

# a penny for your

The Over-the-Counter Bulletin Board is a shadowy world of has-beens, wannabes and outright scams. And the epicentre of that world is right here in B.C.

# stocks



entering the downtown head office of Destiny Media Technologies, it's immediately obvious that the company has seen better times. The expansive lobby screams opulence, with its slate-tile floor, its floor-to-ceiling windows overlooking West Hastings Street 10 floors below, and the massive boardroom table visible through an aqua-tinted glass wall. But there's nobody home. On the receptionist's desk is a bell with a note asking visitors to ring for service.

A few minutes later than our scheduled appointment, 40-year-old CEO Steve Vestergaard saunters through the doors, followed by John Gammack, VP of operations. Both are dressed casually, returning from a quick bite around the corner. They usher their visitor into the corner office, where they deliver a well-honed spiel outlining how Destiny's music-downloading technology is poised to blow iTunes out of the water.

» by David Jordan » portraits by Paul Joseph

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Destiny Media is a survivor. It began in 1991 as a private company developing video games, then got into Internet technology in the mid-1990s. It lived through the tech crash and, if you believe the spiel, is poised to overtake Apple as the leading provider of encryption technology to major record labels.

Destiny is also one of about 300 Vancouver public companies whose only North American trading platform is the U.S. Over the Counter Bulletin Board. The OTC connection is a heavy cross to bear: whenever the phrase appears in the news media, you can be sure that close by will be qualifiers such as "largely unregulated," and comparisons to the "Wild West" or worse. It's common knowledge that the OTCBB is the market of last resort, the refuge of companies that don't qualify for listing on even a junior stock exchange, such as Amex or TSX-Venture.

Delving into Vancouver OTC companies reveals a shadowy world of has-beens, wannabes and outright scams. And just occasionally, you'll see an earnest company such as Destiny, grasping for a shot at legitimacy.

Destiny is one of the few Vancouver OTCBB companies with substantial revenue: in 2005, it posted sales of US\$769,000. Sure, it also posted a net loss of US\$547,000, but at least it has real products that people are paying for. That's a rarity on the OTCBB.

Browse a list of the hundreds of other Vancouver OTCBB companies, and you'll find a motley collection of companies laced by implausible business plans, little or no revenue and substantial losses (just go to [otcbb.com](http://otcbb.com) and type "Vancouver" into the search). Try to track down executive management, and more often than not you'll be led through a maze of reverse takeovers leading to untraceable offshore investors.

It's a market ripe for corruption and Vancouver is a major player. The B.C. Securities Commission is concerned enough that two years ago it struck a committee charged solely with ferreting out the B.C. connection to OTCBB fraud. It found 530 OTCBB companies with direct connections to Vancouver and another 200 local businesses with connections to the even more infamous Pink Sheets—a near cousin of the OTCBB that is subject to even less regulatory oversight.

"In our opinion, the quality of disclosure from many OTCBB companies needs to be improved," says Martin Eady, director of corporate finance for the BCSC. Although he declines to provide numbers, he says the BCSC is currently in the process of working up several cases "of matters that we think are significant."

In the U.S., the National Association of Securities Dealers is equally concerned about the OTC's apparent attraction for scam artists. "It's a persistent problem that doesn't seem to be going away," says Cam Funkhouser, senior VP of market regulation for the self-regulating professional association for U.S. securities dealers. Funkhouser confirms that the NASD is working closely with the BCSC, as well as with the RCMP and other law enforcement agencies. He estimates that the NASD refers about 100 cases of suspected OTCBB fraud a year to the U.S. Securities and Exchange Commission and other enforcement agencies.

Despite its professed concern, the BCSC has a scant record of disciplinary action

against OTCBB companies. In recent years, the BCSC has leveled 23 disciplinary actions for irregularities involving OTCBB trading, but very few of those are for specific findings of wrongdoing against Vancouver companies. They include, for example, the 2002 decision against Jesse Hogan, a 20-something Burnaby kid who loaded up on OTCBB stocks then pumped up their value by flooding online newsletters and chat groups with hot tips.

**t**he OTCBB was created by the NASD as a pilot project in 1990 to provide a formal means of tracking the direct sale of securities among NASD-member brokers and traders. It was formally sanctioned by the SEC in 1997. Although the bulletin board was created by the NASD, the association has no responsibility for monitoring the companies that are traded on it. The association does oversee its member brokers and traders, and it monitors their activity for signs of potential fraud. But the bulletin board is simply an electronic quotation system and unlike stock exchanges, it has no overseeing body that poses minimum listing requirements and monitors listed companies for compliance.

The only requirement OTCBB companies face is that they file regular financial statements with the SEC. There's no requirement, however, as to the information contained in those filings. If you browse through a few filings, you'll find a familiar refrain: massive losses with little or no revenue, backed by often implausible or unrealistic business plans.

The advantages to listing on the OTC are obvious: liquidity and access to U.S. capital markets. But an OTCBB listing comes with a steep price: not only will a company automatically suffer by association with the board but it will face considerable legal and accounting expenses—at least \$100,000 a year—to meet

rigorous SEC filing requirements.

Mike Volker has 25 years' experience working directly with start-up companies too small to qualify for junior-stock-exchange listings. The former chair of the Vancouver Enterprise Forum and current manager of the Vancouver Technology Angel Network says the OTCBB does provide a legitimate capital market for some of these companies, and outlines three types of businesses that typically list on the OTCBB. The first he describes as "honest, well-intentioned but naive and unrealistic people who see this as a way to raise money for their crazy ideas. They're not trying to be dishonest; they're just working hard and trying to get investors to support them."

At the other end of the spectrum, "you get those who are deliberately using OTC companies to scam people. They make promises, they raise money, then they say, 'Oh well, we didn't succeed.' But of course somewhere in the process they've managed to sell some of their shares and make some money that is undeserved."

Falling somewhere between these two poles is a type of OTCBB company that Volker has had considerable first-hand experience with. These tend to be primarily tech companies, and today they are more often than not ones that have fallen on hard times since the tech crash of 2001. Volker describes this group as "companies with good solid business plans and they're using the OTC because there aren't any alternatives. They may not meet the listing requirements to be on the Venture exchange, or they may find it too expensive."

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came along. Destiny quickly switched gears. "We saw a big opportunity to build a security system for the music industry because we saw the Internet was going to threaten their business model," explains Vestergaard.

Good idea, bad timing. First the tech bubble popped, quashing dreams of endless funding for tech start-ups like Destiny. Then Napster, the leading figure in the music-downloading craze, died a slow and painful death.

But Destiny hung in, and today Vestergaard and Gammack are once again ramping up their pitch. Music downloading is back in a big way, and this time it's the record labels that are calling the shots. The labels need a secure way of encrypting their music, Gammack argues, and iTunes, the leading provider of that technology, is sorely lacking. "What we have is way better than iTunes," Gammack boasts. "iTunes is supposed to be a model based on music, but it's not." The iTunes technology is a loss leader invented by Apple to sell iPods, he explains, but it could do a much better job of meeting the needs of the music industry and music enthusiasts. For example, iTunes is not portable: Apple couldn't sell the technology to Wal-Mart so the retail giant could set up its own online music store.

Another Vancouver OTC company earnestly striving for legitimacy in financial markets is Northstar Electronics, which supplies electronics to marine industries. Its history is a story of survival very different from that of Destiny Media – a difference that is immediately evident upon entering its Granville Street head office.

Unlike the spacious glass offices of Destiny Media, Northstar's offices are dark and cramped. To the right of the narrow entrance corridor is a room lined with dark wooden bookshelves overflowing with cardboard storage boxes. At the end of the hallway is a heavy wooden desk in front of a chair upholstered in red leather and brass tacks. On the lobby table is a fishing magazine.

Northstar's primary revenue generators are control consoles for submarines made by Lockheed Martin, and NetMind, a sonar device used in commercial fishing. The company has raised about \$4 million since going public on the OTCBB in 2000. But raising funds has become a tougher slog as the company loses the lustre of a promising start-up. "We found it easier to raise money five or six years ago than today," explains president and CEO Wilson Russell. "It's easier for people to imagine where you can go. When you're actually part of the way there, sometimes it's a little too real for them."

Northstar lost US\$985,000 on revenue of US\$1.6 million in 2005, but Russell is expecting big things, predicting that "revenues will go up in multiples of three times to six times in the next three years." His hopes for graduating from the OTCBB to the American Stock Exchange rest on the company's connection with Lockheed Martin and on its ability to skew its investor pitch toward "homeland security" – a particularly hot commodity on junior capital markets today.

VP Terry McLeod ushers a visitor into a second room lined with dark bookshelves. The shelves in this room are mostly empty, and some tilt askew. One holds a users' manual for MS DOS 6.2.

McLeod disappears for a moment, then returns wrestling a massive, yellowing CRT



Destiny Media clearly belongs to the latter category. Vestergaard and a former partner founded the company on video games in 1991, then got into Internet technologies. Destiny had just released

Radio Destiny, a software program that turns any personal computer into an Internet radio broadcaster, when the MP3 audio format

## Due diligence

For details about Vancouver OTCBB companies, visit these websites:

- Over the Counter Bulletin Board ([otcbb.com](http://otcbb.com)): type "Vancouver" in the search box and you'll find profiles of about 400 companies. The listings are outdated – it's impossible to keep up with continual delistings, changes of business plans and company names – but it's a start.
- U.S. Securities and Exchange Commission ([sec.gov/edgar.shtml](http://sec.gov/edgar.shtml)): All OTCBB companies must comply with SEC filing requirements. Type in a company name to access all of its SEC filings.
- B.C. Securities Commission ([bcsc.bc.ca](http://bcsc.bc.ca)): Type "otcbb" into the search box, and under "decisions and orders" you'll find details of disciplinary actions involving OTCBB trading. □

monitor as he prepares to deliver a PowerPoint presentation. Futzin under the table, he mutters, "Every time you do a presentation, someone moves the..." his words trail off as he straightens up and wanders back down the hallway.

Once the presentation is underway, it quickly becomes apparent that McLeod has a verbal tic: he can't pronounce a sentence without interjecting "Lockheed Martin." He mentions the name probably a hundred times in the course of the 20-minute presentation.

The slides describe an array of current and potential products. In addition to NetMind and the submarine consoles, the panoply of products both current and on the drawing board includes an underwater intruder-detection system, an anti-bioterrorism system, fibre optic cables for the next generation of U.S. Air Force jets and an electronic pen that reads Radio-Frequency Identification (RFID) codes.



Destiny Media and Northstar Electronics are a breed unto themselves. Among the 300 or so Vancouver OTCBB companies reviewed for this story, the business descriptions of maybe a couple of

dozen stand out as indicating potentially solid companies that have maintained a consistent name and address for more than a year. Of those, only Northstar and Destiny agreed to speak to the media.

A number of questions remain regarding

all the others: particularly, why go public? Even among those well-intentioned companies with quirky business plans, why risk the cost of public filings and the public scrutiny that goes with them?

Take, for example, Milk Bottle Cards Inc., which was incorporated in 2004 and lists an address on East 18th Avenue near Main Street as its headquarters. According to the company's SEC filings, founder Nicole Milkovich would seem to be doggedly pursuing a dream of making a business of designing and selling greeting cards.

Milkovich, who graduated from the Emily Carr Institute of Art and Design in 2000, is listed as president, secretary, CFO and sole director. She also holds a full-time day job as a graphic designer for Nick Milkovich Architects (family relation unspecified). Even with the full-time job and occasional freelance gigs, Milkovich still finds about 20 hours a week to devote to her greeting-card business. She has one part-time employee: Carlos Bolbrugge, a graduate of the Capilano College art program (where Milkovich also studied before moving on to Emily Carr). Bolbrugge also has a day job as a graphic designer and devotes about five hours a week to Milk Bottle Cards as VP of design.

Milk Bottle's annual report attests to sincere efforts to develop a viable business. To date, Milkovich has placed her cards in one Vancouver retail store that sells them on consignment. She and her partner have completed one custom order for 100 holiday cards, and "were recently contacted regarding custom wedding invitations... [but] the

potential customer decided to go with a more standard wedding invitation."

Management's discussion and analysis in the most recent annual report offers no shortage of marketing ideas: Milkovich has built a website and hopes to be able to accept online payment soon, she continues to seek more retail stores to carry her cards, she plans to exhibit at home shows, and she plans to host a home party where she will invite friends and family to buy cards from her latest collection.

And she isn't without her share of business challenges. For example, in her latest quarterly filing, Milkovich explains that she and her partner are seeking a solution to problems "due to the overuse of our printer."

Milk Bottle Cards has total assets of \$12,655, and since its inception has lost a total of \$25,159.

An admirable story of enterprise and ambition. But why go public? And why pay the approximately \$100,000 a year it costs to file audited financial statements required by the SEC? We'll never know because Milkovich did not respond to a request for an interview.

At the far end of the OTCBB spectrum are companies so convoluted that untangling the knot of business ventures and offshore owners would be a forensic nightmare. Typically, a Vancouver company incorporates in the U.S. with an unlikely business plan like, say, developing a self-chilling beverage container or selling silk underwear online. The original scheme goes bust within a couple of years and the company launches a new venture through the reverse takeover of an equally dubious U.S. venture. Because it's

## Improbable ventures

The following is a sampling of OTCBB companies based in the Lower Mainland:

■ **Infinex Ventures Inc.**, 323 - 595 Howe Street, Vancouver. In August 2002, bought a number of nanotechnology patents and planned to "work with strategic partners to develop commercial applications for its nanotechnology, such as flat visual display systems for automotive and aircraft dashboards." Now a mineral exploration company.

■ **Intomational Energy, Inc.**, 216 - 1628 W. 1st Ave., Vancouver. (Formerly E.Deal.Net Inc.) Automotive web portal; changed its name

and launched an oil and gas exploration subsidiary in June 2005. (Currently reconsidering economic viability of its automotive Web portal.)

■ **MangaPets, Inc.**, 2608 Finch Hill, Vancouver. In the cash-dispenser business until 2005, when it signed an agreement with a Quebec company for "the design, development and deployment of an online virtual pet portal/website with highly interactive two-dimensional graphical interfaces and a powerful multi-layered back end engine to enable the

building of a worldwide virtual community." Currently seeking to terminate the contract and find a new partner for its pet portal.

■ **NorPac Technologies, Inc.**, 311 - 698 Seymour Street, Vancouver. Owns a patent for a self-chilling beverage container and related parts.

■ **Patriot Gold Corp.**, 501 - 775 Bellevue Ave., West Vancouver. Originally in the business of producing and selling ostrich meat. Became a mineral exploration company in 2000. Its website ([patriotgoldcorp.com](http://patriotgoldcorp.com)) displays an

American flag and Statue of Liberty, and bills Patriot as "America's gold company."

■ **Purchase Point Media Corp.**, 320 - 1100 Melville Street, Vancouver. Owns the patent to an advertising display device that attaches to supermarket shopping carts.

■ **Tora Technologies Inc.**, 205 - 1990 East Kent Avenue, Vancouver. Engaged in the "marketing of custom embroidery products and services through the Internet." □



an all-stock deal – the Vancouver company pays for the acquisition with its own shares – the target company ends up owning the business. For accounting purposes, it's considered a continuous business but the original Vancouver owners disappear into the sunset.

For example, there's Global-Wide Publications Ltd. The OTCBB website describes a plausible business: Global-Wide, headquartered at 595 Howe Street, publishes a bilingual English/Italian newspaper, and distributes 2,500 copies around Vancouver weekly. Look up its latest SEC filings, however, and you'll find out first of all that there's another company with the same name and same business description, headquartered in Santa Rosa, California. Read further and you'll discover that both companies no longer exist. Global-Wide became Viaspace Technologies LLC through a reverse takeover in June 2005 (a takeover that is currently under investigation by the SEC). According to its SEC filings, from its headquarters in Pasadena, "the company's objective is transforming proven space and defence technologies from Caltech/NASA's Jet Propulsion Laboratory into hardware and software solutions that solve today's complex problems."

Then there's the Vancouver company that started out in 1999 selling silk underwear on the Internet under the name Fidelity Capital Concepts Ltd. When that didn't work out, a reverse takeover in November 2004 sent it stateside, where it's now known as id-Confirm, supplier of biometric identity verification devices.

Another former Vancouver company, Snocone Systems Inc., provides a story more convoluted than the plot of a daytime TV drama. The Vancouver company started out selling software to biotech researchers, moved into video surveillance and office betting pools, and today is run by a couple of 25-year-olds in San Diego operating under the name Who's Your Daddy Inc.

Snocone started out in 2000, when it paid \$3,000 for the ownership rights to software potentially useful to biotech researchers. It began trading on the OTCBB in July 2004 and shortly thereafter touted two new business ventures. Through a licensing agreement with SMS Office Pools, it would sell software that lets users tap into sports betting pools via their cell phones. And through an agreement with Riskbiz Internet Services Inc., it would offer "mobile viewing technology" under the brand "Riskeye." The press releases flowed fast and furious. First, Snocone announced that the Vancouver Police Department would be using its video surveillance technology, thanks to a letter of intent it had signed to provide its technology to Smart-Tek Communications Inc.

Then the company announced that it had

reached an agreement with a fashion photographer to use the same video-streaming technology to give cell-phone users access to live model shoots.

Neither venture came to fruition and in April 2005, Snocone suddenly announced it had terminated its previous agreements and acquired Who's Your Daddy, a San Diego company whose primary asset is ownership of the "Who's Your Daddy" trademark. Anyone who wants to put the phrase on a T-shirt or ball cap has to pay the company a licensing fee.

Former Snocone president Vivian Kane suddenly disappeared from the company roster, along with any reference to a Vancouver office. The company is now headquartered in San Diego, and is run by president Dan Fleishman and CEO Edon Moyal, both of whom have held those positions since

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2001, when they were 20 years old. In 2005, Who's Your Daddy lost US\$4.2 million on revenue of US\$77,463.

Sounds like a losing proposition to those of us looking for a sound investment to top up our RRSPs. But try Googling "penny stock," and you'll be introduced to a whole universe of investors whose tolerance for risk and dreams of reward are off the scale by any conventional measure. And it's a universe fuelled largely by Vancouver companies.

If you have the itch to invest, it might not be too late to get in on that self-chilling beverage container. Although its most recent quarterly filing describes a failure to execute the first phase of its business plan due to lack of funding, "product development is estimated to be completed over a timeframe of 7.5 months." But act now: the share price of Norpac Technologies (OTCBB:NRPT) has already doubled, from \$0.12 to \$0.25, since last July.

As for the silk underwear, you've missed the boat. Fidelity Capital Concepts has already done the RTO shuffle and is now based in Denver, selling "biometric identity authentication and verification devices." ■