

IN THE MATTER OF
THE SECURITIES ACT, 1988, S.S.1988, c.S-42.2

AND

IN THE MATTER OF

HAROLD GERHART

AND

GLOBAL FINANCIAL RESOURCES INC.

AND

UNIVERSAL POLLUTION CONTROL (INT.) INC.

D E C I S I O N

Hearing conducted on July 18, 1989

Hearing panel: Marcel de la Gorgendiere, Q.C., Chairman
Herbert Dow, Commission member
Morley Meiklejohn, Commission member

Appearances: J.M. Hall for the Commission staff

Cameron McCannell for Harold Gerhart, Global
Financial Resources Inc. Universal Pollution
Control (Int.)Inc.

Decision dated September 8, 1989

IN THE MATTER OF
THE SECURITIES ACT, 1988, S.S.1988, c.S-42.2

AND

IN THE MATTER OF
HAROLD GERHART

AND

GLOBAL FINANCIAL RESOURCES INC.

AND

UNIVERSAL POLLUTION CONTROL (INT.) INC.

D E C I S I O N

The Commission is asked to determine if it is in the public interest that all trading in the securities of Universal Pollution Control (Int.) Inc. ("Universal") shall permanently cease and that Harold Gerhart ("Gerhart") and Global Financial Resources Inc. ("Global") cease trading in Universal securities; and that any exemptions of The Securities Act, 1988 (the "Act") and its regulations not apply to any trades in securities of Universal by Gerhart, Global and Universal. The question is whether trades were made of securities as they are defined in the Act and regulations.

There is no dispute as to the following facts set out in the Amended Notice of Hearing:

1. Global and Universal are bodies corporate, registered to carry on business in the Province of Saskatchewan;
2. Gerhart is the President and a Director of both Global and Universal and he resides at the City of Regina, in the Province of Saskatchewan;
3. Gerhart, Global and Universal (sometimes hereinafter

collectively referred to as the "Respondents") have from February, 1988 to date solicited and received the approximate sum of \$163,000.00 from ten Saskatchewan residents wishing to receive distribution and marketing rights for waste liquid disposal systems ("Products") to be manufactured by Universal;

4. The Respondents are not and have never been registrants within the meaning of the Act;
5. Universal and Global are not reporting issuers within the meaning of the Act, nor has a receipt been issued by the Director to the Respondents for a prospectus with respect to any distribution of securities by the Respondents within the meaning of the Act, nor has an exemption within the meaning of the Act been granted to the Respondents.
6. The Saskatchewan residents have individually entered into contracts ("Distribution Agreements") with Universal;
7. The Distributor Agreement provides that each of the Saskatchewan residents pays to Universal a sum of money as a product prepayment and that Universal guarantees the delivery of products to the Saskatchewan residents within 120 days of the Distribution Agreement;
- ...
- 10.2 The Respondents are not licensed or exempted from licensing pursuant to The Mortgage Brokers Act;
11. The Respondents did not at any time prior to June 16, 1989 set up a trust account or segregated account to hold the approximate sum of \$163,000.00 received from the Saskatchewan residents nor did the Respondents establish any fund from which to make repayment of the amounts referred to in paragraph 9 above;
12. The product prepayment amounts received from the Saskatchewan residents, totalling approximately \$163,000.00, went into the general funds of the Respondents. The Respondents have expended all of this money in the development of Universal's products;
13. No products have either been allocated or delivered to any Saskatchewan residents to date and as Universal's products are

still in a developmental stage, Universal is not capable of making allocation or delivery of any products until the manufacturing process has commenced;

14. No date has been established for the commencement of the manufacturing process for Universal's products;
15. Neither Global nor Universal have any significant assets nor have current audited financial statements been prepared for either company; It was agreed by both counsel that this point should indicate that the Respondents have no significant assets other than a licensing agreement with the patent holder of a waste disposal system;

By way of a written undertaking provided to the Commission staff dated the 15th of June, 1989, Gerhart, Global and Universal (the "Respondents") acknowledged that:

1. From February, 1988 to date they solicited and received the approximate sum of \$163,000.00 from Saskatchewan residents wishing to receive distribution and marketing rights for products to be manufactured by Universal;
2. They have expended all monies received from Saskatchewan residents in the development of Universal's products;
3. No products have been delivered to Saskatchewan residents to date and as Universal's products are still in a developmental stage, Universal is not capable of making delivery of any products until the manufacturing process has commenced;
4. No date has been established for the commencement of the manufacturing process for Universal's products;
5. The staff of the Saskatchewan Securities Commission (the "Commission") has advised the Respondents that in the opinion of the staff, the activities of the Respondents in soliciting and receiving funds from Saskatchewan residents constitutes trading in securities within the meaning of The Securities Act, 1988, S.S. 1988, c. S-42.2 (the "Act");
6. They are not and have never been registrants within the meaning of the Act;
7. Universal and Global are not reporting issuers within the

meaning of the Act, nor has a receipt been issued by the Director to the Respondents for a prospectus with respect to any distribution of securities by the Respondents within the meaning of the Act, nor has an exemption within the meaning of the Act been granted to the Respondents.

The Respondents also undertook among other things to place in trust with their solicitor all sums received in Saskatchewan to be returned on certain conditions to the individuals, a condition that was not complied with by the hearing date.

The disagreement with the Commission staff is over whether the documents including the contract and accompanying booklet and conduct of Gerhart constituted trading in a security. These documents were unique. They attempted to transfer a right to sell a product (Distributorship) in a specific area as well as constitute an order for the item to be distributed and give a right to apply for a low interest loan on assets to be provided by the purchaser as well a credit for additional product if there was any delay in providing it after the agreed date. It also included a right to a refund together with interest if the product was not delivered by the agreed date in regard to which the information distributed provided for the execution of promissory notes in favor of the investor.

The Respondents agreed to a cease trade and removal of exemptions requested related to the sale of any security that provided for any financing or loan agreement. The Respondents' counsel acknowledged the agreement's constituting a security by virtue of it providing for loans if nothing else. The issue to be decided then was whether an agreement without that provision but providing for the distributorship of the product and providing for a credit on the purchase of product or for interest in lieu in the event of delay would constitute trading in a security as defined in the Act namely by virtue of being a trade in income contracts, debt instrument, or investment contracts.

The Respondents used this contract according to the needs of the purchaser, either as a distributorship for a pollution reduction device to which was attached the possibility of a low interest loan which was a priority to the investor or if it was perceived the investor has a real interest in investing in the distributorship with no interest in obtaining a loan, the interest payable would be stressed in the alternative in any delay of

delivery. The final contract would vary between the parties as a result.

The other uncontroverted fact in evidence (the Respondents produced no witnesses) was that regardless of when the contracts were entered into all parties were told that there would be a product for sale in no later than 120 days. However, there was no contract in existence to manufacture more items to sell. Only the one prototype shown investors existed.

The fact is that regardless of what the investors were told by Gerhart about the commencement of sales there was no means of complying with the agreement as promised and no means of completing the agreement other than with additional funding from more "distributorship" sales. Independently obtained financing might conceivably be used but the Respondents provided no evidence that it was in place or that funds were retained to ensure completion or finance production. The Respondents' counsel suggests that there was financing potential from the exclusive agreement the Respondents had with the patent holder of the prototype. Evidence was presented to show however that the patent holder, Raymond Patrick Britz, had been convicted of fraudulent misrepresentation of a patent of an identical or similar type. The Respondents' counsel was surprised at this fact stating it to be unknown to him. He then confronted his client Gerhart with the certificate of conviction and it was obvious that it was not unknown to Gerhart. That conviction would no doubt affect any financing potential.

The Commission holds that even an agreement of the type considered by the Respondents not to be a security, a distributorship sale with a credit on delay for more product or interest is in fact a security. This arises because there is no product in existence. It would not be a scheme to provide for distribution but rather at best a scheme to raise money for production. The only way this should be done is by full disclosure by prospectus of all relevant risks. If the Respondents had even had a bona fide contract with set delivery dates with a reasonable competent manufacturer one might have considered that they were selling a distributorship and product rather than a security. But where they had none and were only raising funds which one might charitably presume they intended to use eventually for production they were dealing in a contingent interest in a document that could only be considered a security.

This interpretation is consistent with section 2(1)(ss) of the Act the instrument being a document constituting evidence of title to or interest in the assets or earnings of a person 2(1)(ss)(ii) or a note or other evidence of indebtedness or...certificate of a share or interest, ... 2(1)(ss)(v) or any agreement providing that money received will be repaid or treated as a subscription to...units or interests at the option of the recipient or of any person or company 2(1)(ss)(vii) and if by virtue of none of these then as any investment contract 2(1)(ss)(xiv) .

The test of what is an investment contract is outlined by the Supreme Court of Canada in Pacific Coast Coin and OSC December 1977 O.S.C.B. 322(SCC) where it modified the "Howey" test requirements of investment of money, in a common enterprise, in expectation of profits, solely from the efforts of the promoters or a third party.

Rather than "solely" it was determined that it was only necessary that the managerial effort of the promoter or some other person played an essential or substantial role in the making of the profits. The Commission finds that in either the actual scheme or the proposed one the Respondent would have to arrange to have the product manufactured. That fact is sufficient to make the interest sold a security regardless of its other attributes. It is a significant factor distinguishing this agreement from a franchise to sell "Watkins" products or "Fuller Brushes".

The circumstances attached to the sales involved here show how warranted the requirement is to treat the interest as a security requiring full disclosure through a prospectus. It would be doubtful if anyone would have invested if they knew the true state of the likelihood of manufacture or the backgrounds of the promoter and the patent holder.

Having decided the contract in any event is a security on these grounds it is not necessary to decide if it is on any other ground such as a debt instrument and if so whether as such it is exempt under section 81(1)(e). The Respondents have the opinion of the Commission that any agreement even modified to remove financing provisions and the interest or product credit constitutes a security in the absence of product.

The order requested by the Commission staff is therefore granted for a permanent cease trade of Universal Pollution Control

securities and that Harold Gerhart and Global Financial Resources Inc. be ordered to permanently cease trading of any securities of Universal and that the exemptions contained in The Securities Act, 1988 and the regulations be by section 135(1) ordered not to apply to any trades in securities of Universal by Gerhart, Global and Universal.

DATED at the city of Regina, in the Province of Saskatchewan this 8th day of September, 1989.



MARCEL de la GORGENDIERE, Q.C.
CHAIRMAN
SASKATCHEWAN SECURITIES COMMISSION