet a document that offers or solicits trades of securities, and if that document is accessible to persons or companies in that local jurisdiction.
>
> (2) Despite subsection (1), the securities regulatory authorities consider the posting of a document on the Internet that offers or solicits trades of securities not to be a trade or, if applicable, a distribution, in a local jurisdiction if
>
> (a) the document contains a prominently displayed disclaimer that expressly identifies the local jurisdictions and/or foreign jurisdictions in which the offering or solicitation is qualified to be made, and that identification does not include the local jurisdiction; and
>
> (b) reasonable precautions are taken by all persons or companies offering or soliciting trades of securities through

the document posted on the Internet not to sell to anyone resident in the local jurisdiction.

(3) Market participants are reminded that the registration requirements of securities legislation apply in connection with the posting of a prospectus or other offering document on the Internet for use in connection with a distribution in a local jurisdiction. The act of posting a prospectus or offering document in those circumstances is an act in furtherance of a trade in that local jurisdiction, and the person or company posting the prospectus or offering document must, in order to comply with the registration requirements

(a) be registered to trade in the local jurisdiction;

(b) have the benefit of an exemption from the registration requirements in connection with the distribution in the local jurisdiction; or

(c) refer all inquiries concerning the document to a registered dealer in the local jurisdiction.

It is clear that the respondents traded in the securities of the WSE. They similarly traded in the securities of the companies listed on the WSE but, as noted above, this has been addressed as a characteristic of the way the WSE carried on business in the context of section 52(1). The same principles apply in either context.

5. OTHER MATTERS

Certain other matters were raised in Tom Seto's oral and written submissions that should be addressed briefly.

Tom Seto's written submission referred, for the first time in these proceedings, to constitutional issues. His submission mentions, for example, "our Constitutional Right to do business where we want, how we want, when we want, provided we are abiding by the law". There is also a brief discussion of the exclusive jurisdiction of the Canadian federal government over telecommunications and the Internet together with the suggestion that "all matters related to this hearing should be adjourned pending the determination of the constitutional issue with respect to telecommunications which is not a Provincial issue". We find no merit in these submissions.

Tom Seto's written and oral submissions suggested that, when approaching Albertans about listing their companies on the WSE, he and Orest Rusnak were acting as consultants on behalf of those people and not as representatives of the WSE. Tom Seto's written submission says, AFor the [Commission] to disallow a consultant the freedom of speech and expression as to what is available on the open market to facilitate the wishes of his client is undemocratic".

We find no merit in these submissions. The fact that a person may act as a consultant to one party has no bearing on whether they also act on behalf of the WSE. In these situations, the dual roles of Tom Seto and Orest Rusnak created an obvious conflict of interest which was, to some extent, known or disclosed to the other parties. Such knowledge or disclosure does not alter the fact that Tom Seto and Orest Rusnak acted as representatives of the WSE in these situations.

6. CONCLUSION

We find that Orest Rusnak was a director of the WSE, as defined by section 1(e.1) of the Act. We find that the WSE carried on business as an exchange in Alberta, contrary to section 52(1) of the Act. We find that the respondents traded in securities of the WSE, contrary to sections 54(1) and 81(1) of the Act.

We will reconvene the hearing in order to receive submissions as to what orders may be appropriate in the circumstances, and we ask that counsel for Commission staff, in consultation with the respondents, make the necessary arrangements with the Secretary to the Commission.

Dated at the **City of Edmonton** in the **Province of Alberta** this 15th day of February, 2000.

"Original Signed By"
Eric T. Spink
Vice-Chair

"Original Signed By"
Ian McConnan
Commission Member

"Original Signed By"
Jerry Bennis
Commission Member