THE MANITOBA SECURITIES COMMISSION

July 11, 2022

IN THE MATTER OF: THE SECURITIES ACT

- and -

IN THE MATTER OF: WAYNE SOKAL and ESP SOFTWARE INC.

REASONS FOR DECISION
OF
THE MANITOBA SECURITIES COMMISSION

Panel:

Panel Chair:	Mr. J.T. McJannet, Q.C.
Member:	Mr. C.D. Burns
Member:	Mr. D.A. Huberdeau-Reid

Appearances:

Mr. A. Poushangi	)	Counsel for Commission Staff
B. Barnes Trickett	)	Counsel on behalf of Wayne
A. Favereau	)	Sokal
	)	
A. Stacey	)	Counsel on behalf of Grant
A. Doyle	)	Kaufmann

Hearing Dates and Proceedings

Reference herein to "MSC Panel" means this panel hearing this matter, "MSC" means the Manitoba Securities Commission. Wayne Sokal is referred herein as "Sokal" and Grant Kaufmann is referred to herein as "Kaufmann". In addition reference to "Respondents" shall mean "Sokal" and "ESP" as may be applicable. We commenced hearings into this matter on January 9, 2019, continued same on April 24, 2019, May 13, 2020 and January 17 – 20, 2022.

MSC issued Order No. 7500, dated December 3, 2019 authorizing any party to this hearing to bring any preliminary motion for any issue before this MSC Panel including applicability of section 148.2(7) of the Securities Act.

We then ruled that any party in this matter would be entitled to file a Motion before us on any matter dealing with the subject matter set forth in the Notice of Hearing dated the 15th day of November, 2018 as amended on April 5, 2019 and Statement of Allegations dated the 15th day of November, 2018 as amended the 5th day of April, 2019: Amended Notice of Hearing and Statement of Allegations being filed as Exhibits 3 and 4 herein.

Having made the above noted ruling we accepted the Notice of Motion filed by Mr. Stacey, on behalf of his client, Kaufmann, dated March 31st, 2020, and supporting affidavit. We then adjourned the proceedings pending receipt of written argument dealing with the subject matter of the Notice of Motion.

Initial Decision

Upon review of the affidavit executed by Kaufmann and upon hearing counsel and receiving written argument filed by Mr. Stacey and Mr. Barnes Trickett, respective counsel for Kaufmann and the Respondents, we delivered our Decision dated June 19, 2020. We ruled that an application for financial loss by Kaufmann was in the public interest, was in accordance with the Act and that we would hear the application.

Hearing dates were then set to commence on the issues set forth in the Amended Notice of Hearing and amended Statement of Allegations and the Hearing commenced on January 17th through January 20th, 2022.

Allegations

The allegations in this matter are against ESP Software Inc. ("ESP") and Sokal, together the Respondents. Mr. Poushangi appeared on behalf of Commission Staff, Mr. B. Barnes Trickett and Mr. Favereau appeared on behalf of Sokal, Mr. Stacey from time to time as necessary, on behalf of Kaufmann, no one appearing on behalf of ESP. It was noted that ESP was incorporated under the Companies Act, Manitoba and that, some time following its date of incorporation, ESP was dissolved in accordance with the provisions of the said Companies Act. No evidence was submitted indicating that ESP, since dissolution, had ever been reinstated.

We are charged with the responsibility of determining some if not all of the allegations contained in the Amended Statement of Allegations (Exhibit 4) are proven and whether to make and grant an order or orders as set forth in the Amended Notice of Hearing filed as Exhibit 3 as follows:

1. whether or not it is in the public interest to order, pursuant to subsection 148.1(1) and/or s 148.1(1.1) of *The Securities* Act ("Act"), that Wayne Sokal ("Sokal") and ESP Software Inc. ("ESP") pay an administrative penalty;

2. whether or not it is in the public interest to order, pursuant to subsection 19(5) of The Act, that:

   (a) subsection 19(1) of the Act does not, with respect to such of the trades referred to in that subsection, apply to Sokal and ESP;

   (b) subsection 19(2) of the Act does not, with respect to such of the securities referred to in that section, apply to Sokal and ESP;

3. whether or not it is in the public interest to order that Sokal and ESP pay costs of and incidental to the hearing;

4. whether or not it is in the public interest to order, pursuant to subsection 148.3(1) of the Act, that Sokal be prohibited from being a director or officer of an issuer.

5. whether or not, pursuant to section 148.2 of the Act, Sokal and ESP be required to pay compensation for financial loss to G.K.

6. such further and other matters and the making of such further and other orders as the Commission may deem appropriate.

Background Facts

1. ESP was a corporation incorporated pursuant to the laws of Manitoba with head office based in the Town of Dugald, in the Province of Manitoba. ESP was dissolved by the Manitoba Companies Office in 2017.

2. ESP owned the website domain name "www.pokercity.com" and managed the operations of the website.

3. Sokal is a resident of the Town of Dugald, in the Province of Manitoba, and was at all material times the only shareholder, director and officer and incorporator of ESP.

4. Neither Sokal or ESP were registered in any capacity with MSC under the provisions of the Securities Act (the "Act").

5. Commission Staff submitted the Amended Notice of Hearing and the Amended Statement of Allegations subsequent to receiving an application for claim for financial loss by Kaufmann. Commission Staff requested that this MSC Panel order:

> "whether pursuant to section 148.2 of the Act, Sokal and ESP be required to pay compensation for financial loss to Kaufmann".

6. Kaufmann is a resident of the Rural Municipality of Springfield, in the Province of Manitoba.

7. On June 10, 2020, as stated, we published Reasons for Decision stating that the application to this MSC Panel for claim for financial loss by Kaufmann was in the public interest and was in accordance with the Act.

8. On July 9, 2020, Counsel for the Respondent filed a Notice with the Manitoba Court of Appeal requesting leave to appeal regarding the decision of this MSC Panel dated June 10, 2020.

9. The facts as laid out in the Amended Statement of Allegations and confirmed through testimony of Sokal and Kaufmann include the following:

a) In October, 2006 Kaufmann met Sokal through a mutual friend. Subsequent to this encounter, both attended a number of social events including a Christmas dinner at Sokal's home.

b) In the spring of 2007, Sokal invited Kaufmann to his home on a number of occasions. On the occasions where Kaufmann attended to Sokal's home, Sokal solicited Kaufmann to invest in shares of an online poker company Sokal was planning on starting: "Poker City".

c) On or about August 23, 2007, Sokal solicited and received from Kaufmann $10,000.00 USD for investment in shares of ESP.

d) On or about September 25, 2007, Sokal solicited and received from Kaufmann a further $10,000.00 CDN for investment in shares of ESP.

e) On or about November 23, 2007, Sokal solicited and received from Kaufmann a further $67,500.00 CDN for investment in shares of ESP.

f) Between November 15, 2007 and November 23, 2007, Sokal recorded the issuance of a share certificate for 102,500 non-voting Class A shares of ESP in Kaufmann's name.

g) In or about March, 2009, not having received repayment of any of his funds nor any profits promised to him, Kaufmann asked and was granted access to the corporate bank account of ESP. In the opinion of

Kaufmann all funds advanced were to be allocated for the operation of ESP, but some of such funds were not utilized for business purposes.

h) In or about April 2009, Sokal solicited Kaufmann for further investments in ESP. Kaufmann refused Sokal's request to invest further monies in ESP.

i) A Statement of Claim was filed by Kaufmann against ESP and Sokal in the Manitoba Court of Queen's Bench on November 15, 2013.

j) On May 2, 2014, ESP and Sokal filed a Statement of Defense denying all allegations contained in the Kaufmann Statement of Claim.

k) On May 27, 2014 a letter was sent from Sokal and ESP to Kaufmann advising Kaufmann that the additional $10,000.00 USD that Kaufmann was required to pay for additional ESP shares was in arrears, and that Kaufmann's failure to pay would result in a reduced number of shares to be issued to Kaufmann for his initial investments and for the additional $10,000.00 USD amount now claimed to be in arrears and that all shares allocated to Kaufmann would be returned to the ESP corporate treasury.

l) On September 1, 2014, a letter was sent from Sokal and ESP to Kaufmann informing him that due to the balance of $10,000.00 USD still being in arrears, that he, Sokal, being the sole director of ESP, made the decision that ESP revoke all 102,500 shares into corporate

treasury for non-payment, with an internal valuation of $0.038 USD per share, resulting in a reduction in the amount of the arrears of $10,000.00 USD to $6,105.00 USD still being owed, with immediate action to follow.

m) In response to enquiries made by Commission Staff, Sokal on or about January 23, 2015 provided Commission Staff with documentation showing that between October 2, 2007 and November 23, 2007 Sokal and ESP issued 62,500 shares in ESP to four additional Manitoba residents for valuable consideration.

Evidence

Commission Staff submitted that, despite the lengthy testimony and extensive documents filed as Exhibits "the instant case is actually a simple one".

With respect we are unable to agree.

Commission Staff filed written argument with us with several binders containing numerous authorities and articles to assist us in our deliberations and, once Sokal's counsel had filed their written argument and binders containing their authorities, then Commission Staff managed to file further argument in response to the brief of Sokal's counsel and containing further authorities.

Add to all of this material, the transcript of more than 1,000 pages, we have concluded a "Simple One" it is not.

Exhibit 5 makes it clear that Sokal and ESP:

a) have never been registered in any capacity under the provisions of the Act;

b) have never filed a preliminary prospectus or prospectus with MSC;

c) have never applied for or been granted any exemption orders from the Commission under section 20 of the Act;

d) have never filed any reports under clause 7 of the Regulation to the Act or any notices under clause 91 or 92 of the Regulation with respect to any trades under section 19 of the Act or clauses 90 or 91 of the Regulation; and

e) have never filed any reports of any exempt distribution under National Instrument 45-106 in respect of any securities of ESP.

Family, Friends and Business Associates

The Family, Friends and Business Associates exemption is available where the person who purchases the security falls into the category of a close personal friend of a director, executive officer or control person of the issuer.

Commission Staff submits that the Family, Friends and Business Associates exemption does not apply to any trades carried out by Sokal and ESP such that such exemption would have exempt Sokal and ESP from being registered under section 6(1) of the Act and exempted Sokal and ESP from any requirement to file with MSC a preliminary prospectus and prospectus and from obtaining receipts from the Director of the MSC. While not an absolute requirement we note that Sokal did not obtain any documents from Kaufmann stating that he, Kaufmann, qualified under the provisions of the Friends exemption which, had he Kaufmann, so qualified, would exempt Sokal/ESP from complying with the provisions of the Act with respect to Kaufmann's investment.

Kaufmann had known Sokal for just a few months prior to investing in ESP. The Respondents have failed to demonstrate that they were entitled to the family, friends and business associates exemption in dealing with Kaufmann.

Sokal's counsel submits that it is Commission Staff's burden to demonstrate that Kaufmann is part of "the public". While we do not necessarily agree that such burden is that of Commission Staff, ultimately the responsibility to decide that Kaufmann is part of "the public" is the panel's responsibility – a "question of fact" as stated in various cases to which we have been referred.

In our view we must make our decision – a "question of fact" on the evidence before us.

How the securities are marketed – if marketed at all – may, depending on circumstances assist us in determining if Kaufmann is a member "of the public". No real evidence exists on this point.

We find that what may or may not have been set forth in a prospectus is not the issue. Kaufmann is not the author of nor is he required to be the author of any prospectus. That responsibility rests solely with Sokal and ESP.

Limitation of Actions Act

We acknowledge the limitations set out in this legislation and comments made by Sokal's counsel with respect to Section 148.2(3) of the Act. However we find that the Limitation of Actions Act does not apply to the Act.

Comments by Sokal's Counsel on Kaufmann's Claim

As to section 148.2(3) of the Act, this panel issued its decision on this section dated June 20, 2020. We understand that Sokal's counsel has requested leave to appeal to the Manitoba Court of Appeal. We refer the Respondent to our opinion. Our decision remains in effect. We make no comment with regard to comments by Sokal's counsel on Type of Proceedings, which Limitation Periods Apply, and where the Manitoba Securities Commission may be considered Her Majesty or the Crown.

Public Interest

Finally with respect to submission by Sokal's counsel on the issue of "the Public Interest" we find that indeed there is "the Public Interest" aspect to these proceedings and this Panel has made its determination in that regard based upon all of the facts in evidence. Yes the "Public Interest" is a factor considered by this Panel. We agree with Commission Staff that issuers who do not comply with section 6(1) and section 37(1) of the Act and are not otherwise subject to exemption from such sections set out in a manner contrary to the "Public Interest" with which the MSC have every right and obligation, under the Act, to supervise, direct and address.

We have disregarded any evidence suggesting financial management of ESP was "dilatory" meaning there were certain personal expenditures, applicable to Sokal, out of the ESP bank accounts. We make no decision relating thereto other than to state we agree with Sokal's Counsel – controlling and directing how accounting records are to be organized and maintained, at least in this case, is not a function of the MSC.

Observations

While the length of time that an investor may know the issuer of securities is but one consideration in determining that the Friends, Family and Business Associates exemption may apply. In Kaufmann's case he had known Sokal for just a few months prior to investing in ESP. It is noteworthy that the other investors in ESP Software were known by Sokal for much longer.

Gary Gach for 50 years;

Larry Chartrand for 40 years;

Christina Bellerose for 30 years; and

Don Perry for 9 years.

Companion Policy NI 45-106 states that the Friends, Family and Business Associates exemption is premised on the ability of an investor to assess a person's capabilities and trustworthiness.

Having set out the Friends, Family and Business Associates exemption generally, and assuming it is available, it is necessary to discuss the rationale of the exemption.

The Companion Policy to NI 45-106 states the regulator's views of the meaning of "close personal friend" and "close business associate" of a person who is a director, officer or founder. These policies state that the relationship must at the time of the trade, be of a nature that the investor can assess the person's capabilities and trustworthiness. An investor purportedly a closer personal friend must have known that person well enough, and have known them for a sufficient period of time to make that assessment...

Was the relationship for a sufficient period of time to establish a knowledgeable relationship? We find that the answer to this question is: no.

We have noted the decisions referenced in the Solara Technologies Case, Re 2010, BCSECCOM 163, 2010 Carswell BC 4397, the Verify Smart Corp. Case, Re 2011 BSSECCOM 599, 2010 Carswell BC 4053 and the Limelight Entertainment Case Re 2008 ONSEC 4, 2008 Carswell Ont 680,310 OSC B1727. These cases suggest that the person who is relying on the exemption should be able to demonstrate that the exemption is valid.

In Solara Technologies Inc. case the Court stated that the issuer who chooses to rely on an exemption has the responsibility to ensure that the Act is being complied with. An assertion that a person is a close personal friend is not sufficient to determine whether an exemption is available.

Furthermore in the Solara Technologies Inc. case, the Court stated:

> "When the person chooses to rely on an exemption, two considerations are relevant to the responsibility to ensure compliance with the Act. First the person trading has the onus of proving that the exemption is available. Second, it is unlikely an issuer will be able to prove that an exemption was available at the time of trade if it does not have documentation to prove it made a proper determination to that effect. A representation that merely asserts, with nothing else, that the investor is a close personal friend, or an accredited investor is not sufficient to determine whether an exemption is available."

In the Verify Smart Corp. Case the Court concluded that it is the person trading in securities responsibility to ensure that the trade complied with the Act.

The Court in the Verify Smart Corp. case stated:

> "It is the responsibility of a person trading securities to ensure that the trade complies with the Act. This is so whether the person chooses to comply by filing a prospectus, or by using an available exemption."

The Ontario Securities Commission in the Limelight Entertainment case stated that the onus is on the Respondent to provide that an exemption from the requirements of the Act have been satisfied.

In Limelight Entertainment Inc. case it was stated:

> "Staff has established that the Respondents traded without registration and distributed shares without qualifying those shares under a prospectus. Having done so, the onus shifts to the Respondents to prove that an exemption from those requirements was available in the circumstances."

As apparent from the above, case law makes it clear that the onus to show that exemptions to the Act are available is on the Respondents. This principle is also supported by NI 45-106CP.

In the Lavallee case, 2007 ABASC 794, the Court outlined the general rational for registration and prospectus exemptions. In short exemptions are the exceptions as registration is meant to assist the investor in making an informed decision.

The Court described the general rationals for registration and prospectus exemptions as follows:

> "Prospectus and registration exemptions are departures from basis requirements.....
>
> ...registration is designed to give investors the benefits associated with the involvement of a registrant who is knowledgeable about securities....
>
> ....The prospectus requirement is meant to assist the investor in making an informed investment decision by providing reliable facts relating to matters such as the issuing company, its management, the offered securities and the risks involved."

Conclusion

We have concluded:

a) that Kaufmann personally and/or carrying on business under the firm name and style of G. Kaufmann Truckyn & Equipment Rentals invested $10,000. USD and $77,500. CDN in ESP upon representations made to him by Sokal;

b) that Sokal is a "person" as defined in the Act;

c) that ESP is a "company" as defined in the Act;

d) that Sokal and ESP engaged in trading as defined in the Act within the Province of Manitoba.

Counsel for Sokal relies on two points of law, namely:

a) that the prospectus requirement set out in the Act does not apply as Sokal did not offer securities "to the public", a necessary condition required to trigger the

> prospectus requirement and "To Sokal, Kaufmann was not a member of the public".

With respect, we do not accept this position.

It is true and correct that:

> "the public consists of those members of the community at large who need the protection of the regulatory framework to make an informed investment decision".

We also acknowledge that the two tests, both of which are recognized by counsel for the parties, are the "need to know test" and the "common bonds test" and that the "common bonds test" is most normally applicable in Canadian law. We also note that it is not necessary that both tests be applicable to exclude an investor from falling into "the public category".

The "public" need not consist of any specific number of parties. As stated in R. v. Empire Dock Ltd., 1940 Carswell BC 104, 55 B.C.R. 34:

> "when the term is used, it must be considered as relative to the question at issue and the circumstances of each particular case"

-and-

We refer to R. v. Piepgrass 1959, 29 WWR 218, wherein the Alberta Court of Appeal stated:

> "It is clear from the cases cited and from the authorities cited that it is impossible to define with any degree of precision what is meant by the term "offer for sale to the public" ....

It is clear from the authorities that whether or not there was an offering to the public is a finding of fact: supra Piepgrass at paragraphs 30 – 34.

In our opinion then we find as a fact that circumstances surrounding the events wherein Kaufmann advanced funds to Sokal and/or ESP – the company in which Sokal is the guiding light as incorporator, shareholder, director and officer – do not remove Kaufmann from falling within the category of "public". Again then:

> We find that the Respondent has failed to demonstrate that Kaufmann falls into the category of the Family, Friends and Business Associates exemption.

We reviewed copies of ESP share certificates, ESP shareholder ledgers (Exhibit 9) which, indicate Mr. Kaufmann owning shares in ESP in exchange for cheques issued by Kaufmann to ESP totalling $10,000.00 U.S. and $77,500.00 CDN. Exhibit 9 also indicates shares to be issued, or issued to four individuals – Gary Gach, Don Perry, Larry Chartrand and Christina Bellerose. Sokal's evidence was that he had been friends with these four individuals for many years respectively. There has been no suggestion that these four individuals were members of the public – rightly so but Sokal and Kaufmann's connections are very much less. That is not to say that a short time of association may not cause an individual to "not be a member of the public", but it is a factor to consider. The circumstances and instances surrounding their relationship must be considered as must Sokal's relationship with others. Sokal testified that he

and Kaufmann were friends sufficient that Kaufmann was not a member of the public. Kaufmann testified to the contrary.

Kaufmann's evidence was he worried about getting his money back, that he pressed Sokal about payment, that eventually Sokal authorized Kaufmann to access the bank account details – all after the fact.

Sokal's evidence as to their relationship rested on a few backyard parties – and little else – there is no evidence that he ever met and talked with Kaufmann about Kaufmann investing in ESP.

b) Secondly, that the claim by Grant Kaufmann for financial compensation pursuant to 148.2 of the Act should be barred based on the interpretation of The Limitations of Actions Act.

With respect, we do not accept this position.

After a thorough review of The Limitations of Action Act we find that it does not bar Kaufmann from financial compensation pursuant to 148.2 of the Act. It is true that the Limitations of Action Act does apply in numerous scenarios involving civil proceedings and prosecutions and has consistently applied across provincial jurisdictions to apply to court proceedings.

However, the Manitoba Securities Commission is an independent tribunal not a court of law. In addition, under section 2(3) of the Act this proceeding is considered administrative.

When we consider the distinction between administrative actions and civil proceedings, we considered the function of the Manitoba Securities Commission which is to maintain the public trust in local capital markets systems. While ensuring facilitation of capital raising activities, our overarching function is to ensure the protection of investors. We are able to do this through the administration of the Act.

In addition, based on reasoning above, we do not hold Orders for Financial Loss to be akin to private actions in civil proceedings due to these orders being in the interest of the public and are not orders issued for the benefit of private parties seeking redress or remedies. The Commission is limited in its authority that pertains to the Act and our findings cannot include an award for general damages, punitive damages or interest.

Finally, the Commission has on two occasions decided The Limitations of Actions Act does not apply. In Jack Hiebert Neufeld, Geoffrey Scott Edgelow and The Jack Neufeld Family Charitable Foundation, Re: 2017, (MSC). 493, it was determined on page 3, para 4) that

> "...applying the LAA to non-prosecutorial [non-civil] proceedings under the Act would not protect the public interest".

In addition, this MSC Panel reiterates its own 2019 decision made in the Madison Street Limited Partnership, 5218838 Manitoba Ltd. and Brenda Andre, 2019 (MSC).

Order

Comments on the issue of delays in this matter may be forthcoming.

We hereby determine that it is in the public interest, pursuant to section 19(5) of the Act, to order and we hereby order that:

a) subsection 19(1) of the Act does not with respect to such trades referred to in that subsection, apply to Sokal and ESP;

b) subsection 19(2) of the Act does not, with respect to such of the securities referred to in that section, apply to Sokal and ESP;

c) that, pursuant to subsection 148.3(1) of the Act, Sokal is prohibited from being a director or officer of an issuer;

d) that pursuant to section 148.2 of the Act, Sokal pay compensation for financial loss to Kaufmann in the sum of $77,500.00 CDN. and $10,000.00 USD on that date, which date shall be on or before the 1st day of June, 2023, being the final date upon which Kaufmann shall be entitled to satisfy the Director of the MSC that the action that he has commenced against Sokal and ESP in the Manitoba Court of Queen's Bench, has been discontinued, that he has consented to a judgment of the Court of Queen's Bench dismissing the action, staying the action or otherwise abandoning the action on terms acceptable to the MSC.

Argument - Additional Hearing Dates

Upon completion of the hearing, written argument was received with Books of Authorities for our consideration. It was understood that, once we had rendered decisions on the issues then further hearing dates would be set to allow the parties to present argument as to whether we should order (a) payment of an administrative penalty; (b) costs of the investigation and this Hearing; and (c) identify the parties and the amounts to be paid by any such parties and (d) any other matter arising out of this Hearing.

Note: In our June 10, 2020 decision dealing with the Kaufmann motion, we stated that costs in connection with that motion shall "be considered upon completion of the hearing". Parties are therefore expected to address the question of costs on the Kaufmann Notice of Motion.

"J.T. McJannet, Q.C."
J.T. McJannet, Q.C.
Panel Chair

"C.D. Burns"
C.D. Burns
Member

"D.A. Huberdeau-Reid"
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Member