

2009 BCSECCOM 22

**Henry Jung, David John Allen
and Reginald Clarke Handford**

Sections 161(1) and 162 of the *Securities Act*, RSBC 1996, c. 418

Hearing

Panel	Brent W. Aitken Kenneth G. Hanna David J. Smith	Vice Chair Commissioner Commissioner
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Date Submissions Completed	December 30, 2008
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Date of Decision	January 19, 2009
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Submissions Filed By	
Graham R. MacLennan	For the Executive Director
Shawn R. McColm	

Henry Jung	For himself
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Decision

Introduction

- ¶ 1 This decision should be read with our Findings made on November 5, 2008 (see 2008 BCSECCOM 588), in which we found that Henry Jung contravened the *Securities Act*, RSBC 1996, c. 418. We found that the other two respondents, David John Allen and Reginald Clarke Handford, did not contravene the Act.
- ¶ 2 In our Findings, we directed Jung and the executive director to file submissions on sanctions and to apply for an oral hearing if they wanted one. Both parties made submissions. Neither party applied for an oral hearing.
- ¶ 3 The hearing was about Jung's activities on behalf of Bright Star, a junior mining exploration company. Bright Star was a reporting issuer traded on what is now the TSX Venture Exchange. It has since been delisted, and dissolved for failure to file its annual returns.
- ¶ 4 Jung is a chartered accountant whose involvement with Bright Star began in 2001, when he hired key officers and arranged for the appointment of a new board of directors.

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- ¶ 5 Bright Star directors said Jung provided the “impetus” for the company, was the “number one” person providing direction to the company, the “general manager,” and the one that “ran the company.”
- ¶ 6 Jung determined what matters went before the board, although as a matter of practice he operated autonomously, binding the company in significant matters. Bright Star’s principal activities were mineral exploration and financing. Jung was the one who made the significant decisions about both. Jung used his own funds to provide Bright Star with working capital. Jung did everything significant in connection with Bright Star’s largest financing, the debenture issue described below.
- ¶ 7 On behalf of Bright Star, Jung:
- hired and supervised key staff
 - negotiated and signed agreements
 - managed the company’s cash flow
 - prepared and signed cheques
 - was solely responsible for the company’s accounting
 - prepared unaudited financial statements
 - managed the relationship with the company’s auditors
 - sought financing
 - sought property acquisitions.
- ¶ 8 We found that Jung was a *de facto* director and officer of Bright Star.
- ¶ 9 Between July 2001 and September 2004, Jung made hundreds of trades in Bright Star shares in his own name and through companies controlled or directed by him – trades representing a total volume of 5.7 million shares. Jung did not file any insider trading reports for any of these trades.
- ¶ 10 In 1996 the exchange became concerned about Jung’s suitability as an officer or director of exchange listed companies. In a May 1996 letter to Jung, the exchange referred to Jung’s past history with companies where he was “not appointed officially as a director” but “performed a significant role similar to that of a director or officer.” The exchange went on to say, “your suitability as a director or officer or someone who performs similar functions to those of a director is questionable.” Jung says that this letter was the reason he did not put his name forward to be a director of Bright Star.
- ¶ 11 In early 2002, Bright Star entered into a financing arrangement that Jung negotiated with John Cornwall of Ottawa. Bright Star issued three debentures to three Ontario companies controlled by Cornwall. The companies paid for the

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debentures with promissory notes. Cornwall then placed newspaper advertisements to find cash investors. He found 130 individuals who invested a total of nearly \$3 million in cash in Bright Star debentures.

- ¶ 12 The investors were told little about Bright Star, its business, or its prospects. They appear to have had little understanding of the nature of their investment, or the associated risk. Cornwall told several investors that the face value of the debenture was “guaranteed.”
- ¶ 13 The debentures are now worthless.
- ¶ 14 Jung managed and directed the debenture financing. He was Bright Star’s sole contact with Cornwall. He negotiated the terms of the debentures. He alone dealt with Bright Star’s counsel on legal issues related to the financing. He was the sole signatory of the subscription agreements between Bright Star and the individual investors and the debentures Bright Star issued to them. He arranged the involvement of Octagon Capital Corporation in setting up accounts for the individual investors.
- ¶ 15 Jung required Cornwall to obtain from each investor a letter addressed to Bright Star stating “This is to confirm my purchase and the transfer to me of a portion of an existing . . . convertible debenture that has been previously issued.”
- ¶ 16 We found that Cornwall and Jung contemplated that the financing would be accomplished through the sale of debentures to individual investors.

Findings

- ¶ 17 We found that Jung:
1. as a *de facto* director and senior officer, was an insider of Bright Star, and traded securities of Bright Star without filing reports of those trades, contrary to section 87 of the Act; and
 2. traded in Bright Star debentures without being registered to do so, contrary to section 34(1), and distributed those securities without filing a prospectus, contrary to section 61(1).

Discussion

- ¶ 18 The Executive Director says we should prohibit Jung, for 15 years, from:
- trading securities,
 - using the exemptions under the Act,
 - acting as a director, officer, registrant or promoter,
 - engaging in a management or consultative capacity in connection with

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- activities in the securities market, and
- engaging in investor relations activities.

- ¶ 19 The executive director also seeks an administrative penalty of \$100,000.
- ¶ 20 Jung says that the appropriate sanction would be a prohibition from acting as a director or officer of any issuer, and from acting as a registrant, for six months, and an administrative penalty of \$5,000.
- ¶ 21 In *Re Eron Mortgage Corporation* [2000] 7 BCSC Weekly Summary 22, the Commission discussed the factors relevant to sanction as follows (at page 24):

In making orders under sections 161 and 162 of the Act, the Commission must consider what is in the public interest in the context of its mandate to regulate trading in securities. The circumstances of each case are different, so it is not possible to produce an exhaustive list of all of the factors that the Commission considers in making orders under sections 161 and 162, but the following are usually relevant:

- the seriousness of respondent's conduct,
- the harm suffered by investors as a result of the respondent's conduct,
- the damage done to the integrity of the capital markets in British Columbia by the respondent's conduct,
- the extent to which the respondent was enriched,
- factors that mitigate the respondent's conduct,
- the respondent's past conduct,
- the risk to investors and the capital markets posed by the respondent's continued participation in the capital markets of British Columbia,
- the respondent's fitness to be a registrant or to bear the responsibilities associated with being a director, officer or adviser to issuers,
- the need to demonstrate the consequences of inappropriate conduct to those who enjoy the benefits of access to the capital markets,
- the need to deter those who participate in the capital markets from engaging in inappropriate conduct, and
- orders made by the Commission in similar circumstances in the past.

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Seriousness of misconduct

- ¶ 22 Jung's misconduct is serious. He was an insider of Bright Star and, over a three-year period, made hundreds of trades representing about 5.7 million of its common shares without filing insider trading reports. The filing of insider trading reports is an important element of securities regulation because it informs the market about trading in the issuer's shares by those who know the issuer the best – its management. Jung's failure to file reports for over three years for hundreds of trades aggregating millions of shares is serious contravention of the requirement and damages the integrity of our markets.
- ¶ 23 More seriously, Jung traded nearly \$3 million of Bright Star debentures to individual investors across Canada in an illegal distribution.
- ¶ 24 The requirements to be registered to trade securities, and to file a prospectus to distribute securities, are intended to prevent distributions of securities with the outcome that resulted in this case. Had the Bright Star investors had the benefit of the advice of a registrant, and the disclosure required by a prospectus, it is unlikely they would have invested and their losses could have been averted.

Harm to investors

- ¶ 25 Jung's conduct harmed investors. Jung refers to the losses suffered by only two investors, British Columbia residents who he says lost less than \$25,000. In any event, he denies any responsibility for their losses, and those of the other 128 investors who purchased about \$3 million of now-worthless debentures. He says Cornwall is to blame. These submissions not only rely on facts not in evidence (the losses of the unnamed investors he describes), but contradict our finding that he played the leading role in the distribution to all 130 investors.

Damage to integrity of the market

- ¶ 26 Jung's focus on the two British Columbia investors, and his disregard of the 128 other investors who purchased Bright Star debentures and lost their investment, shows his failure to understand the impact of his conduct on British Columbia's capital markets. There is always damage done to British Columbia's capital markets when a British Columbia reporting issuer perpetrates an illegal distribution from British Columbia. That only a small number of British Columbia residents participated in the distribution is not relevant. What matters is the scale of the distribution. Here, the scale of the distribution – investments of \$3 million by 130 investors in seven provinces – was significant, and cannot but have damaged the reputation of our capital markets.

Enrichment

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- ¶ 27 Bright Star paid Jung \$60,000 per year, which was at least partly funded by the proceeds of the debenture issue. Jung says his working capital loans to Bright Star left him with losses of \$250,000, and that he lost his own investment in Bright Star. There is no evidence on either subject in the record.

Mitigating factors

- ¶ 28 We are not aware of any mitigating factors. Jung says he relied on legal advice about the Bright Star debenture issue, but there is no evidence on that subject in the record.

Past conduct, risk, fitness, and deterrence

- ¶ 29 Jung did not put his name forward as a director of Bright Star because of the exchange's May 1996 letter advising him that his suitability as a director or officer was "questionable." The exchange was of the view that Jung had a pattern of performing the role of a director or officer of public companies without being officially appointed to those positions. Despite this warning that the issue was not his formal title but his actual conduct, Jung nonetheless acted as a *de facto* director and senior officer of Bright Star.
- ¶ 30 The Act regulates securities trading in the public interest. What matters is the substance of conduct, not its form. Jung, however, ignores substance and conducts himself according to the form.
- ¶ 31 For example, Jung said he could not have been responsible for all of the things that Bright Star did because he did not carry a director or officer title, nor was he formally appointed to any director or officer position. Despite clear evidence that he ran the company, the cornerstone of his defence was that he had an unwritten employment agreement (of which we found no evidence) that specified the scope of his authority. He failed to recognize that what was important was what he did, not what the agreement said. In his submissions on sanctions, he continues to describe his role in terms that contradict our Findings.
- ¶ 32 Jung insisted that Cornwall obtain letters from investors confirming their debenture investment as the acquisition of an existing, previously issued debenture. This shows Jung's apparent belief that, despite his signature on debentures issued to the investors by Bright Star, if he could document the transactions as resales of previously issued securities, the financing would not be a distribution.
- ¶ 33 In his submissions, Jung minimizes his role in the debenture distribution, saying that all he did was sign them. It was Cornwall, not him, who sold the debentures, he says, and so "any losses suffered by investors were due to Cornwall and not

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Jung.” He apparently sees no link between his role in directing the debenture financing and the losses suffered by investors.

- ¶ 34 For these reasons, Jung is not, in our opinion, currently fit to participate in public markets and were he to continue to do so, he would present a risk to investors.
- ¶ 35 It is appropriate to make orders that demonstrate the consequences of Jung’s misconduct, and that will have an appropriate deterrent effect.

Previous decisions

- ¶ 36 Jung cited several authorities but we do not consider them relevant to the circumstances.
- ¶ 37 The executive director cites four illegal distribution cases (*L.O.M Medical International, Inc. and John Klippenstein* 2004 BCSECCOM 289; *Edgson* 2005 BCSECCOM 393; *Heeres* 2005 BCSECCOM 395; and *RAB Energy* 2004 BCSECCOM 632) and one insider trading report case (*Steffensen* [2000] 9 BCSC Weekly Summary 11). *LOM* is a decision of the Commission; the other cases are settlements made with the executive director.
- ¶ 38 In *LOM*, *LOM* and Klippenstein participated in an illegal distribution of *LOM* shares, raising about US\$1.4 million and C\$279,000 from 352 investors.
- ¶ 39 *LOM* involved factors that do not apply here. Klippenstein made misrepresentations, and he and his family took substantial cash out of *LOM*.
- ¶ 40 A significant aggravating factor in *LOM* was that while Klippenstein was engaging in the illegal distribution, he was under sanction by the Saskatchewan Securities Commission for a previous illegal distribution in that province. Here, Jung did not proceed in the face of an explicit prohibition from acting as a director and officer, but he arranged his relationship with Bright Star in a manner intended to avoid the issue raised by the Exchange in 1996 – acting as a director and officer despite not having the formal title. In addition, Jung has failed to accept responsibility for the harm done to investors and markets as a result of the illegal distribution.
- ¶ 41 The Commission made 10-year prohibition orders against Klippenstein under section 161(1) and ordered an administrative penalty of \$100,000. The administrative penalties in illegal distribution cases not involving misrepresentation or fraud are significantly lower.

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¶ 42 In *Steffenson*, an insider failed to report nearly 500 trades representing over 1.1 million shares. He subsequently filed the reports and paid late filing fees of \$1,600. Steffensen agreed to 3-year prohibitions under section 161(1), a \$5,000 penalty, and \$1,000 in costs. Jung traded 5.7 million shares and made more trades than Steffensen. In *Steffensen* there was also evidence about the volume of trading in the company's shares generally, and about fluctuations in the share price, evidence we do not have here.

Orders

¶ 43 Considering it to be in the public interest, we order:

1. under section 161(1)(b) of the Act, that Jung cease trading, and is prohibited from purchasing, securities or exchange contracts, except that Jung may trade for his own account through a registrant, if he gives the registrant a copy of this decision,
2. under section 161(1)(d)(i), that Jung resign any position he holds as a director or officer of an issuer (except an issuer all the securities of which are owned beneficially by him, his wife, or his children), registrant or investment fund manager,
3. under section 161(1)(d)(ii), that Jung is prohibited from becoming or acting as a director or officer of any issuer (except an issuer all the securities of which are owned beneficially by him, his wife, or his children), registrant or investment fund manager,
4. under section 161(1)(d)(iii), that Jung is prohibited from becoming or acting as a registrant, investment fund manager or promoter,
5. under section 161(1)(d)(iv), that Jung is prohibited from acting in a management or consultative capacity in connection with activities in the securities market,
6. under section 161(1)(d)(v), that Jung is prohibited from engaging in investor relations activities,

until the later of January 18, 2024 and the date Jung pays the amount in paragraph 7 of these orders; and

7. under section 162, that Jung pay an administrative penalty of \$70,000.

¶ 44 January 19, 2009

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¶ 45 For the Commission

Brent W. Aitken
Vice Chair

Kenneth G. Hanna
Commissioner

David J. Smith
Commissioner