AMENDED THIS October 4, 2010 PURSUANT TO
MODIFIÉ CE CONFORMÉMENT À
☑ RULE/LA RÈGLE 26.02 (A)
☐ THE ORDER OF
L'ORDONNANCE DU
DATED / FAIT LE
J. Stevens
REGISTRAR GREFFIER
SUPERIOR COURT OF JUSTICE COUR SUPÉRIEURE DE JUSTICE

Court File No. 10-0690

ONTARIO

SUPERIOR COURT OF JUSTICE

BETWEEN:

GEORGE FRENCH

Plaintiff

- and -

INVESTIA FINANCIAL SERVICES INCORPORATED, MONEY CONCEPTS (BARRIE), DIAMOND TREE CAPITAL INC., DAVID KARAS AND FINANCIAL VICTORY ASSOCIATES INC.

Defendants

Proceeding under the *Class Proceedings Act,* 1992

AMENDED STATEMENT OF CLAIM

TO THE DEFENDANT(S)

A LEGAL PROCEEDING HAS BEEN COMMENCED AGAINST YOU by The Plaintiff(s). The claim made against you is set out in the following pages.

IF YOU WISH TO DEFEND THIS PROCEEDING, you or an Ontario lawyer acting for you must prepare a statement of defence of Form 18A prescribed by the Rules of Civil Procedure, serve it on the Plaintiff(s) lawyer(s) or, where the Plaintiff(s) do(es) not have a lawyer, serve it on the Plaintiff(s), and file it, with proof of service, in this court office, WITHIN TWENTY DAYS after this statement of claim is served on you, if you are served in Ontario.

If you are served in another province or territory of Canada or in the United States of America, the period for serving and filing your statement of defence is forty days. If you are served outside Canada and the United States of America, the period is sixty days.

Instead of serving and filing a statement of defence, you may serve and file a notice of intent to defend in Form 18B prescribed by the Rules of Civil

Procedure. This will entitle you to ten more days within which to serve and file your statement of defence.

IF YOU FAIL TO DEFEND THIS PROCEEDING, JUDGMENT MAY BE GIVEN AGAINST YOU IN YOUR ABSENCE AND WITHOUT FURTHER NOTICE TO YOU. IF YOU WISH TO DEFEND THIS PROCEEDING BUT ARE UNABLE TO PAY LEGAL FEES, LEGAL AID MAY BE AVAILABLE TO YOU BY CONTACTING A LOCAL LEGAL AID OFFICE.

Date: June 25, 2010

Issued by: N. MAISONNEUVE
Clerk / Registrar
Superior Court of Justice

Address of court office:

114 Worsley Street
Barrie, ON L4M 1M1

TO: Investia Financial Services Incorporated
522 University Avenue, 4th Floor
Toronto, ON M5G 1Y7

AND TO: Money Concepts (Barrie)
c/o Investia
522 University Avenue, 4th Floor
Toronto, ON M5G 1Y7

AND TO: Diamond Tree Capital Inc.
35 Worsley Street
Barrie, ON L4M 1L7

AND TO: David Karas
35 Clapperton Street
Barrie ON L4M 3E6

AND TO: Financial Victory Associates Inc.
35 Clapperton Street
Barrie ON L4M 3E6

CLAIM

1. The Plaintiff, George French, claims on behalf of himself and on behalf of each member of the class in Ontario:

(a) general damages in the amount of $2,000,000.00 for each;

(b) reimbursement of all commissions and/or fees and the recovery of all premiums paid for unnecessary and inappropriate life insurance, together with prejudgement interest thereon;

(c) an accounting for all compensation paid to any of the Defendants by members of the class and, in the alternative to the claim for damages, restitution in an amount to be determined by such accounting pursuant to the principles of waiver of tort;

(d) punitive and/or exemplary damages in the sum of $50,000,000.00;

(e) Interest on all sums owing at the rate of interest charged by lenders (described hereafter) to class members in connection with loans arranged by the Defendants and/or prejudgment interest in accordance with the *Courts of Justice Act*;

(f) the costs of this action on a substantial indemnity basis together with applicable Goods and Services Tax and/or Harmonized Sales Tax payable pursuant to the provisions of the *Excise Tax Act*, R.S.C. 1985, c. E-15, as amended, and/or any other applicable legislation; and,

(g) such further and other relief as this Honourable Court may deem just.

Overview

2. This claim is brought by the proposed representative plaintiff, George French, a farmer who sought to protect his savings by relying on the advice of his financial advisor. George French and the other class members fell

victim to investment strategies designed to generate compensation for the advisor (hereafter described) and his firm and associates at the expense of the advisor's clients. These strategies involved borrowing to invest in mutual funds, and are referred to herein as "Leveraging" or the "Leveraging Scheme."

3. The advisor and his firm encouraged the Leveraging which was unsuitable for all class members, including George French. The interests of the advisor and his firm conflicted with those of class members in that the said strategies increased revenue to the advisor and his firm without benefit, and at unsuitable risk, to their clients.

The Parties

4. The Representative Plaintiff, George French ("George"), is a retired dairy farmer who was born in 1952. He resides in Phelpston, a village outside Barrie, Ontario. George is a representative of a class of persons ("the Class Members") all of whom were clients of Karas, who purchased financial products from one or more of the Defendants through the Leveraging Scheme. The Class Members are hereinafter also referred to as either the "Clients" or the "Plaintiffs" and may be further defined in the motion for certification. The Plaintiffs plead and rely upon the provisions of the *Class Proceedings Act, 1992, S.O. 1992, c. 6.*

5. The Defendant, Money Concepts Canada ("MCC") was a financial advisory firm with offices across Canada. In 2001, AEGON Dealer Services Canada Inc. ("AEGON") purchased the assets and trade name – and continued the business – of MCC. Investia Financial Services Incorporated ("Investia") is a mutual fund dealer with offices across Canada, including in Barrie. It is

registered with and regulated by the Ontario Securities Commission ("OSC") and the Mutual Fund Dealers Association ("MFDA"). Investia merged with and is the successor company of AEGON effective September 30, 2008. For the purpose of this pleading, all references to the "Firm" shall mean Investia, AEGON and/or MCC, as the case may be. Investia is liable in law for the conduct of its predecessors, AEGON and MCC.

6. Money Concepts Barrie ("MCB") was the trade name of the Barrie branch office of the Firm, and carries on business selling mutual funds, insurance and financial advice to the Firm's retail investors in that neighbourhood. MCB was the Firm's top Canadian branch by sales performance from 1988 to 2009 and top international branch from 1993 to 2009. The Firm is liable for the conduct of MCB.

7. Financial Victory Associates Inc. ("FVA") provides financial advice and services to retail investors for compensation. It has offices in Barrie and it is not registered with the OSC despite Ontario Securities Act ("OSA") requirements for such registration, as an advisor. FVA and MCB shared advisors, office premises, staff, clients, private client information, advice to clients and written communications. All FVA clients were clients of the Firm and were referred to FVA directly or indirectly by the MCB office. FVA circulated the alerts and advice for the stop-loss component of the Leveraging Scheme directly to its Clients and also to MCB's advisors and staff for the purpose of providing financial advice and generating solicited and discretionary trades for Clients arising from the stop-loss component of the Leveraging Scheme.

8. Diamond Tree Capital Inc. ("DTC") is an unregulated financial advisory firm maintained by David Karas to operate several financial advisory businesses, either directly or through affiliated companies. The stop-loss component of the Leveraging Scheme was run through a DTC business. All DTC businesses have offices in Barrie.

9. David Karas ("Karas") is a well-known media personality in and around Barrie. He is a published author, with books published in association with MCB and the Firm and resides in Barrie. He was formerly registered as a mutual fund salesperson and remains registered as an insurance salesperson. Karas represented to Clients that he held the designations of CFP, RFP and RFC. He was therefore obliged to adhere to the standards of the organizations that grant and regulate such designations. He is the directing mind of all the other defendants except the Firm, (which are hereinafter referred to as the "Karas Companies") and served as a director of MCC. Karas was rewarded for being the Firm's top Canadian individual producer by sales from 1989 until 2009, which Karas represented to Clients as evidence of his superior skills as a financial advisor and planner.

10. At all materials times, Karas acted for Clients directly and/or through agents, or sub-advisors employed by the Firm and/or the Karas Companies.

11. Karas was at all materials times acting on behalf of the Karas Companies and/or the Firm, who are responsible for his actions and those of the Karas Companies.

The Investment Scheme

12. The Firm and/or Karas and/or the Karas Companies, for whom the Firm is responsible, recommended to Class Members, a one size-fits all investment strategy based on the Leveraging Scheme (which is further defined in the paragraphs below), without regard to the suitability of the strategy for any individual client and without consideration of each individuals client's investment objectives.

The Leveraging Scheme

13. In 2003, Karas implemented the Leveraging Scheme to increase the commissions and other compensation generated for his own benefit, that of The Karas companies, and that of the Firm, without regard to the suitability of such strategy for his Clients.

14. The Leveraging Scheme was based on layering levels of debt for each client. First, he had Clients borrow as much from their own lending sources as possible with a view to raising money to buy mutual funds, increasing the Clients' assets under his management (or "AUM"). This permitted Karas to use the client's AUM as collateral to have them borrow more money from lenders who advanced loans on the collateral security of mutual funds he acquired for class members, effectively using borrowed money to borrow more money.

15. The more those Clients borrowed for investment, the more compensation was paid to Karas, the Karas Companies and the Firm.

16. Contrary to Karas' advice and representations, the most significant impact of the Leveraging Scheme on Clients was that greater debt caused

greater debt-carrying charges and a greater risk exposure, in the event that underlying investments failed to attain the higher returns required to carry the debt or in the event the underlying investments declined in value.

17. When Karas presented the Leveraging Scheme to Clients, he represented that Leveraging would reduce Clients' investment risk and that the carrying charges in respect of the loans, and any premiums on insurance he sold, would be paid through the profits earned by the investments. Karas also represented that the value of the investments would increase over each and every 12 month period. These representations were false and made for the purpose of enticing Clients to increase their investments for the benefit of Karas, the Karas Companies and the Firm.

18. Karas did not properly, or at all, disclose to Clients the actual risks associated with the Leveraging Scheme.

19. The Leveraging Scheme was a one-size-fits-all solution for Clients. Karas failed in his regulatory duty to tailor the investment recommendations to specific Clients, simply recommending the maximum possible loans for every client.

20. The Firm knew of Karas' implementation of the Leveraging Scheme as a general strategy to increase AUM and thereby increase compensation for Karas and the Karas Companies and the Firm. The Firm rewarded Karas for his resulting sales successes.

The Dealings between George and Karas

21. George and his late father, Elmer, were dairy farmers. They jointly owned and operated a dairy farm, quota and herd of cattle in Phelpston. Prior to seeking financial advice from the Firm, they invested their savings in guaranteed bank deposits ("GICs"). Their needs were modest, as was their income. George had saved $300,000 as the basis for his financial security in retirement.

22. George never married. Neither Elmer nor George had any dependants.

23. In 1992, Elmer and George sought financial advice outside their local bank branch and they began to deal with Virginia Lamb ("Ms. Lamb"), the manager of the Barrie branch of MCC. Elmer and George had a high school education only and had no financial experience outside of farming. Their goal was to preserve their savings and to reduce any risk to their financial security. When Elmer died in 1999, George inherited the farm, quota, herd of cattle and their joint savings.

24. In January 2000, George owned the farm, the herd and dairy quota, and maintained approximately $380,000 in two Firm investment accounts with Ms. Lamb, a registered retirement savings plan ("RRSP") and an open account. Both accounts held mutual funds purchased on the advice of Ms. Lamb. George had no debt.

25. In 2000, Ms. Lamb advised George to borrow $78,000 to invest in mutual funds. She represented to George that this was a safe and secure method of preserving his capital. George relied on and followed her advice. At

that time, George's income varied from $30,000 to $60,000, depending upon dairy market conditions. Ms. Lamb did not explain, and George was not aware of, the risks inherent in Leveraging.

26. In 2002-2003, Ms. Lamb retired. By 2003, Karas had assumed control over Ms. Lamb's clients and book of business, including George's accounts.

27. In 2003, Karas succeeded Ms. Lamb as the Firm's authorized advisor with respect to George's account, and as the Barrie branch manager.

28. Karas immediately recommended and implemented the Leveraging strategy to George, who relied on and followed this advice to his detriment. In 2003 and 2004, Karas recommended and arranged for George to borrow a further $300,000 from B2B Trust, Manulife and TD Canada Trust, for the purpose of investing with Karas and the Karas Companies and the Firm. By the end of 2004, George's total leveraged loans were $382,000.

29. With each leveraged loan the compensation paid to Karas and the Firm increased substantially. So, too, the risk of loss to George increased substantially.

30. In 2005, George sold his dairy quota. As a result of the sale, George ceased to earn income from the farm. He so advised Karas. In recognition that a material change had occurred in George's affairs, Karas completed an updated "Know Your Client" (or "KYC") form that identified George's investment objective as being 50% fixed income and 50% long term

capital growth, and that he had a "medium" risk tolerance. It showed his income as greater than $150,000.

31. Karas knew that KYC was inaccurate in that:

(a) The income recorded on the KYC resulted from the one-time sale of the dairy quota and did not indicate George's future or historic income and was made with the intent by Karas to mislead the Firm and lenders to support Karas obtaining further Leveraging loans for George;

(b) Karas knew that the Leveraging Scheme made even medium-risk mutual funds a high-risk investment; and,

(c) Karas knew that George's objectives were current income and preservation of capital.

32. In 2005 and concurrently with the 2005 KYC update, Karas advised George to increase his loans by a further $300,000 from AGF Trust and B2B Trust to invest with the Firm and him.

33. In 2006 Karas recommended and arranged for George to borrow $189,000 from TD Canada Trust, and in 2007, a further $180,000 from AGF Trust. By the end of 2007, George's loans exceeded $1 million.

34. From 2000 to 2007, George's loans increased from nil to over $1 million. During the same period, his investments (gross) increased to $1.3 million. George owed loans almost equal to his open investments (i.e. excluding the RRSP). George's investment equity of approximately $300,000 had not materially changed, although there was an appearance of tremendous growth. In fact, there was only an increased risk of severe loss.

35. At all material times, Karas was aware that severely declining market conditions would likely occur within the foreseeable future and that when such a market decline occurred; Clients were at a significant risk of losing all, or

more than all, of their capital. In George's case, Karas and the Firm knew that when a market decline occurred, George's investment equity could be wiped out and he would be facing net loans without the ability to repay them. Karas and the Firm failed to advise George of this foreseeable and cyclically likely risk.

Market Decline in 2008-2009

36. From August 2008 to February 2009, George's portfolio was decimated by market conditions and the commissions and compensation he paid. George's losses exceeded those of the equity markets generally because:

(a) His portfolio asset allocation was overwhelmingly in equities and contained less than 8% fixed income securities, contrary to the 2005 KYC update information and contrary to his actual investment objectives;

(b) Much of his portfolio was allocated to unsuitably high risk investments, including smaller companies, companies in emerging markets, and companies in narrow economic sectors;

(c) Much of his portfolio was allocated to assets in foreign currency at a time when the Canadian dollar appreciated in value;

(d) His portfolio contained no cash;

(e) Because so much of his portfolio represented borrowed money, his ownership value disappeared and he owed far more than the value of his holdings; and,

(f) The borrowing costs, investment fees and insurance premiums greatly exceeded the small income generated from the portfolio.

37. In November 2008, the change in George's account was a material change in his financial circumstances. Industry regulations required an update of George's investment objectives. Karas prepared a new KYC form to reflect the

existing holdings of 10% income and 90% long term capital growth. This update did not reflect George's actual objectives, but better reflected his actual portfolio holdings but for the Leveraged loans. The actual portfolio was very high risk and short term by reason of the debt, and remained unsuitable for George.

38. The loans arranged by Karas for George provided for interest-only payments monthly. This limited the withdrawals from the AUM, thereby maximizing his compensation with an increased risk of loss to George. Leveraging therefore created a conflict of interest between advisor and client. George wanted to pay down principal, but Karas advised against this, and George followed this advice.

Insurance

39. In 2006 and 2007, Karas advised, and arranged for, George to purchase life, critical care and long-term care insurance, for premiums totalling $22,000 annually. This was more than George's disposable income.

40. The life insurance policy sold to George was unsuitable in that Karas knew that George had neither the need nor the wish to leave an estate. The life insurance policy also was unsuitable for George as he could not afford to maintain that policy's premiums, despite Karas' representation that all premiums for all policies would be paid from the profits earned through the Leveraging Scheme.

41. The policy was sold in a manner that maximized Karas' compensation. Its cost was initially low but carried escalating premiums through a yearly renewable term, in which the premium would increase as George aged,

beyond any foreseeable ability of George to pay. Karas did not warn of the impact of the escalating cost when he sold the contract to George. He did not disclose the compensation he received. He arranged for payment of these policies beyond any commission "claw-back" period to ensure payment of the maximum compensation, all without regard to George's best interests.

FVA

42. Toward the end of 2006, Karas created FVA, to provide market timing alerts with appropriate moments to sell or purchase funds. These alerts were intended to serve as investment recommendations to Clients. FVA included a stop-loss component for Clients which required Karas to sell relevant holdings if they reached pre-defined loss thresholds. Karas represented to Clients that they would make greater market profits and eliminate the exposure of their holdings to loss by subscribing to and paying a fee (the "FVA Fee") for this service.

43. Karas did not disclose to Clients how the additional FVA Fee further impeded their ability to earn a profit from Leveraging and how it increased the risk of loss. The FVA charged an annual fee equal to 0.75% of George's mutual fund holdings, so that the funds had to earn a profit of at least another 0.75% per annum to offset the added expense.

Conversion of RRSP Accounts

44. In January 2009, Karas arranged for Clients in or nearing retirement to convert their RRSP accounts into registered retirement income fund accounts ("RRIF") to assure lenders that Clients had the cash flow to pay interest on the loans, FVA Fees, and insurance premiums. In George's case, Karas had assured him that the growth in the open account would cover all the carrying charges for loans and insurance. After the decline in the value of his account in late 2008, Karas demanded that George pay these carrying charges from other sources or convert the RRSP to RRIF. George chose the latter course.

45. None of the RRIF withdrawals provided George with income, as all such funds had to be used to pay these charges. The advice to convert from RRSP to RRIF, absent the prior acts of negligence, was inappropriate and prevented George's registered account from participating in the market rebound of 2009.

George's Account

46. By early 2009, George owed $500,000 more than his portfolio value, a loss of $880,000 from the inception of Leveraging in 2000. George's holdings with the Firm outside the RRIF are pledged to his lenders. As a result of his losses, George has been unable to find a financial advisor prepared to provide advice in connection with that portfolio.

47. At periodic meetings between George and Karas, Karas used terms George did not, and could not be expected to, understand. At the conclusion of

each meeting, Karas produced several documents for George to sign without offering George the opportunity to read them or to ask questions. Karas advised George at such meetings:

(a) not to review the paperwork;

(b) that the documents were routine and insignificant;

(c) to rely on Karas' summary as complete and sufficient;

(d) to sign incomplete forms; and,

(e) to sign blank forms.

Conflict of Interest

48. At all material times, Karas knew that the interests of Karas, the Karas Companies and the Firm conflicted with the interests of George in that Karas, the Karas Companies and the Firm benefited without any risk to them when George borrowed money from others to invest with them (by which they earned compensation) while George's risk and costs materially increased by Leveraging.

49. Karas owed an obligation to George and to all his clients to avoid conflicts of interest. He breached this obligation with George and with his other clients in that:

(a) He had discretion in selecting lenders, product issuers, product types and product amounts, and he chose to recommend lenders, and issuers, types, and amounts of products that were calculated by him to generate the most revenue for the Defendants, without considering whether these recommendations were the most suitable for his clients, or even whether they were suitable for his clients at all;

(b) He had discretion in recommending investment strategies and he chose to recommend the strategy that was calculated by him to generate the most revenue for the Defendants without considering whether it was the most suitable for his clients, or even whether it was suitable for his clients at all;

(c) With respect to the documents that he provided his clients for signature, he had a discretion in informing his clients as to which documents, and which portions of such documents, they should read before they undertook commitments, and he chose not to identify those documents and portions of documents that explained to his clients their actual or potential risks and obligations. Further, he accepted the signatures of his clients with the knowledge that they had assumed obligations and undertook risks without understanding the nature thereof;

(d) He had discretion in providing advice to his clients with respect to the potential risks and rewards arising from decisions made by his clients, and he chose to provide such advice in a manner that was calculated by him to generate the most revenue for the Defendants, without explaining the risks (as to likelihood of loss, the extent of that loss and the volatility of the strategies) and the rewards (both as to likelihood of rewards and the extent of that reward); and,

(e) He had discretion in recommending advisory services to his clients, and he chose to recommend FVA as an advisory service so as to generate substantial revenue for himself, and without disclosing his personal interest in FVA. Further, he failed to disclose to his clients that he was the principal investment strategist behind FVA and that he was unqualified and inexperienced in such field of endeavour and that he was compensated for this role. Further, he failed to disclose to his clients that the FVA system had not been back-tested, could not be independently verified as being valuable to clients, was discretionary to Karas, was not reliable and was of no value whatsoever to his clients. He represented to his clients that the FVA offered investment advantages that were speculative or untrue, knowing that his clients lacked the sophistication to assess the value proposition.

Class Experience

50. The Plaintiffs plead that George's experience with Karas, the Karas Companies and the Firm as described in paragraphs **20 to 48** above, was typical of the experience of Class Members. The Plaintiffs further plead that the Leveraging Scheme was misrepresented to all Class Members in a similar manner and that each of them were, as the result of the Defendants' breach of duty, similarly exposed.

Involvement by the Firm

51. Karas provided the Firm with full details of the Leveraging Scheme and the Firm accepted this scheme as compliant with its duties and obligations to its Clients until August 2008.

52. In August 2008, Investia conducted an audit of the activities of MCB and Karas as part of its purchase of AEGON. Investia discovered significant breaches of process and standards, including breaches of regulations. Investia was required by the MFDA and the OSC to report these breaches but failed to do so. Investia failed to warn the Clients of the breaches related to their investments and the investment advice they received from Karas.

53. At the same time, Investia also terminated use of FVA and the stop-loss mechanism which was designed to provide notice to the Clients of changes in the value of their investments, thus rendering ineffective the stop-loss component of the Leveraging Scheme upon which Clients relied in particular during a declining market. Even after FVA and the stop-loss mechanism was

terminated. Clients continued to pay FVA Fees while relying on the safety net they had been told that it represented.

The MFDA and OSC Rules

54. The MFDA regulates registered mutual fund dealers and their financial advisors across Canada including the defendant Investia.

55. The OSC is the regulatory body responsible for overseeing Ontario's companies and individuals dealing in and advising on securities in Ontario and Ontario capital markets. The OSC's oversight includes the development and enforcement of rules to safeguard investors and to deter misconduct by licensed dealers and financial advisors, including the Defendants.

56. The MFDA was established by the Canadian Securities Administrators including the OSC, as a self-regulating organization responsible for the operations, standards of practice and business conduct of mutual fund dealers and their representatives, including the Defendants. The MFDA's mandate includes enhancement of investor protections.

57. MFDA Rule 2.2.1 requires that every new account application must include Know-Your Client information ("KYC" information) before an account can be opened. The KYC information requires each MFDA member and financial advisor acting on their behalf to learn the essential facts relative to each client and to each account accepted and to ensure that each order accepted or recommendation made for any account of a client is suitable and in keeping with the client's investment objectives.

58. Pursuant to the OSC's Staff Notice 31-505 Section 1.5(1)(b), registrants under the Ontario Securities Act are required to determine whether a proposed purchase, sale or holding of a security for a client is suitable by considering the general investment needs and objectives of the indidividual client and the attributes and associated risks of the products they are recommending to clients.

59. In April of 2008, The MFDA provided guidance to its members in Member Regulation Notice (MR-0069) of suitability guidelines. In particular, MR-0069 reminded members of their duties when assessing leveraging. The MFDA noted that leveraging is not suitable for all investors and that its members must ensure that leveraging recommendations are consistent with clients KYC information.

60. The MFDA's Member Regulation Notice (MR-0069) on Suitability Guidelines for Leveraging states as follows:

> "Leverage is not suitable for all investors and the appropriateness of a recommendation to use leverage must be assessed on a client-by-client basis, having regard to the client's age, financial circumstances, investment objectives, risk tolerance, time horizon, the manner in which they intend to secure and repay their loan and any other factors that are known at the time or reasonably ascertainable and may be relevant in the circumstances. Members must have policies and procedures in place with

respect to leveraging, including criteria that would indicate when it is an unsuitable strategy and the approval process."

61. The MFDA's Member Regulation Notice (MR-0069) also states that clients should not be relying on the growth of mutual funds in the account or make withdrawals from registered investments to make payments on borrowed funds used for leveraging.

62. The MFDA's Leverage Supervision Guide further states that "leveraging is likely unsuitable for unemployed, low income, self-employed (i.e. those with unstable income) or retired individuals." So too, clients relying on growth or distribution of from the mutual funds are likely unsuitable clients for leveraged investing.

Duty of Care

63. The Defendants at all material times owed a duty of care to the Class Members:

(a) To ensure that all KYC records were current, accurate, complete and sufficient and to make only suitable recommendations to buy, hold and sell as appropriate for each client's true KYC circumstances;

(b) To use due diligence to determine each client's investment needs and objectives, and to use due diligence to keep such information current;

(c) To ensure the suitability of all financial advice to each client;

(d) To explain to clients the risks of each of the securities and insurance contracts considered for his or her account and to procure his or her informed consent with respect to each transaction before making commitments to acquire or sell such securities and insurance contracts;

(e) To provide each client with a balanced presentation of available investment options and clear disclosure of the risks associated with the use of investment options such as Leveraging;

(f) To advise each client that using borrowed money to finance the purchase of securities involves greater risk than a purchase using cash resources only and that should clients borrow money to purchase securities, their responsibility to repay the loan as required by its terms remains the same even if the value of the securities purchased declines;

(g) To make full disclosure of all of the risks associated with the Leveraging Scheme;

(h) To ensure that the Leveraging Scheme only be used by clients that are comfortable with the higher risks associated with leveraging;

(i) To advise each client that the value of the leveraged portfolio may fall below the value of the loan;

(j) To advise each client that there is a magnification of risk where a leverage strategy is used;

(k) To advise each client that even where returns on leveraged investments are positive, interest costs may exceed the returns received;

(l) To advise each client that whether investment returns are positive or negative, the client must still pay back the loan plus the agreed interest, which may cause the client hardship;

(m) To advise each client that the client may be forced to realize losses as a result of the terms of secured loans;

(n) To advise each client that the client should not be relying on the growth of mutual funds in the account to make payments on the leveraged loan;

(o) To advise each client that the client should not have to make withdrawals from registered investments to make payments on the leveraged loan;

(p) To advise each client that any loans secured against the client's home can put the client's equity interest in the home at risk;

(q) To advise each client that if a client is relying on investment returns to cover the cost of borrowing and the investment falls in value, the client could default on the loan;

(r) To make full disclosure to each client of the expenses incurred by the client with respect to each of the transactions (including purchases, sales, switches, loans and insurance transactions) considered for their accounts, including potential expenses that may be incurred from a future sale or transaction;

(s) To make full disclosure to each client of all of the compensation to be received by the Defendants with respect to each of the transactions considered for the client's accounts, including potential transaction and referral fees, commissions and expenses that may be incurred from the transaction or from the continued holding of the security or insurance contract or from a future sale or transaction;

(t) To advise each client with respect to the availability of alternative investment and insurance choices which the Defendants could not offer to him;

(u) To ensure that all advice provided to each client was comprehensible to the client considering the client's education, experience and training and to take such steps as necessary to ensure all contracts, forms and documents were understood by the Clients;

(v) To disclose all conflicts of interests and to ensure that client interests were paramount in all circumstances of conflict;

(w) In the case of the Firm, to develop a policies and procedures manual which outlines the following:

(i) The requirement that investment advisors such as Karas deliver risk disclosure documents to clients in accordance with the rules of the MFDA and OSC;

(ii) Appropriate client circumstances for recommending the purchase of securities with borrowed funds;

(iii) Information required to be maintained in the client file including lending documents which should be consistent with KYC information on file for the client;

(iv) Procedures for the identification and review of leveraged trades by the Firm as required by the MFDA; and,

(v) Procedures for making appropriate arrangements between investment advisors like Karas and lenders to ensure the proper recording and supervision of leveraging recommendations.

(x) In the case of the Firm, to comply with their duty of care and with industry regulations and standards and to warn Clients, should Karas stray from such standards. This duty included the duty to conduct audits pursuant to the Firm's regulatory duties.

64. The duty of care owed by the Defendants to the Class Members was in all cases fiduciary in nature.

Breach of Duty

65. The Defendants breached this duty of care to the Class Members in that:

(a) They failed to ensure that each investment recommendation to a client was suitable to the client's individual circumstances;

(b) They failed to ensure that a licensed financial advisor made every buy, hold and sell recommendation to a client;

(c) They participated in schemes to generate compensation for their own benefit in conflict with prudent financial practices, without regard to their Clients interests and without appropriate disclosure of their conflicts of interest;

(d) They caused their Clients to borrow money and to buy, sell and switch mutual funds for the purpose of generating compensation, a process called "churning";

(e) They caused their Clients to take unnecessary risks with respect to the loans, mutual funds and insurance contracts and failed to properly disclose such risks to their Clients and record such risks on KYC forms;

(f) They failed to use due diligence to determine and keep up to date their Clients actual circumstances on their KYC forms;

(g) They failed to ensure each recommendation for their Clients accounts were suitable to their Clients actual KYC circumstances;

(h) They failed to use due diligence with respect to each of the securities considered for purchase, holding or sale for the accounts of their Clients;

(i) They failed to explain to their Clients the risks of the portfolio as a whole and of each of the securities considered and each leverage loan recommended for their accounts.

(j) They failed to make full disclosure of all of the risks associated with the Leveraging Scheme;

(k) They failed to make full disclosure with respect to each of the expenses incurred by their Clients and the impact of these expenses on their Clients investments;

(l) They failed to properly disclose the compensation they earned from their Clients business, and the conflicts relating to such compensation;

(m) Karas failed to adhere to the standards of the voluntary licensing organizations to which he belonged and to which he was committed to adhere;

(n) They recommended and sold unsuitable and unaffordable life insurance policies;

(o) They failed to comply with the rules and regulations of the MFDA and OSC as set out at paragraphs **54-62**; and,

(p) In the case of the Firm:

(i) It failed to warn the Clients they were taking excessive risk with respect to both the amount of debt they took on for the purpose of investment and the nature of the investments purchased for the accounts;

(ii) It failed to make disclosure to the Clients of the risks associated with the Leveraging Scheme;

(iii) It failed to develop policies and procedures to address the issues related to borrowing for the purchase of securities by the Clients;

(iv) It failed to abide by, monitor, or enforce any policies and procedures that were developed to address the issues related to the borrowing for the purchase of securities by the Clients;

(v) It failed to advise the Clients that it had instructed the termination of the use of the stop-loss mechanism they relied upon;

(vi) It failed to supervise the services provided by Karas to the Clients;

(vii) It failed to ensure that its Clients investments and leveraged loans were suitable;

(viii) It provided incentives to Karas to increase the risk taken by Clients by rewarding Karas on the basis of AUM without regard to the associated risk to the Clients;

(ix) It failed to warn the Clients of improper actions with respect to their accounts including, but not limited to, the Leveraging Scheme; and,

(x) It represented that Karas was an excellent advisor by rewarding him for generating excessive revenue to the Firm through the Leveraging Scheme.

66. Karas recommended the Leveraging Scheme as an appropriate investment strategy for all of his clients, and because the Firm knew of the practice and profited from it, the Firm owed a heightened duty to supervise Karas to ensure that he strictly complied with the Firm's policies and industry regulations, to ensure that his strategies were suitable for the Clients, to ensure that the Clients appreciated the risks they undertook and to warn Clients of the risks they ran in respect of the Leveraging Scheme. In all respects, the Firm failed.

67. Investia is also liable vicariously, by OSC and MFDA regulation, for the conduct of Karas and the Karas Companies.

Damages

68. The Class Members damages, which were caused by the Defendants' misconduct and breaches of duties, as described above (in particular at paragraphs 49 and 65), that the Class Members at all times relied upon the Defendants to fulfill, include:

- the loss of the value of money invested through the Leveraging Scheme;
- liability of debts incurred in furtherance of the Leveraging Scheme;
- the cost of debt servicing and debt penalties resulting from the Leveraging Scheme;
- the cost of fees and insurance premiums incurred as part of the Leveraging Scheme; and,
- the loss of value to RRSP investments through their premature conversion to RRIFs.

69. As a result of the Defendants' said misconduct, the Plaintiffs have suffered and continue to suffer serious psychological injures and pain and suffering including loss of reputation.

70. As a result of the Defendants' misconduct the Plaintiffs have suffered and continue to suffer expenses and special damages, including extensive financial and other pecuniary losses, of a nature and amount to be particularized prior to trial.

71. The Defendants earned undisclosed compensation (together, the "Revenues") at the expense of the Plaintiffs, including:

(a) Fees for the sale of mutual funds,

(b) Fees for arranging the various loans,

(c) Fees, called "trailers", paid by mutual fund managers to advisors on a quarterly basis, and

(d) Premiums from the sale of insurance.

72. The earning and receipt of the Revenues occurred by reason of breach of duty, and the Defendants' earning of such Revenues was made at the expense of Plaintiffs, either directly as paid by the Plaintiffs, or indirectly as paid by lenders

73. The Plaintiffs have suffered a detriment as set out in paragraphs **68-70** and the Defendants have obtained a benefit without juristic reason.

74. The Plaintiffs plead in the alternative to their claim for damages that they are entitled to "waive the tort" claim in negligence and instead elect to claim payment of the revenues generated by the Defendants.

75. The conduct of Investia merits aggravated damages in that its direction to Karas and MCB to discontinue use of the stop-loss mechanism, constituted a direction to breach contractual commitments with Clients as well as an acknowledgement of a history of regulatory breach, which they permitted to persist despite actual knowledge that such breach would lead to widespread loss on the part of Clients. Further, Investia permitted Karas to police himself despite Investia's being charged with such responsibility to safeguard the interests of Clients and being aware of Karas' conflict of interest, as described above.

76. In the alternative, the conduct of Investia as described herein merits punitive damages in that it constituted high-handed, malicious, arbitrary, and highly reprehensible misconduct that departs to a marked degree from ordinary standards of decent behaviour on the part of financial intermediaries.

77. The Plaintiffs propose that the trial of this action take place in Barrie, Ontario.

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Court File No. 10-0690

ONTARIO

SUPERIOR COURT OF JUSTICE

Proceeding Commenced at Barrie

AMENDED STATEMENT OF CLAIM

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