UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Administrative Proceedings Rulings
Release No. 6525 / March 28, 2019

Administrative Proceeding
File No. 3-18017

In the Matter of

Can-Cal Resources Ltd.,
China Fruits Corp., and
SkyStar Bio-Pharmaceutical Co.

Order Denying the Division of Enforcement's Motion for Summary Disposition

The Division of Enforcement moved for summary disposition against the only remaining Respondent in this proceeding, Can-Cal Resources Ltd., arguing that in light of Can-Cal's long period of delinquency in filing required periodic reports with the Securities and Exchange Commission, the registration of Can-Cal's securities should be revoked under Section 12(j) of the Securities Exchange Act of 1934. Because the Division has not shown "that there is no genuine issue with regard to any material fact and that [it] is entitled to summary disposition as a matter of law,"[1] its motion is DENIED.

Background[2]

Can-Cal is an exploration stage company incorporated in Nevada with a principal office in Red Deer, Alberta, Canada, and with current interests in

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[1] 17 C.F.R. § 201.250(b).

[2] The summary that follows omits some of what transpired, including a period of intervention by shareholders who filed briefs, participated in prehearing conferences, and generally argued against the revocation of Can-Cal's securities.

mineral properties at Cerbat, Arizona, and Pisgah, California.[3] Its corporate status is currently active.[4]

In June 2014, thirty-five Can-Cal shareholders filed a derivative shareholder complaint in the District Court of Clark County, Nevada.[5] The shareholders accused Can-Cal's management of entering into agreements with Candeo Lava Products Inc. that limited Can-Cal's ability to profit from the volcanic material on the Pisgah property and of keeping information from shareholders by filing false and misleading reports with the Commission.[6]

Can-Cal stopped filing periodic reports with the Commission in January 2016; the last report filed was a quarterly report for the period ended September 30, 2015.[7] The company claims that it stopped filing reports because it lacked funds due to the shareholder litigation and out of concern that any representations made in the reports might be used by the shareholders.[8]

The Commission instituted this proceeding against Can-Cal in June 2017 because it had not filed its periodic reports.[9] Can-Cal answered the

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[3] *See* Can-Cal Res. Ltd., Annual Report 1, 7 (Form 10-K) (Apr. 11, 2018). I take official notice of Can-Cal's filings on the Commission's EDGAR database. 17 C.F.R. § 201.323; *see Helpeo, Inc.*, Exchange Act Release No. 82551, 2018 WL 487320, at *4 n.37 (Jan. 19, 2018) (taking official notice under Rule 323 of EDGAR filings).

[4] Nevada Secretary of State, Can-Cal Res. Ltd., https://www.nvsos.gov/SOSEntitySearch/CorpDetails.aspx?lx8nvq=67b8FLyCzfg8pZcMBsqbow%253d%253d&nt7=0 (last visited Mar. 21, 2019). I take official notice of Can-Cal's corporate information from the Nevada Secretary of State's website. 17 C.F.R. § 201.323; *see Helpeo*, 2018 WL 487320, at *4 n.38 (taking official notice under Rule 323 of records maintained by the Nevada Secretary of State).

[5] *Sloan v. Can-Cal Res. Ltd.*, No. A-14-701465-B (Nev. Dist. Ct. Clark Cty. May 29, 2014).

[6] Motion to Intervene (Jun. 16, 2017), Ex. 1 at 1 (derivative shareholder complaint).

[7] Can-Cal Res. Ltd., Quarterly Report (Form 10-Q) (Jan. 7, 2016).

[8] Can-Cal Supp. Opp'n (Jan. 4, 2019), Ex. 1 at 2 (Decl. of Casey Douglass).

[9] Order Instituting Proceedings ¶¶ I, II.A.1.

order instituting proceedings in July 2017. In November 2017, the Division filed the instant motion for summary disposition. Can-Cal filed an opposition in January 2018, claiming that there was a tentative settlement to resolve the shareholder litigation and that it would become current in its reporting obligations within thirty days.[10]

In March 2018, Can-Cal filed a comprehensive annual report on Form 10-K for fiscal years 2015 and 2016, which contained audited financial statements for 2014 through 2016 and unaudited financial statements in lieu of the delinquent quarterly reports for 2016 and 2017.[11] The Commission's Division of Corporation Finance "did not find any material deficiencies" in Can-Cal's comprehensive 10-K.[12]

On April 2, 2018, the Nevada district court preliminarily approved a stipulation and agreement of settlement resolving the shareholder litigation.[13] The settlement included an agreement between Can-Cal and Candeo that obligates Candeo to purchase approximately $150,000 worth of volcanic materials from Can-Cal's Pisgah property each year for at least the next twenty years.[14] The court-ordered stipulation also required Candeo to pay for audit fees to complete Can-Cal's delinquent periodic filings for 2015 through 2017.[15]

A little over a week later, Can-Cal filed an annual report on Form 10-K for fiscal year 2017.[16] Since then, Can-Cal has timely filed its three quarterly

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10 Can-Cal Opp'n 1–3 (Jan. 5, 2018).

11 Can-Cal Res. Ltd., Comprehensive Annual Report, at "Explanatory Note" (Form 10-K) (Mar. 12, 2018) ("Super-K").

12 Prehr'g Tr. 5 (May 7, 2018).

13 Can-Cal Supp. Docs. (Jul. 11, 2018), Ex. 1 at 2 (district court final judgment and order of dismissal).

14 Can-Cal Supp. Docs. (May 22, 2018), Stipulation and Agreement of Settlement, Ex. A at 3–4 (Second Amended and Restated Material Supply Agreement).

15 *Id.*, Stipulation at 16.

16 Can-Cal Res. Ltd., Annual Report (Form 10-K) (Apr. 11, 2018).

reports for fiscal year 2018; its most recent 10-Q, for the quarter ended September 30, 2018, was filed in November 2018.[17]

In May 2018, the administrative law judge then assigned to this proceeding held a prehearing conference to discuss its status. The Division argued that Can-Cal was still delinquent because it had failed to file any 10-Qs for 2016 or 2017.[18] The Division further maintained that regardless of Can-Cal's recent efforts to become current, revocation was appropriate under Commission precedent, particularly *Absolute Potential, Inc.*[19]

However, the administrative law judge was unable to rule on the Division's motion because the Commission stayed all administrative proceedings from June until August 2018.[20] In September 2018, because of the Commission's ruling in the wake of the Supreme Court's decision in *Lucia v. SEC*,[21] the proceeding was reassigned to a different administrative law judge for a new hearing, although the parties agreed to rely on the record created before the prior administrative law judge.[22] The new administrative law judge ordered two additional rounds of briefing, which concluded in February 2019.[23]

In March 2019, the administrative law judge ordered the parties to decide how they wished to proceed should he deny the Division's summary

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17 Can-Cal Res. Ltd., Quarterly Report (Form 10-Q) (Nov. 14, 2018).

18 Prehr'g Tr. 5 (May 7, 2018).

19 Exchange Act Release No. 71866, 2014 WL 1338256 (Apr. 4, 2014); *see* Prehr'g Tr. 9–10.

20 *Pending Admin. Proc.*, Securities Act Release No. 10536, 2018 WL 4003609, at *1 & n.3 (Aug. 22, 2018).

21 138 S. Ct. 2044 (2018).

22 *Pending Admin. Proc.*, 2018 WL 4003609, at *1; *Pending Admin. Proc.*, Admin. Proc. Rulings Release No. 5955, 2018 SEC LEXIS 2264, at *2–3 (ALJ Sept. 12, 2018); *Can-Cal Res. Ltd.*, Admin. Proc. Rulings Release No. 6163, 2018 SEC LEXIS 2792, at *1 (ALJ Oct. 11, 2018).

23 *Can-Cal*, 2018 SEC LEXIS 2792, at *1; *Can-Cal Res. Ltd.*, Admin. Proc. Rulings Release No. 6392, 2018 SEC LEXIS 3440, at *5 (ALJ Dec. 10, 2018); *Can-Cal Res. Ltd.*, Admin. Proc. Rulings Release No. 6433, 2019 SEC LEXIS 67, at *1 (ALJ Feb. 1, 2019).

disposition motion.[24] Can-Cal wants the matter considered as a case stated and argues that no further filings or testimony are necessary.[25] The Division maintains, however, that if summary disposition is denied, there should be a hearing, where it will attempt to prove that Can-Cal is still not current in its periodic reports.[26]

In the last few weeks, several Can-Cal shareholders submitted letters to this office asking the assigned administrative law judge not to revoke the company's registration. I have caused these letters to be filed with the Office of the Secretary and made part of the record in this proceeding.

On March 18, this proceeding was reassigned to me.[27]

Discussion

Under Rule 250(b), summary disposition is appropriate in an Exchange Act Section 12(j) proceeding where there is no genuine issue as to any material fact and the movant is entitled to summary disposition as a matter of law.[28] In assessing the summary disposition record, the facts, as well as the reasonable inferences that may be drawn from them, must be viewed in the light most favorable to the non-moving party.[29]

Exchange Act Section 13(a) and Rules 13a-1 and 13a-13 require issuers of securities registered with the Commission to file annual and quarterly reports with the Commission. Compliance with these reporting requirements is mandatory.[30] Scienter is not required to establish violations of Exchange

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[24] *Can-Cal Res. Ltd.*, Admin. Proc. Rulings Release No. 6486, 2019 SEC LEXIS 341, at *1–2 (ALJ Mar. 6, 2019).

[25] Can-Cal Notice 1–2 (Mar. 15, 2019).

[26] Div. Statement of Intent 1–2 (Mar. 13, 2019).

[27] *Can-Cal Res. Ltd.*, Admin. Proc. Rulings Release No. 6509, 2019 SEC LEXIS 514 (ALJ).

[28] *See* 17 C.F.R. § 201.250(b); *Absolute Potential*, 2014 WL 1338256, at *5.

[29] *Joseph P. Doxey*, Exchange Act Release No. 77773, 2016 WL 2593988, at *2 (May 5, 2016).

[30] 15 U.S.C. § 78m(a); 17 C.F.R. §§ 240.13a-1, .13a-13(a); *see America's Sports Voice, Inc.*, Exchange Act Release No. 55511, 2007 WL 858747, at *4 (Mar. 22, 2007), *recons. denied*, Exchange Act Release No. 55867, 2007 WL 1624611 (June 6, 2007).

Act Section 13(a) and Rules 13a-1 and 13a-13.[31] There is no dispute that Can-Cal failed to file timely periodic reports for nearly two years. As a result, it did not comply with Exchange Act Section 13(a) and Rules 13a-1 and 13a-13.

Under Exchange Act Section 12(j), the Commission is authorized, "as it deems necessary or appropriate for the protection of investors," to revoke the registration of a security or suspend the registration for a period not exceeding twelve months if it finds, after notice and an opportunity for hearing, that the issuer of the security has failed to comply with any provision of the Exchange Act or rules thereunder.[32]

In determining what sanctions will ensure that investors are adequately protected, the Commission "consider[s], among other things, the seriousness of the issuer's violations, the isolated or recurrent nature of the violations, the degree of culpability involved, the extent of the issuer's efforts to remedy its past violations and ensure future compliance, and the credibility of its assurances, if any, against further violations."[33]

Can-Cal's violations are serious because the reporting requirements are the primary tool that Congress "fashioned for the protection of investors from negligent, careless, and deliberate misrepresentations" in the sale of securities.[34] Can-Cal's violations, which went on for nearly two years, were recurrent.[35] And Can-Cal is culpable because it knew about the reporting

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[31] *See SEC v. McNulty*, 137 F.3d 732, 740–41 (2d Cir. 1998); *SEC v. Wills*, 472 F. Supp. 1250, 1268 (D.D.C. 1978).

[32] 15 U.S.C. § 78*l*(j).

[33] *Gateway Int'l Holdings, Inc.*, Exchange Act Release No. 53907, 2006 WL 1506286, at *4 (May 31, 2006).

[34] *Eagletech Commc'ns, Inc.*, Exchange Act Release No. 54095, 2006 WL 1835958, at *3 (July 5, 2006) (quoting *SEC v. Beisinger Indus. Corp.*, 552 F.2d 15, 18 (1st Cir. 1977)).

[35] *See Nature's Sunshine Prods., Inc.*, Exchange Act Release No. 59268, 2009 WL 137145, at *5 (Jan. 21, 2009) (respondent failed to file seven required periodic reports due over a two-year period); *Impax Labs., Inc.*, Exchange Act Release No. 57864, 2008 WL 2167956, at *7 (May 23, 2008) (respondent's failure to make eight filings over an eighteen-month period considered recurrent).

requirements; the fact it lacked the funds to file reports due to ongoing litigation does not excuse its noncompliance.[36]

A company's recurrent failure to file reports is so serious that only a "strongly compelling showing" on the remaining factors—its remedial efforts and assurances against future violations—will save it from revocation.[37] Although the Commission demands strict compliance with Section 13(a) and its rules, a company's "subsequent filing history is an important factor to be considered in determining whether revocation is necessary or appropriate for the protection of investors."[38] Revocation is not automatic, particularly when the company has made significant efforts to come into compliance.[39]

The Division's primary argument is that the circumstances here are on all fours with those in *Absolute Potential*, where the Commission revoked the registration of Absolute's securities even though it filed all of its delinquent reports after the Section 12(j) proceeding against it was initiated.[40] But there are differences between that cases and this one. The Commission noted that although another company had "demonstrated a willingness to provide extensive financial support [to Absolute], through loans, it was not legally bound to do so."[41] But even assuming that Absolute would continue to receive sufficient funding to complete future reports, the Commission found that

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[36] *See Nature's Sunshine Prods.*, 2009 WL 137145, at *6 (finding culpability when there is no indication the violation was inadvertent). Arguably, the company's financial issues may explain why it was noncompliant. However, its second reason for noncompliance—that it did not file required reports because of an additional concern that if the filings were made, the representations therein might be used by the shareholders in litigation—raises an issue about the company's attitude toward compliance with its reporting obligations that cannot be resolved on summary disposition.

[37] *Impax Labs.*, 2008 WL 2167956, at *8.

[38] *e-Smart, Techs., Inc.*, Exchange Act Release No. 50514, 2004 WL 2309336, at *2 (Oct. 12, 2004).

[39] *See id.* (remanding proceeding to the administrative law judge because after the initial decision was issued the company filed its most recent reports and "ha[d] begun to fill the gaps in its reporting history by" filing delinquent reports).

[40] *See, e.g.*, Div. Supp. Br. 1–6 (Feb. 13, 2019) (Div. Feb. 2019 Br.).

[41] *Absolute Potential*, 2014 WL 1338256, at *5.

Absolute's assurances of future compliance were not credible because the "undisputed *material* facts in the record regarding Absolute's protracted delinquencies, unpersuasive explanations for those delinquencies, and the absence of concrete remedial changes to ensure compliance demonstrate that Absolute is likely to violate the reporting requirements in the future regardless of the viability of its funding resources."[42] Moreover, Absolute had continued to struggle with its ability to establish and maintain internal control over financial reporting.[43] Finally, Absolute was a shell company with one employee who presented an unilluminating explanation of why the company ignored its reporting obligations until it was faced with a revocation proceeding, and two of the company's latest quarterly reports contained inaccuracies.[44]

Here, Can-Cal is not a shell company and Candeo is required by the court-approved settlement to buy volcanic material from Can-Cal for approximately $150,000 each year for at least 20 years. Can-Cal's chairman declared that "[t]hese payments alone should more than adequately cover the costs to pay Can-Cal's audit firm" to prepare the documents necessary for its securities filings.[45] These facts distinguish Can-Cal's situation from every case the Division cites.[46] And, viewing the record in the light most favorable

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[42] *Id.* (internal footnote omitted).

[43] *Id.*

[44] *Id.* at *1, *3, *4.

[45] Can-Cal Supp. Opp'n (Jan. 4, 2019), Ex. 1 at 2.

[46] For example, the Division discusses the initial decision in *Ads in Motion, Inc.*, where the administrative law judge revoked an issuer's registration even though the issuer was not a shell company and had fully caught up in its periodic reports. Initial Decision Release No. 611, 2014 WL 2601712, at *5 (ALJ Jun. 11, 2014); *see* Div. Feb. 2019 Br. 2–3 & Ex. A. *Ads in Motion*, however, is a not a precedential decision. Moreover, the administrative law judge in that case was primarily persuaded by the fact that the company had "insufficient working capital to carry on normal day-to-day operations," was unable "to raise equity capital," and had "substantial doubt about [its] ability to continue as a going concern." *Ads in Motion*, 2014 WL 2601712, at *7–8. And although Can-Cal also has a "going concern" advisory in its most recent filings, that concern is mitigated by the guaranteed funding it is receiving from the agreement with Candeo. *See* Can-Cal Res. Ltd., Quarterly Report 12 (Form 10-Q) (Nov. 14, 2018) (noting uncertainty as to ability to continue as a going concern, but also noting that the company had $9,877 available to sustain operations as opposed to the $769 it had in December 2017).

to Can-Cal, I cannot say that its assurances of future compliance are not credible. Yet, since Can-Cal's financial health is dependent on Candeo's viability, there are also material questions of fact concerning Candeo's solvency that need to be addressed at a hearing.

Further, although the Commission frowns on sanctions other than revocation when issuers "'make last minute filings' only after becoming the subject of Exchange Act Section 12(j) proceedings,"[47] Can-Cal argues that its return to compliance was precipitated not by the proceeding, but by the conclusion of the shareholder litigation and the settlement agreement with Candeo. Can-Cal's argument is supported by the evidence; the court-ordered stipulation required Candeo to pay for Can-Cal's return to compliance. Moreover, due to the protracted nature of this proceeding, Can-Cal has now timely filed periodic reports for a year, demonstrating its ability to comply with its reporting obligations. And finally, Corporation Finance indicated that it did not find any material deficiencies in Can-Cal's comprehensive 10-K covering 2015 and 2016.

The Division has suggested that Can-Cal is not really current because it failed to file 10-Qs for 2016 and 2017.[48] But the Division's position does not establish that revocation is required as a matter of law when an issuer is currently filing its reports in a timely fashion and all the material information in the missing quarterly reports is available to investors in a consolidated 10-K.[49]

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[47] *Calais Res., Inc.*, Exchange Act Release No. 67312, 2012 WL 2499349, at *7 (June 29, 2012) (quoting *Nature's Sunshine Prods.*, 2009 WL 137145, at *6).

[48] As noted above, the Division made this argument at the May 2018 prehearing conference. In its October 2018 and February 2019 supplemental briefs, however, the Division acknowledged that Can-Cal was no longer delinquent in its periodic filings and said nothing about Can-Cal's failure to file 10-Qs for 2016 and 2017. *See* Div. Supp. Br. 1 (Oct. 31, 2018); Div. Feb. 2019 Br. 4.

[49] *See* Super-K at F-16 to F-21 (unaudited financials with the information that would have been in Can-Cal's missed quarterly reports). Although the Commission's "rules do not provide for the filing of consolidated annual reports," *e-Smart, Techs.*, 2004 WL 2309336, at *1 n.3, such as the one Can-Cal filed, the Division does not argue that Can-Cal is still delinquent in its annual reporting—only that it remains delinquent in its quarterly reporting. And in any event, the Commission has only stated its disapproval of

(continued…)

The Division also argues that Can-Cal failed to comply with other provisions of the Exchange Act, and that these failures can be taken into account when assessing sanctions. At one point the Division maintained that Can-Cal did not comply with Exchange Act Section 16(a) because it failed to file Forms 3 and 4 when new directors were appointed and when these directors became beneficial owners of the company's stock.[50] Can-Cal has since filed the appropriate Forms 3 and 4.[51] In its most recent brief, the Division argues that Can-Cal did not comply with Exchange Act Section 14(a) and (c) because it failed to file most proxy statements since its inception, which should weigh against its promises to remain current.[52] But because the Division first raised this argument in its final brief over a year-and-a-half into the proceeding, Can-Cal has had no opportunity to respond to it. And, in

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consolidated annual reports in the first instance. *See Calais*, 2012 WL 2499349, at *5 (explaining that "[i]f issuers were permitted, at their discretion, to consolidate multiple years of annual reports into a single filing, the investing public would not be assured of the timely disclosure mandated by the Exchange Act"). In other words, when an issuer files a consolidated annual report covering more than one year, it violates the reporting requirements by definition, as investors were deprived of timely financial information. The fact that the information is available after the fact in a consolidated report does not cure the violation. It is at least arguable, however, that as long as the consolidated report contains no material deficiencies, the issuer could be considered current in its filings. *See* Division of Corporation Finance, Financial Reporting Manual § 1320.4 (Dec. 1, 2017), https://www.sec.gov/divisions/corpfin/cffinancialreportingmanual.pdf (noting that even though filing a consolidated 10-K does not absolve a registrant from liability for its delinquency, Corporation Finance will generally not ask "a delinquent registrant to file separately all of its delinquent filings if the registrant files a comprehensive annual report on Form 10-K that includes all material information that would have been included in those filings"); *Am. Stellar Energy, Inc.*, Exchange Act Release No. 64897, 2011 WL 2783483, at *5 (July 18, 2011) (disapproving of a consolidated report because it did not contain a comparison between the audited financials of each year covered in the report). The same policy could apply to missing 10-Qs; the filing of a 10-K containing the material information that would have been in the 10-Qs does not absolve the registrant of liability, but is sufficient for the purposes of becoming current.

50 Div. Mot. 9–11 (Nov. 3, 2017).

51 Can-Cal Supp. Docs. (July 11, 2018), Ex. 2.

52 Div. Feb. 2019 Br. 5.

any event, viewing the facts in the light most favorable to Can-Cal and given its relative financial stability and its commitment to file periodic reports going forward, I am not persuaded at this point that the company's alleged failure to file proxy statements diminishes the credibility of its assurances against future violations of the reporting requirements.

In sum, there are material questions of law and fact remaining as to the appropriate remedy for Can-Cal's reporting violations. The Division has not met its burden on summary disposition to show that revocation of Can-Cal's securities is necessary for the protection of investors despite the company's efforts to become current and its assurances that it will remain current.

Order

The Division's motion for summary disposition is DENIED.

By April 5, 2019, the parties shall confer and file a notice, jointly if possible, indicating a preferred location for a hearing and a date for the hearing to commence by May 28, 2019. In their notice, the parties shall also provide a proposed schedule for the submission and exchange of witness and exhibit lists prior to the hearing and any other necessary prehearing submissions. I will not entertain prehearing briefs.

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James E. Grimes
Administrative Law Judge