Osgoode Hall Law Journal

Volume 14, Number 3 (December 1976) Article 3

December 1976

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MENS REA AND PUBLIC TRADES PROHIBITED UNDER *THE SECURITIES ACT*

By D. A. B. STEEL*

Lawyers sometimes have difficulty advising a client concerning statutory prohibitions of actions done for a specific purpose. The client wants to know how a court would determine that his action was done for the specific purpose prohibited by the statute. Is the purpose ascertained from the actual consequences of the action or from what a reasonable person could have foreseen to be the consequences? Or do the client's actual intentions at the time determine the purpose of the action, and, if so, does it make any difference to his guilt if he was unaware of the statutory prohibition?

Sections 35 and 57 of *The Securities Act* of Ontario[1] contain prohibitions of this kind. Section 35(1) prohibits any trade in the course of distribution to the public until both a preliminary prospectus and a prospectus have been filed with the Securities Commission and receipts issued.[2] Section 57 restricts the kind of printed and written materials that may be sent out by someone trading in a security in the course of distributing that security to the public. Both subdivisions of the definitions contained in s. 1(1) 6a of the Ontario Act identify a "distribution to the public" as trades made "for the purpose" of distributing securities to the public. "Trade" or "trading" is defined to include any dealing or attempt to deal with a security for valuable consideration or any act directly or indirectly in furtherance of such dealing or attempt. This broad definition of "trade" covers many different kinds of things done in connection with securities transactions expected to take place in the future, including transactions which may or may not be for the purpose of distributing securities to the public.

Many investment dealers, for example, publish newsletters and reports which contain descriptions of companies whose shares are listed on a stock exchange. Salesmen send these letters and reports to customers mainly for the purpose of enabling them to decide whether to buy, sell or hold the shares. In most cases, therefore, sending the newsletters or reports constitutes a "trade".

From time to time, companies whose shares are listed on a stock exchange file with the Securities Commission preliminary prospectuses relating to a proposed issue of securities. The question then arises as to the legality of the distribution of the newsletters or reports describing such a company.

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[1] R.S.O. 1970, c. 426.

[2] This is subject to s.(2) of the Act which permits the distribution of certain documents during the "waiting period".

In this situation, there are three possible intentions in sending out the newsletter. First, it may be admitted that the report or newsletter was sent out to the customers for the purpose of selling some of the securities proposed to be issued under the prospectus and with knowledge that this act was wrongful (*i.e.*, prohibited by s. 35 and not permitted by s. 36(2)). Another possibility is that although sending out the newsletter or report was for the purpose of selling some of the prospectus securities, it may be denied that it was done with knowledge of the prohibition. Thirdly, irrespective of any knowledge of the prohibition, the report or newsletter may have been distributed not for the purpose of selling any of the prospectus securities but rather of effecting a trade in another security (*e.g.*, the listed shares). To what extent are either of the two latter possibilities available as a defence to a prosecution under Part XIII of the Ontario Act?

It is surprising that "ignorance of the law" (*i.e.*, unawareness that an action is prohibited by law) should ever be put forward as a defence to a prosecution for breach of the prohibition.[3] Nevertheless, it does happen occasionally.[4] Defence counsel follow the following chain of reasoning. First, it is submitted that the doctrine of *mens rea* applies to the offence in question. Although there is a general presumption that any offence requires both *actus reus* and *mens rea* as essential ingredients, there are certain categories of "strict liability" offences where proof of the guilty act alone is sufficient for conviction. These categories were described by Wright, J. in *Sherras* v. *De Rutzen*,[5] and have been adopted in other decisions. They are:

(1) where the offences are not criminal in any real sense, but are acts which in the public interest are prohibited under a penalty (*i.e.*, revenue statutes); or

(2) public nuisances; or

(3) where, although the proceeding is criminal in form, it is really only a summary mode of enforcing a civil right (*i.e.*, unintentional trespass).[6]

Even where the offence falls within one of the strict liability categories, it may be described by the prohibiting statute in such a way that a mental element is imported into it. Words such as "knowingly" and "wilfully" and expressions like "with intent" have this effect. So also do phrases such as "acquiescing in" and words like "authorizing" and "permitting", and, as will

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[3] One of the more extreme examples of the failure of this defence is *R.* v. *Bailey* (1800), 168 E.R. 651 where the accused was found guilty of "malicious shooting", an offence created by statute enacted when he was at sea; he was still at sea when he committed the offence. The accused received a pardon in lieu of acquittal. The defence of ignorance of the law is excluded in criminal prosecutions by s. 19 of the *Criminal Code*, R.S.C. 1970, c. C-34 as amended.

[4] Sometimes successfully, as in *R.* v. *Ross*, [1945], 3 D.L.R. 574 where the accused was acquitted on a charge of entering (for the purpose of hunting) a "closed area" declared as such by ministerial order made the day after he left for his trip.

[5] (1895), 1 Q.B. 918.

[6] *Regina* v. *V.K. Mason Construction Ltd.*, [1968] 1 O.R. 399 at 404, *per* Lieff, J.; *Regina* v. *Pierce Fisheries* (1970), 12 D.L.R. (3d) 591 is a leading Canadian example of the operation of "strict liability".

be considered below, "for the purpose of". In cases where the mental element has been imported by the manner of describing an offence which is not in one of the strict liability categories, *mens rea* is a twofold essential ingredient: both as the intent specified as part of the offence, and also as knowledge of the factual elements constituting the guilty action. G. A. Ferguson described this twofold aspect succinctly in his article *Mens Rea Evaluated in Terms of the Essential Elements of a Crime: Specific Intent and Drunkenness.* He wrote:

> When a crime requires a specific intent, this intent is expressed in the definition of the crime. The required mental element of such a crime is an intent to do all the essential elements of the *actus reus plus* the special or additional intent specifically expressed in the crime. (emphasis added)[7]

Where words importing a mental element are lacking, the court still has the duty to determine if the offence falls into a strict liability category. As Ritchie, J. pointed out in the *Pierce Fisheries* case, the absence of such words is "not conclusive" in showing that the offence is one of strict liability.[8]

Having established (either by showing that the offence does not fall within one of the "strict liability" categories or by demonstrating the importation of a mental element by appropriate words or phrases in the statute) that *mens rea* is applicable to the offence, defence counsel attempts to show next that the doctrine of *mens rea* means that "an evil intention or a knowledge of the wrongfulness of the act is an essential ingredient."[9] If this famous dictum of Wright, J. were interpreted literally it would require knowledge that an act constituting an offence is wrongful to be an essential ingredient of that offence. What he really meant to say, however, must be that "knowledge of the wrongful act is an essential ingredient of every offence." In the *De Rutzen* case, the innkeeper knew that it was illegal to serve liquor to a police officer while on duty. He also knew that he was serving liquor to a police officer. What he did not know (and had no means of knowing) was that the police officer to whom he was serving the liquor was on duty at the time. And it was this last act which was wrongful. It is knowledge that the act that is being done is the kind of act that is prescribed in the prohibiting legislation which is the essential ingredient irrespective of any knowledge of that legislation. In the *De Rutzen* situation, it would not have been a defence that the innkeeper did not know of the prohibition so long as he knew the police officer he was serving was on duty.

The case of *Regina* v. *Brown*[10] related to trades which were prohibited under the provisions of *The Securities Act, 1962* of British Columbia[11] by reason of the accused not being registered thereunder. Verchere, J. held that ignorance of the prohibition did not excuse the appellant, *ignorantia juris neminem excusat.*[12] Although question number two in the stated case put to

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[7] (1971), 4 Ottawa U. Law Rev. 356 at 372.

[8] *Supra,* note 6 at 600.

[9] *Sherras* v. *De Rutzen, supra,* note 5 at 921.

[10] (1971), 16 D.L.R. (3d) 350 (B.C.S.C.).

[11] S.B.C. 1962, c. 55.

[12] *Supra,* note 10 at 354-55.

Verchere, J. specifically asked if the Provincial Judge was right in holding that *mens rea* was not an essential ingredient of the offence, Verchere, J. was careful not to base his judgment on the inapplicability of the doctrine of *mens rea. Mens rea* consists not of knowledge of the prohibition but of all the essential facts which together constitute the prohibited action.

This principle has been somewhat obscured by the judgment of the Appellate Division of the Alberta Supreme Court in *Regina* v. *Burkinshaw*.[13] This was an appeal by the Crown from an acquittal by Tavender, D.C.J.[14] of the charge of "authorizing, permitting or acquiescing in" an offence under *The Securities Act, 1967*,[15] namely trading in securities when not registered under that Act. Tavender, D.C.J. found at trial that the main offender (a co-operative trading company of which the accused were directors) had traded in securities when unregistered and that the accused were fully aware and in control of the actions of the main offender. He also found that *mens rea* applied to "authorizing, permitting or acquiescing in" an offence under the Alberta Act and that since the accused had obtained an opinion from a firm of prominent Vancouver solicitors that the offenders' proposed transactions would not constitute an offence, they were not guilty.

In giving the unanimous judgment of the Appellate Division of the Alberta Supreme Court, Clement, J.A. found that *mens rea* was not an essential ingredient either of the main culprit's offence or of the accused's offence of authorizing, permitting or acquiescing in the main offence. In incorrectly and unnecessarily denying that *mens rea* is an essential ingredient in "authorizing, permitting or acquiescing in" another person's offence, Clement, J.A. lent credence to Tavender, D.C.J.'s erroneous view that *mens rea* requires a knowledge of the applicability of the prohibition to the act in question.[16] In the facts of the *Burkinshaw* case, it was not possible for the accused to raise the defence of absence of *mens rea*. They knew exactly what the main offender had done. They were in fact its only agents in doing it. They therefore knew precisely what it was that they were authorizing, permitting or acquiescing in. For the defence of absence of *mens rea* to be available to them, they would have had to be able to show either that, to their knowledge, the actions of the main offender which they were authorizing, permitting or acquiescing in were not those which constituted an offence under *The Securities Act* of Alberta or that while they knew what the main offender was actually doing, they had not authorized, permitted or acquiesced in it. For example, if, in a

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[13] [1973] 5 W.W.R. 764.

[14] [1973] 3 W.W.R. 150.

[15] S.A. 1967, c. 76.

[16] The same error was made by Danis, J. in *Regina* v. *Wineberg*, [1955] O.W.N. 345 (Ont. H.C.) where he said at 349:

> The provisions of Section 111(3) [of the *Excise Tax Act*] especially the words "who has directed, authorized, condoned, or participated in the commission of the offence," lead me to conclude that *mens rea*, or an intention to do wrong or break the law, is a necessary ingredient of the offence, otherwise how could one condone, forgive or approve of an offence without knowing that it is an offence or that it is wrong?

The dictum of Danis, J. should properly only be applicable to the offence of "condoning" and not to those of "directing, authorizing or participating".

slightly different set of circumstances, the accused had been charged with authorizing, permitting or acquiescing in the main offender's mailing to the public at large an offer of memberships in the co-operative, and if in authorizing (or acquiescing in) the mailing in question the accused had been under the impression that what was being mailed was a brochure describing the co-operative and not an offer of membership, the defence of absence of *mens rea* would certainly have been available.[17]

It makes no sense to say, as did Clement, J.A., that the offence of authorizing, permitting or acquiescing in imports no consideration of *mens rea*. On the contrary, *mens rea* is the heart of the offence. If you do not know what in fact you are authorizing, permitting or acquiescing in, then you cannot be said to have authorized, permitted or acquiesced in it. Clement, J.A. based his dictum on the majority judgment of the Supreme Court of Canada in *Regina* v. *Pierce Fisheries* in which the Supreme Court of Canada upheld a conviction for possession of undersized lobsters even though the defendant lacked *mens rea* in that it did not know (and probably could not have known without an inordinate expenditure of time and money) that it had possession of them. In that case, however, Ritchie, J., in giving the majority judgment, stated:

> In considering the language of the Regulation [S. 3(1) (b) of the Lobster Fishery Regulations P.C. 1963 — 745, S.O.R./63-173] it is significant though not conclusive, that it contains no such words as "knowingly", "wilfully", "with intent" or "without lawful excuse"; whereas such words occur in a number of sections of the *Fisheries Act* itself which create offences for which *mens rea* is made an essential ingredient.[18]

Clement, J.A., therefore, had no authority for his dictum denying the applicability of *mens rea* in cases of authorizing, permitting or acquiescing in an offence. It would have been better if his judgment had been based on the defendants' admission that they knew they were "acquiescing in" the offering of memberships in the co-operative and upon *ignorantia juris neminem excusat*, namely that the assurance from their solicitors that this was not prohibited was no excuse.

Once it is admitted that a trade is for the purpose of selling securities to the public, there is clearly no defence available which can be based on the accused not being aware that such a trade is prohibited. But the reason why the accused cannot raise this defence is that ignorance of the law is no excuse, not that *mens rea* is not applicable.

The distinction between the two was made clear by Lebel, J. in delivering the judgment of the Ontario Court of Appeal in *Regina ex rel. Irwin* v. *Dalley*,[19] where the accused was held to have been "knowingly responsible"

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[17] The defence of absence of acquiescence was even less available to the accused than absence of *mens rea* since there were no other individuals involved whose actions they could have refrained from authorizing, permitting or acquiescing in.

[18] *Supra*, note 6 at 600.

[19] (1957), 8 D.L.R. (2d) 179 at 186-87.

for an offence under *The Securities Act* even though unaware of "doing anything contrary to law."[20]

That *mens rea* is applicable to the offence of breaching the prohibitions in ss. 35 and 57 of the Ontario Act will be shown when we examine the next possibility, namely that the trade (although made at a time when a preliminary prospectus had been filed and not of a character permitted by s. 35(2)) was nonetheless not prohibited in that it was for the purpose of effecting a transaction for value not in respect of the securities (to be distributed to the public) referred to in the preliminary prospectus but in respect of quite other securities (already distributed and not falling within the "control block" category of the definition of "distribution to the public").[21]

What is meant by the word "purpose" in connection with "distributing securities to the public"? In *Crofter Hand Woven Harris Tweed Co. Ltd.* v. *Veitch*, Lord Simon distinguished "intent" (in the context of intending all the reasonable consequences of one's acts) on the one hand from "purpose" or "object" (in the sense of one's main reason for doing something) on the other. He said:

> ... in some branches of the law, "intention" may be understood to cover results which may reasonably flow from what is deliberately done, on the principle that a man is to be treated as intending the reasonable consequence of his acts. Nothing of the sort appears to be involved here. It is much safer to use a word like "purpose" or "object". The question to be answered, in determining whether a combination to do an act which damages others is actionable, even though it would not be actionable if done by a single person, is not "did the combiners appreciate, or should they be treated as appreciating, that others would suffer from their action" but "what is the real reason why the combiners did it?" Or, as Lord Cave puts it, "what is the real purpose of the combination?" The test is not what is the natural result to the plaintiffs of such combined action, or what is the resulting damage which the defendants realize or should realize will follow, but what is in truth the object *in the minds of the combiners* when they acted as they did." (emphasis added)[22]

In *Sweet* v. *Parsley*, Lord Morris of Borth-y-Gest held that the offence of being concerned in the management of premises used for the purpose of smoking cannabis, by its wording, indicated that *mens rea* was an essential ingriedient of the offence.[23]

Lord Diplock stated that " 'purpose' connotes an intention by some person to achieve a result desired by him." Lord Diplock also found that knowledge of the facts constituting the offence was an essential ingredient by virtue of the use of the word "purpose".[24]

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[20] Other examples of the use of "knowingly" remitting in a requirement for evidence of a guilty mind in securities offences are *Regina* v. *Burrows*, [1952] O.W.N. 797 and *Regina* v. *Oliver*, [1967] 1 O.R. 300 *per* Donohue, J. at 303-04.

[21] Securities forming all or part of or derived from "the holdings of any person, company or any combination of persons or companies holding a sufficient number of any of the securities of a company to materially affect the control of such company ..." (s. 1(1) 6a).

[22] [1942] A.C. 435 at 444-45.

[23] [1969] 1 All E.R. 347 at 355. This judgment was approved by the Supreme Court of Canada in *Pierce Fisheries*, *supra*, note 6.

[24] *Id.* at 363-64.

In the case of *Regina* v. *Slegg and Slegg Forest Products Ltd.*, Ostler, D.J. held that certain offences under *The Securities Act, 1967* of British Columbia (including the offence of trading in the course of "primary distribution to the public" without a prospectus having been filed with the Securities Commission) fell into the strict liability category of offences created by statutes which are not subject to the presumption that *mens rea* is an essential ingredient. Ostler, D.J. reached this conclusion after observing that the section includes no words such as "maliciously, fraudulently, wilfully or knowingly which imply the necessity of establishing a guilty mind on the part of the accused."[25] It is unfortunate that he directed his attention neither to the need to establish whether the offence fell within one of the "strict liability" categories, notwithstanding the absence of words importing a mental element, nor to the definition of "primary distribution to the public" contained in the British Columbia *Securities Act, 1967* which contains the same references to "purpose" as the Ontario Act.[26]

Ostler, D.J.'s dictum as to the inapplicability of the doctrine of *mens rea* may not have affected the outcome; there was evidence that the actions of the accused had been with the intention of distributing the securities to the public. However, not all situations involving "distributions to the public" will be as straightforward as that in the *Slegg* case.

In the example referred to above, the purpose (in the sense envisaged by Lord Simon in the *Crofter* case and by Lord Diplock in the *Parsley* case) of a salesman in sending out a newsletter or report (containing a description of a company whose shares are listed on an exchange and which also happens to have filed a preliminary prospectus) may be to effect a transaction for value in the listed shares and not the securities referred to in the preliminary prospectus. If this can be established by evidence, then it would seem that there would be a good defence to a charge of having contravened the prohibition contained in s. 35, notwithstanding any evidence that, for instance, one or more customers receiving the newsletter or report were actually persuaded thereby to subscribe for the securities referred to in the preliminary prospectus. The salesman could be well aware of the prohibition contained in s. 35 but believe at the same time that his action in sending out the newsletter or report would only result in customers' buying or selling the listed shares and not the prospectus securities.

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[25] [1974] 4 W.W.R. 402 at 407.

[26] "Primary distribution to the public," used in relation to trading in securities, means

(i) trades that are made for the purpose of distributing to the public securities issued by a company and not previously distributed; or

(ii) trades in previously issued securities for the purpose of distributing such securitiles to the public where the securities form all or a part of or are derived from the holdings of any person, company, or any combination of persons or companies holding a sufficient number of any of the securities of a company to materially affect the control of the company,

whether the trades are made directly to the public or indirectly to the public through an underwriter or otherwise, and includes any transaction or series of transactions involving a purchase and sale or a repurchase and resale in the course of or incidental to the distribution.

One qualification should be made to this view. The reason (or main purpose) of the salesman's action could be as suggested but he could also be aware that (although he may not have desired it as a result) some of the customers might be prompted by the report or newsletter into subscribing for the prospectus securities. It has been suggested that the word "purpose" includes probable results of an action even though the reason for doing the action (its "main" purpose) is something else. Lord Devlin, for example, in *Chandler et al* v. *Director of Public Prosecutions* said:

> I shall begin by considering the word "purpose", for both sides have relied on this word in different senses. Broadly, the appellants contend that it is to be given a subjective meaning and the Crown an objective one.
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> I have no doubt that it is subjective. A purpose must exist in the mind. It cannot exist anywhere else. The word can be used to designate either the main object which a man wants or hopes to achieve by the contemplated act, or it can be used to designate those objects which he knows will probably be achieved by the act, whether he wants them or not. I am satisfied that in the criminal law in general, and in this statute in particular, its ordinary sense is the latter one.[27]

The conclusion, therefore, is that, notwithstanding the *Burkinshaw* and *Slegg* decisions, in order for it to be established that an offence has been committed under ss. 35 or 57 of the Ontario Act, it will have to be shown that the accused knew the relevant facts about what he was doing and that either that the main reason for the trade in his mind was to distribute securities to the public or that he knew that a probable (if possibly undesired) result of the trade would be a distribution of securities to the public.

The Securities Act, 1975 introduced (as Bill 98) into the Ontario Legislature last year, dropped the references to "purpose" and "public" from the definition of "distribution."[28] If this approach is adopted in future securities legislation, it may be argued that *mens rea* will no longer be available as a defence against charges of "illegal distribution" of securities. This will certainly be the case with regard to the particular intent specified in describing the offence ("purpose of distributing"). What about *mens rea* in the context of knowledge that the trade in question is one of the kinds of acts prohibited?

Although trades prohibited by securities legislation would hardly fall within the categories of "public nuisances" and their prohibition is certainly not a "summary mode of enforcing a civil right" (the second and third of Wright, J.'s three strict liability categories), the prohibition may certainly be

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[27] [1962] 3 All E.R. 142 at 155.

[28] The definition of "distribution" in Bill 98 read as follows:

"distribution", where used in relation to trading in securities, means,

(i) a trade in securities of an issuer which have not been previously issued.

(ii) a trade or on behalf of an issuer in previously issued securities of that issuer which have been redeemed or purchased by or donated to that issuer, or

(iii) a trade in previously issued securities of an issuer from the holdings of any person, company or combination of persons or companies holding a sufficient number of any securities of that issuer to affect materially the control of the issuer, but any holding of any person, company or combination of persons and companies holding more than 20 per cent of the outstanding voting evidence to the contrary, be deemed to affect materially the control of that issuer,

and "distribute", "distributed" and "distributing" have a corresponding meaning.

regarded as creating a non-criminal offence prohibited in the public interest (Wright, J.'s first strict liability category).

In the first place, securities legislation has been upheld as legislation in relation to property and civil rights and not trespassing upon the jurisdiction of the Parliament of Canada in matters of criminal law.[29]

In the second place, the securities laws are legislation "in the public interest" designed for the protection of the public at large.[30]

The conclusion appears inescapable that with the disappearance of "purpose" from the definition of "distribution", the offence of trading (as distinct from "acquiescing in" trading or "knowingly" trading) contrary to a *Securities Act* prohibition would be one of strict liability and the defence of absence of *mens rea* would not be available.

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[29] *Re Williams and Williams* (1961), 29 D.L.R. (2d) 107 (O.C.A.).

[30] *Id.* at 108, *per* Roach, J.A.