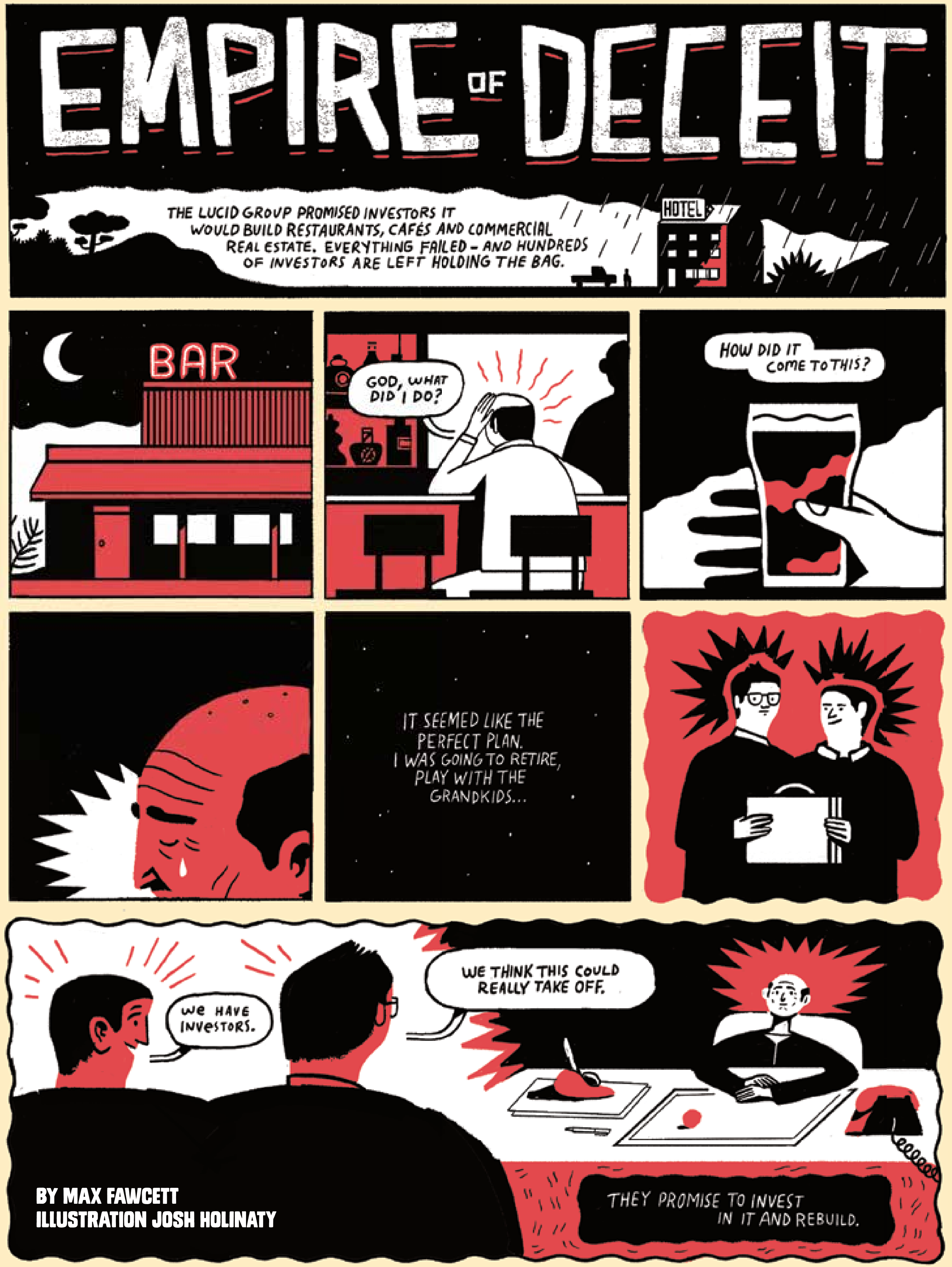
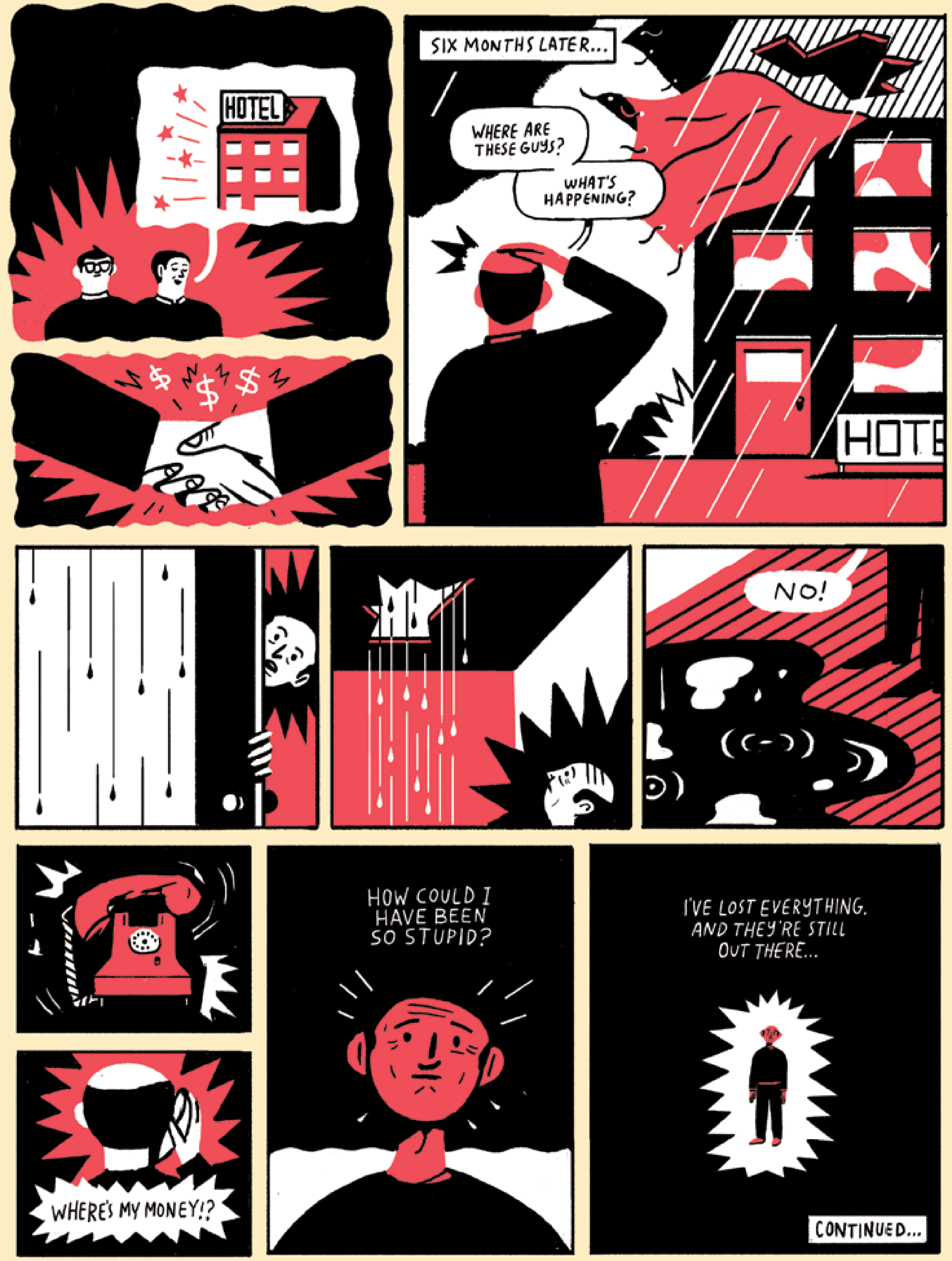

EMPIRE OF DECEIT
THE LUCID GROUP PROMISED INVESTORS IT WOULD BUILD RESTAURANTS, CAFÉS AND COMMERCIAL REAL ESTATE. EVERYTHING FAILED – AND HUNDREDS OF INVESTORS ARE LEFT HOLDING THE BAG.
HOTEL
BAR
GOD, WHAT DID I DO?
HOW DID IT COME TO THIS?
IT SEEMED LIKE THE PERFECT PLAN. I WAS GOING TO RETIRE, PLAY WITH THE GRANDKIDS...
WE HAVE INVESTORS.
WE THINK THIS COULD REALLY TAKE OFF.
THEY PROMISE TO INVEST IN IT AND REBUILD.
BY MAX FAWCETT
ILLUSTRATION JOSH HOLINATY


HOTEL
$ $ $
SIX MONTHS LATER...
WHERE ARE THESE GUYS?
WHAT'S HAPPENING?
HOTE
NO!
WHERE'S MY MONEY!?
HOW COULD I HAVE BEEN SO STUPID?
I'VE LOST EVERYTHING. AND THEY'RE STILL OUT THERE...
CONTINUED...

CONTINUED...

SILICON VALLEY HAS PRODUCED A LOT OF INTERESTING AND USEFUL THINGS OVER THE LAST DECADE OR SO, FROM LIFE-CHANGING SOCIAL NETWORKING APPLICATIONS TO A REDEFINITION OF JUST HOW CASUAL BUSINESS CASUAL DRESS CAN BE.

One of those key exports is its willingness to embrace, and even celebrate, the experience of failure. Dave McClure, an angel investor and founder of 500 Startups, told Inc. magazine writer Eric Markowitz that he often refers to his tech incubator as "the fail factory." Tech entrepreneurs aren't the only people falling over themselves to acknowledge the virtues of failing. J.K. Rowling gave a stirring commencement address at Harvard about the role it played in her career. There are literally dozens of TED Talks on it. And it seems like every business publication on the planet has produced at least one piece of service journalism on the subject.

But regardless of how they do it, those who worship at the altar of failure have one thing in common: they view it as a transitional stage, the entrepreneurial equivalent of adolescence. It isn't supposed to happen over, and over, and over again, the way it did for 20-something former competitive figure skater Adam Drybrough and Blaine Kennedy, his much older business partner. Over the course of a seven-year period, the pair left a string of broken businesses and failed ventures in their wake that practically defies belief both in the variety of their purpose and the consistency of their outcome. There was Chiasso, a chain of coffee shops launched in 2010 and expanded to a few locations in Calgary. By September 2013, the landlord of its last location was changing the locks. There was Calgary's Flatiron Restaurant & Bar, which opened with fanfare and closed soon after. There was a restaurant concept called Kaynes, which promised "great food and timeless rock" but whose last Twitter post, on September 1, 2011, said it was closed to "deal with a plumbing upgrade."

These failed businesses were merely the public face of the pair's apparent ineptitude. They were overshadowed – and, some say, underwritten – by a series of failed exempt market deals they sold to investors. Virtually all of those investors have been left with nothing, other than varying degrees of anger, humiliation and frustration, to show for the tens of millions of dollars they entrusted to Drybrough and Kennedy between 2007 and 2012. The only real question that's left, one that a Court of Queen's Bench judge will answer later this year, is whether those failures were merely the product of two colossally incompetent businesspeople or whether they were done by design. And make no mistake: there were no happy outcomes, no edifying lessons to be learned from their experience. Except one, perhaps: trust nobody.

IT'S A SPECTACULAR FALL FROM GRACE FOR A company that, a few years ago, was a toast of the town. In an August 2008 profile in the *Calgary Herald*, then 23-year-old Drybrough, the public face of the Lucid Group of Companies, talked up the aspirations and achievements of his fledgling outfit. He claimed it had 35 employees and would reach $60 million in sales that year. The company, he said, dabbled in everything from luxury rentals in Calgary to real estate development in Fort McMurray and even an RRSP-eligible investment fund that targeted distressed U.S. real estate in Arizona, California and Florida. What was the secret to their success? "We haven't put our heads down and stayed the course," Drybrough said. "We adapted. In this market, you have to adapt because what makes money two years ago is not going to make money now." As it turned out, nothing they did made money.

It might be tempting to blame that on some epically bad timing. After all, when Drybrough spoke with the *Herald*, the global economy was in the midst of falling apart. They wouldn't be the first entrepreneurs to take on too much leverage at precisely the wrong time, only to have their creditors call their loans and repossess their assets. There's just one problem with that theory: based on a series of interviews with investors and the evidence contained in a mountain of court documents, that doesn't appear to be what happened with the Lucid Group. Instead, there's a consistent pattern across their various projects of double-dealing, related party transactions and, the ASC alleges, outright fraud.

> **Pius Pfeifer knew there was trouble when he started receiving phone calls from investors wondering why they hadn't received their scheduled interest payment.**

Actually, there's more than one problem with the bad-timing theory. After all, Lucid was raising money long after oil prices had bottomed and the global recovery had gained traction. Grant Chorney, an accountant and an investor in the Lucid Group's Ramsay Crossing project (a real estate development in southeast Calgary), had the misfortune of living a few doors down from Drybrough. "I'd spoken to him about the project, and it seemed pretty viable," Chorney says. "They seemed to have a lot going on at the time." He plunked $150,000 down, but by May 2012, the monthly interest payments Chorney was due on his investment stopped coming, and he quickly realized that they might not ever start up again. "They would just not return calls, and there was no correspondence of any sort that there was any problem with the project."

BROKEN PROMISES AND FAILED VENTURES

Just a few of Lucid's failed businesses; FlatIron, Chiasso and Kayne's

In the end, the original owner from whom Lucid had bought the land ended up foreclosing on it and repossessing the asset. Trades that had done some early excavation and site preparation work went unpaid. Even the city ended up getting stiffed on the property tax bill. And the more Chorney thought about it, the more he believed he'd been had from the outset. "There was never any intent, in my opinion, to complete any project that they were ever involved in," he says. "Their *modus operandi* was to collect as much money as they could, and lay out as little money as they could, and then walk away from the project."

That certainly seems to be the case with Lucid Fort McMurray, a project that promised to take an old RV park that sat on 30 acres of land near the airport and turn it into a mixed-use commercial development. On October 22, 2008, the company issued an offering memorandum in which Lucid Capital Fort McMurray would seek to raise up to $16 million for the express purpose of loaning the funds to a related party, Lucid Commercial Fort McMurray, which would then buy the land and develop the property. The pitch was a superficially attractive one, given both the enormous growth in Fort McMurray and the fact that memories of near $150-per-barrel oil prices were still in people's minds. The investment was backstopped by a first charge of the lands, which they told prospective investors had been appraised independently at $25 million. The profits from the ongoing operation of the RV Park on the lands, meanwhile, would be directed towards the cost of developing them.

It seemed, in other words, like an investment with plenty of upside – most importantly, the double-digit interest rate it paid investors – and almost no downside. A total of 86 investors kicked in between $6,000 and $3 million each, and on December 30 of 2008 Lucid Commercial, "as assignee of Golden Eagle RV Park Holdings," bought the land for $7.5 million. But as Andrew Basi, a senior vice-president with Grant Thornton Alger and the eventual court-appointed bankruptcy trustee for Lucid Capital Fort McMurray, noted in a sworn affidavit dated June 13, 2012, that was the point of original sin. After all, Lucid Capital also paid a $2.5-million assignment fee to Golden Eagle RV Park Holdings. Its sole director? Blaine Kennedy.

Drybrough, the sole director of both Lucid Capital Fort McMurray and Lucid Commercial Fort McMurray, >

quickly incorporated a company just a few weeks after the land sale had closed called Lucid RV Park. This was not part of the deal that Lucid Fort McMurray's investors had signed up for, nor was it something of which they were even aware. It appears, based on Basi's testimony, that this new company's sole purpose was to insert itself in between the RV rental revenues and the company that was supposed to collect them. "Contrary to the information set out in the offering memorandum, Lucid Commercial did not operate or receive rental income from the RV Park," Basi attested.

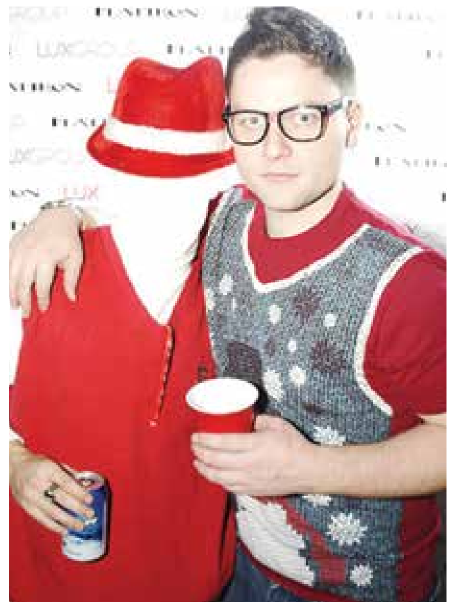
And while it's not clear what those net revenues were, they were considerable. Under the terms of its lease, Lucid RV paid Lucid Commercial $180,000 per year plus GST in rent. According to the park's previous owner, who sold it to Kennedy, it always made money – even during the slower winter months. Basi continued: "[The previous owner] also advised that the RV Park was profitable and during the last year that [he] operated the RV Park, the net income from operations was approximately $600,000."

The cherry on this shameful sundae was an agreement which effectively prevented Lucid Capital – the investors, in other words – from terminating the lease agreement with Lucid RV. In his 2012 testimony, Basi is clearly perplexed by it all. "It appears the only reason these agreements were entered into by the related parties is to divert the revenue derived from the Lands away from Lucid Capital and its Investors and to Kennedy and Drybrough."

The needlessly convoluted way in which Drybrough and Kennedy structured Lucid Fort McMurray, where one company (Lucid Capital) raised the money and then purchased the property from a related one (Lucid Commercial), wasn't a one-off. Instead, it appears to be standard operating procedure. "A virtually identical real estate investment structure was devised by Lucid Capital Barlow and Lucid Commercial Barlow (together, "Lucid Barlow"), with an investment in a freestanding single level restaurant building in northeast Calgary," Basi attested. "Both of the Lucid Barlow entities are now in bankruptcy proceedings and the investors are unlikely to recoup their full principal investments."

AND WHILE THE FORT MCMURRAY

scam may have been Drybrough and Kennedy's most lucrative, it wasn't their most craven. That title probably belongs to their dealings with Pius Pfeifer, the septuagenarian owner of the Capri Hotel in downtown Meadow Lake, Saskatchewan. The hotel had been built in 1971, and by the time Drybrough and Kennedy approached Pfeifer, he was well into his retirement and more than ready to sell. "I wanted to get out. I'm elderly, and the hotel needed a complete renovation. I didn't want to get into it anymore." The deal they pitched him was, at the time, worth entertaining: interest-only payments for three years while they paid for the renovations, and then the full balance of the purchase price. "They were squeezing me and squeezing me and I didn't want to say no. I was living in Edmonton, and it didn't make sense for me to hang on. That's why I sold."



Adam Drybrough, pictured at the opening of Flatiron. We were unable to find a picture of Blaine Kennedy

It was, he says, the biggest mistake of his life. Pfeifer knew there was trouble when he started receiving phone calls from Lucid investors wondering why they hadn't received their scheduled interest payment. By all accounts, Drybrough and Kennedy did what they had done – and would do – with other projects, selling investors on the inherent value of the land and the rich stream of double-digit interest payments they'd receive and making a few initial payments to them and doing a bit of cursory site prep work before going AWOL. In the case of the Capri Hotel, that meant starting to install a new roof before apparently abandoning the work – and the hotel. "Everything had to be replaced, there was so much damage," Pfeifer says. "And by the time I got going I found more and more. If I would have known at the beginning I probably would have walked away from it. They destroyed the building." They also stuck the contractors that had opened up the roof with unpaid invoices, and the Town of Meadow Lake with an outstanding property tax bill worth more than $44,000 and a gaping wound in the heart of its downtown.

The Lucid saga raises many questions, not the least of which is why they were able to raise so much money in the first place. Drybrough had been fined $25,000 back in 2009 by the Alberta Securities Commission for using the word "guaranteed" in reference to the revenue streams mentioned in advertisements for its Lucid St. Petersburg offering that were placed in the *Edmonton Journal* and *Calgary Herald*. Kennedy, meanwhile, had a history with the ASC that made Drybrough's infraction look like a misunderstanding. As the ASC itself noted in its February 16, 2012, decision assessing – and denying – Kennedy's application to become an exempt market dealer under the auspices of Harrington Capital, he was the epitome of someone who shouldn't be allowed near capital markets. There was the fact that he'd declared personal bankruptcy twice, discharged first from it in 1998 and again in 2007. There were the numerous civil actions that he'd been named in, many of which involved securities-related transgressions and all of which ended either in consent or default judgments. "ASC Staff further submitted that the evidence of past financial difficulties pointed to poor judgment skills and a heightened risk that there may be a propensity to 'engage in self-interested activities at the expense of clients', should future financial problems arise," wrote David Linder, the executive director of the ASC.

Given that record, how did they manage to raise any money at all? In part, it's because the people entrusting Kennedy and Drybrough with their money didn't know about any of this. But it's also because they were good at what they were doing: selling. They had convincing marketing materials and investor presentations, and they knew how to convince the people who attended them that their interests were the same as Lucid's interests. Take the email exchange that Jason Nelson, who invested $300,000 in Lucid Fort McMurray, had with Lucid salesman Darin Marchewka. "Lucid invests a lot of money in the marketing and advertising of the investments as well as in due diligence of projects," Marchewka wrote to Nelson in late October 2008. "We have two law firms that do due diligence to make sure nothing is missed. The most important thing that Lucid has in the game is our name. If you notice all our investments have the Lucid name in them.... We have everything to lose by putting our name on all our projects. If we do one bad deal, it could affect all our companies."

> **"We have two law firms that do due diligence to make sure nothing is missed. The most important thing that Lucid has in the game is our name."** – Darin Marchewka, Lucid salesman

They were also good at playing on the perception that real estate's inevitable trajectory is upwards, and at using other sources to bolster their credibility, be it the media, other businesspeople or just conspicuous displays of wealth. In 2010, for example, they spent $65,000 sponsoring former Rangeland Derby champion Kelly Sutherland's chuckwagon. That was on the heels of a similar sponsorship of Vern Nolin in 2008. Bernard Callebaut, the former owner of his eponymous chocolate company who's now plying his trade as Papa Chocolat, dealt briefly with Drybrough and Kennedy in 2011, when they agreed to provide him with some capital in exchange for a working partnership that would see his chocolates sold at their Chiasso Café and Flatiron locations. But Callebaut says it quickly became clear that they were more interested in leveraging his brand value to buttress their own. "They wanted to use me to raise money – use my name," He says. "I've been in business for 30 years in Calgary, so my name definitely had some meaning to the business community. That's the way I see it – that's my feeling. Because, ultimately, they didn't do anything. They didn't have the money. They simply didn't have the money. And then they came up with a whole bunch of excuses. You don't do this, you don't do that and that's why we didn't give you the money. But the bottom line is they didn't have the money."

WHILE IT MIGHT BE TEMPTING TO

write off as the authors of their own misfortune, people who either failed to understand that the rates of return promised by Lucid – often approaching 20 per cent – could not come without some degree of risk, Ron Reinhold says we shouldn't do so. He's the owner of Rainbow Investigations, a former private investigator and an expert on mortgage fraud. "These victims, for the most part, are real victims – they're not sophisticated," he says. "Most of them have never bought a property in their life or made a real estate investment in their life. So they don't really understand what questions to ask. You show them a thick legal document and they don't know what to read or what to look for there."

Dana, a woman who didn't want her last name used to protect the privacy of her parents, wishes she'd encouraged them to take those thick legal documents to a lawyer. They ended up investing $400,000, much of it drawn from their RRSPs, in two Lucid projects. When those projects went south, Kennedy said it was her parent's fault. "One of the things Blaine told people is that they knew what they were getting into. He blamed them, basically, for what was happening." Did her parents know what they were getting into? "No, they didn't. And now they wish they would have looked into the paperwork and the contract. I remember my parents sitting on my couch and looking at the Fort McMurray hotel. I'll never forget it for as long as I live – they sat on my couch and said, 'Should we do this or not?'"

And while there's still hope they'll recover some portion of the money they invested, the stress of the entire experience has weighed on her parents. "Quite often, we'll have that conversation, but we keep it away from Dad as much as we can. He has enough stress already, and I wouldn't want him to have any more. The last five years have aged him – it's depleted him. That was his living – that was his life. And it's gone. To know you're going to have to sell your house and live in something shabby for the rest of your life, knowing that somebody else has your money? I feel pretty sorry for them. It's degrading."

If there's any solace in this story, it's that there won't be any more victims. After years of trading on their reputation and the unwillingness of regulators to more aggressively examine their behaviour, the conduct of Drybrough and Kennedy has caught up with them. In October 2012, they were charged jointly with 17 criminal counts, ranging from fraud and making false statements to trading in securities without a prospectus. Kennedy was slapped with an additional 23 charges. This July, they'll have to answer for all of them. AV