SUPREME COURT OF NOVA SCOTIA
Citation: ***National Bank Financial Ltd. v. Potter***, 2013 NSSC 248

Date: 2013-08-07
Docket: Hfx 174294 (Debt Action)
Hfx 206439 (Main Action)
Hfx 208293 (Barthe Action)
Hfx 246337 (National Bank/Weir Action)
Hfx 216059 (Wadden/BMO Action)
Registry: Halifax

Between:

National Bank Financial Ltd.

Plaintiff/
Defendant by Counterclaim in Hfx. No. 174294

-and-

Daniel Frederick Potter, Gramm & Company Incorporated, Starr's Point Capital Incorporated, 2532230 Nova Scotia Limited, 3020828 Nova Scotia Limited, Ronald D. Richter, Solutioninc Limited, John Francis Sullivan, Linda Fay Sullivan, Calvin W. Wadden, Craig Anthony Dunham. Douglas George Rudolph, Gerard B. McInnis, Janine M. McInnis, Lowell R. Weir, Blackwood Holdings Incorporated, and Staffing Strategists International Inc.

Defendants/
Plaintiffs by Counterclaim in Hfx. No. 174294

-and-

Daniel Potter, Starr's Point Capital Incorporated, Fiona Imrie, Gramm & Company Incorporated, 2532230 Nova Scotia Limited, 3020828 Nova Scotia Limited, Ronald Richter, Donald Snow, Meg Research.com Limited, 3027748 Nova Scotia Limited, Calvin Wadden, Raymond Courtney, Bernard Schelew, Blois Colpitts, Stewart McKelvey Stirling Scales, Bruce Clarke, 2317540 Nova Scotia Limited, Knowledge House Inc., The Estate of the Late Michael Barthe, represented by his Executrix Barbara Barthe, Lutz Ristow, Derek Banks and Plastics Maritime Ltd.

Third Parties in Hfx. No. 174294

And Between:

Calvin Wadden, 3019620 Nova Scotia Limited and
Andrea Wadden

Plaintiffs in Hfx. No. 216059

-and-

BMO Nesbitt Burns

Defendant in Hfx. No. 216059

Judge: The Honourable Justice Gregory M. Warner

Heard: February 13th to April 17th, 2012, at Halifax, Nova Scotia

Final Written Submissions: December 21st, 2012

Counsel: James Hodgson, David Coles QC and Robert Blair, for NBFL and National Bank of Canada

W. Dale Dunlop, and Sean MacDonald, for Calvin Wadden, Andrea Wadden, 3019620 Nova Scotia Limited, the Estate of Michael Barthe, Lowell Weir, Carol McLaughlin-Weir, Blackwood Holdings Inc., and Craig Dunham

Linda Fuerst, for BMO Nesbitt Burns

BY THE COURT:

A.1 Introduction

[1] There are no winners in this story. The events give a black eye to the Canadian public securities industry.

[2] Knowledge House Inc., a publicly-traded technology company, collapsed in August 2001 and closed in September. Eighteen months earlier its share value appeared to be $110,000,000. The events leading to the collapse epitomize the concern expressed by David Dodge, a former Governor of the Bank of Canada, about Canada's international reputation as the 'Wild West' of financial markets.

[3] Along the way from penny stock to 'tech darling' to collapse, the entrepreneur behind the rise and fall, who took control of KHI in late 1998, immediately appeared to exponentially grow its size and sales, and, on paper, its value, by the purchase of three private technology companies in exchange for shares of KHI. While the company had sales, it never had real income, a viable business plan or secure financing.

[4] With the help of other insiders, including some of those who had sold their companies to KHI for shares, a lawyer, and Bruce Clarke, a stock broker employed by NBFL, the President of KHI, kept KHI afloat until August 2001 by manipulative and artificial trading in KHI shares, while attempting to create a viable business and secure financing, deter existing shareholders from selling their shares, and entice wealthy individuals and institutions to invest.

[5] The primary instrument of the artificial and manipulative trading in KHI shares was Bruce Clarke. The failure of NBFL to supervise Bruce Clarke facilitated that trading in a manner that was contrary to statutory and industry regulations, and NBFL's own rules.

[6] Only NBFL/NBC, BMO Nesbitt Burns, one insider and three "outsiders" were still parties to this litigation by the start of the trial. In this decision, claims of the three "outsiders" against NBFL are affirmed, the claims of the insider against NBFL and BMO are denied and NBFL's third party claim against the insider partially affirmed.

A.2 Brief History of KHI

[7] Knowledge House Inc. ("KHI") was incorporated as Knowledge Publishing House Limited in Nova Scotia in 1984. Its controlling shareholder, president and chief executive officer was Dr. Bernard Schelew. It provided computer-based programs and software in the field of medical and pharmaceutical education. In 1988, it was listed on the Montreal Exchange and continued thereafter for 11 years as a publically traded penny stock with annual sales under $700,000.00.

[8] Daniel F. Potter ("Potter"), a lawyer by training, described himself since 1991 as a "technology information and education entrepreneur." He founded "ITI Institute," a post-graduate IT education institution in 1984. From 1991 to 1998, he was chair and CEO of ITI Education Corporation, its parent corporation. In 1998, Torstar Corporation invested 37 million dollars in ITI Education and became the major shareholder (39%). Potter gained a reputation for success with the rapid growth and the sale of ITI to a reputable national corporation.

[9] Potter became a director of KHI in 1985. When he ceased as CEO and chair of ITI in 1998, he became actively involved in KHI and, by early 1999, he was the chairman, CEO and, with his spouse, the largest shareholder. Through an aggressive acquisition program, Potter immediately caused KHI to embark in a new direction as an internet and IT-based education services business.

[10] To add to KHI's small pharma-education software business, KHI acquired over a six-month period in early 1999 three rapidly growing private technology businesses:

i) in February 1999, "Silicon Island" and "Centre for Distance Education Limited". The former provided a computer and telecommunication infrastructure to host online education programs; the latter provided direct experience in distance education. As consideration for the acquisition of these two businesses, KHI issued to the principals, Don Snow and Dr. Ken MacLeod, 1.6 million KHI shares and hired them as senior executives.

ii) in June 1999, Micronet Information Systems Limited. Micronet, founded in 1994, was in the business of selling computer hardware and software programs. It was particularly successful in the provision of services to schools. At the time of acquisition, it had just been the successful bidder in a multimillion dollar, multi year tender to provide computers and IT support services to the Nova Scotia public school system. As consideration for the acquisition of this enterprise, KHI issued to its principals, Calvin Wadden and Raymond Courtney, 2.2 million KHI shares and hired them as senior executives.

iii) in July 1999, Innovative Systems Limited. Innovative was Atlantic Canada's authorized reseller of Apple products and, like Micronet, had a rapidly growing business as supplier of Apple computers and IT support services to the public through four retail outlets, and to the Nova Scotia public school system. As consideration for the acquisition of its business, KHI issued to its principals, Craig Dunham and Steven Wilsack, 300,000 KHI shares, and contracts to continue running Innovative.

[11] In rapid succession, KHI entered into partnerships with some of its major suppliers, most notably, IBM Canada Ltd.

[12] Through the activities of the three acquisitions, KHI's revenues grew from $813,000.00 for the twelve months ending February 28, 1999, to 15 million dollars (on a consolidated basis) for the ten months ending December 31, 1999, and 39 million dollars for the year 2000.

[13] In 1999, KHI lost 2.7 million dollars (23 cents per share) and in 2000, 6.5 million dollars (46 cents per share).

[14] In December 1999, KHI moved its public stock listing from the Montreal Exchange to the Toronto Stock Exchange. From partial trading records of KHI on the ME and after December 6, 1999 on the TSE, it appears that the trading activity, inclusive of block trades arranged by KHI insiders, crosses and other transactions that I conclude were the result of manipulation by KHI insiders and Bruce Clarke, was as follows:

1996	753,000 trades in the price range of $0.09 to $0.20
1997	2.7 million trades in the range of $0.09 cents to $1.00
1998	2.9 million trades in the range of $0.50 to $2.00
January to June 1999	2.1 million trades in the range of $1.80 to $4.00
July to December 1999	Records were not before the Court except for the period December 6 to 31, 1999, when the price rose from $4.05 to $6.25
2000	5.2 million trades in the range of $5.50 to a peak price on March 29, 2000 of $9.85
January to July 2001	1.1 million trades in the range of $4.25 to $6.25
from mid-August until the end of the month	the price dropped to 4.5 cents per share

[15] Based on the trading price, the shareholders' equity in KHI fell from 111.9 million dollars on March 29, 2000, to about 2.8 million dollars when it closed its doors on September 13, 2001.

A.3 Brief History of Litigation

[16] The history of this litigation can be read in many reported decisions, in particular *National Bank Financial Ltd v Potter*, 2008 NSCA 92, and *National Bank Financial Ltd v Potter*, 2011 NSSC 407.

[17] In a decision of the Nova Scotia Court Appeal, upholding the refusal of NBFL's motion for leave to amend its pleadings to delete claims of wrongdoing against its broker, Bruce Clarke, Cromwell JA (as he then was) briefly summarized the history as follows:

> [7] The parties are involved in complex litigation concerning the collapse of Knowledge House Inc. (KHI) in August of 2001. NBFL started a number of actions against clients and former clients for unpaid margin debt arising from this collapse. Some of the defendants defended these claims by alleging that they had been the victims of a conspiracy involving NBFL's employee, Bruce Clarke, and others to manipulate KHI share prices.
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> [8] NBFL responded by pleading two main allegations. First, it defended the conspiracy claims by denying there was any conspiracy and any vicarious liability for Mr. Clarke's actions. Second, in what is now known as the main action, NBFL issued a statement of claim against Messrs Potter, Clarke, Colpitts, his law firm and others alleging that they conspired to manipulate the price fo KHI shares and that the conspiracy resulted in a fraud being committed against NBFL.
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> [9] With respect to Mr. Clarke's alleged involvement, NBFL alleged that he acted on his own behalf and as the agent for an insider group of shareholders to conduct elements of the scheme, including trading in KHI shares in his numbered company account, his RRSP and other accounts in order to maintain the public market price of the shares, placing and carrying out orders of the other alleged conspirators, monitoring KHI's order book and trading activity on the TSE, maintaining buy orders for KHI shares in the TSE order book, soliciting NBFL clients to purchase shares of KHI and discouraging those clients from selling KHI shares.
>
> [10] NBFL maintained in sworn testimony that, before making these allegations, it had thoroughly investigated the matter and concluded that it "was never an issue [that]... we were going to sue Bruce Clarke .... We believed that we had more than sufficient evidence to name every person [including Mr. Clarke] in that claim ..." (AB 2828 - 2830).
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> [11] Following the issuance of NBFL's statement of claim in the main action, several of the respondents started actions against NBFL in which they incorporated by reference, NBFL's allegations of conspiracy. In its various defences, NBFL, among other things, denied the conspiracy.

[18] By 2008, there were more than 54 groups of parties named in 11 actions under case management. At the commencement of trial on February 13, 2012, five actions involving six groups of parties remained.

[19] The remaining defendants in NBFL's Debt Action (174294) are Calvin Wadden, Craig Dunham, Lowell Weir and Weir's corporation Blackwood Holdings Incorporated. NBFL sued for unpaid margin debt arising from the collapse of KHI. The defendants counterclaimed against NBFL for the actions of Bruce Clarke. NBFL third-partied, among others, Calvin Wadden and Michel Barthe for any liability it may have in respect of the counterclaims.

[20] The only remaining defendant in NBFL's Main Action (206439), against KHI insiders for conspiring to manipulate the price of KHI shares resulting in a fraud against NBFL, is Calvin Wadden.

[21] In the Barthe Action (208293) commenced by Michael Barthe and Lutz Ristow against NBFL for its failure to supervise Clarke and the wrongdoing of Clarke as alleged by NBFL in the Main Action, the only remaining plaintiff is the Estate of Michael Barthe. In its pleadings, NBFL denied liability and claimed that Barthe was part of the stock manipulation scheme. NBFL third-partied Wadden in respect of any liability to Barthe.

[22] In the Wadden Action (216059), Calvin Wadden, Andrea Wadden and a numbered company controlled by Calvin Wadden, sued BMO Nesbitt Burns alleging that its brokers were part of the stock manipulation scheme, and that BMO's handling of their accounts between March and August 2000 was negligent and in breach of its contractual obligations to the plaintiffs. BMO denied liability.

[23] In the NBC/Weir Action (246337), National Bank of Canada sued Lowell Weir and Carol McLaughlin-Weir on a promissory note given by the defendants to the Bank to secure a March 2003 "loan". The Weirs claim that the money was actually an advance on NBFL's intended settlement of Weirs' claims against NBFL and that NBFL represented it would complete after it had recovered from the other responsible parties in NBFL's litigation. The Weirs defended and counterclaimed against NBC, based on NBC's responsibility for NBFL and the conduct of Clarke.

A.4 The Trial

[24] The trial commenced on February 13, 2012. It ended much earlier than scheduled, on April 17, 2012. The Dunlop Clients called eight witnesses, BMO, one short witness, and NBFL/NBC, no witnesses.

[25] The order for presentation of evidence was determined in a pretrial written decision (2011 NSSC 407).

[26] Three groups of parties remain:

i) The Dunlop Clients (all represented by lawyer W. Dale Dunlop) - Calvin Wadden ("Wadden"), Andrea Wadden ("Ms. Wadden") and their numbered company 3019620 Nova Scotia Limited, Craig Dunham ("Dunham"), Lowell Weir ("Weir"), Blackwood Holdings Incorporated (the Weir company) ("Blackwood"), Carol McLaughlin-Weir ("McLaughlin-Weir") and the Estate of Michael Barthe ("Barthe"). These clients' interests are not identical.

ii) NBFL, and its parent, National Bank of Canada ("NBC").

iii) BMO Nesbitt Burns Inc. ("BMO") (only in respect of the Wadden Action).

[27] While the claims in the five remaining actions were, by agreement, heard together, BMO and the Dunlop Clients agreed, that the claims in the Wadden Action (216059) are more limited in substance, time line and events, than the claims between the Dunlop Clients and NBFL/NBC.

[28] It was agreed by all parties that some evidence was admissible only in the Wadden Action, some admissible only in the four actions involving NBFL and NBC, and some admissible in all five actions. Consequently, counsel for BMO did not attend at trial for all of the evidence.

[29] The evidence admitted in the Wadden Action consists of:

i) documentary evidence contained in Joint Exhibit Books tendered by agreement of BMO Nesbitt Burns and the Waddens, and identified as such, subject to the conditions of admissibility set out in the indexes to these joint exhibits, and other exhibits tendered by agreement;

ii) the oral evidence of Ms. Wadden, Brian MacLellan Q.C. ("MacLellan"), Harold Greenwood ("Greenwood"), Derek Banks ("Banks"), Wadden and Robert Lowe ("Lowe"); and

iii) other exhibits tendered through or referred to by these witnesses in their oral evidence.

[30] BMO and the Waddens specifically agreed that, despite the pleadings, no claim was being pursued by the Waddens of involvement by BMO or any of its employees or agents in the allegations of wrongful manipulation of the share price of KHI shares.

[31] The evidence admitted in the four actions between Dunlop Clients and NBFL / NBC, consists of:

i) documentary evidence contained in Joint Exhibit Books tendered by agreement between the Dunlop Clients and NBFL / NBC, subject to the agreed upon conditions of admissibility set out in the indexes, and other exhibits tendered by agreement;

ii) the oral evidence of Andrea Wadden, Brian MacLellan, Harold Greenwood, Calvin Wadden, Bruce Clarke, Derek Banks, Craig Dunham, Lowell Weir and Carol McLaughlin-Weir;

iii) other exhibits tendered through or referred to by these witnesses in their oral evidence;

iv) the settlement agreement between NBFL and a securities regulator, admitted pursuant to a decision of this Court reported as 2012 NSSC 76; and

v) excerpts from the discovery examinations of Richard Rousseau, Barbara Barthe and Lutz Ristow as well as from the written responses to Interrogatories of Barbara Barthe and Lutz

Ristow.

B Submissions: NBFL and Dunlop Clients

B.1 NBFL/NBC Submissions

[32] NBFL and NBC sued on margin accounts for liquidated sums. There is no real contest that, subject to counterclaims and set offs, debts were incurred in the amounts claimed in respect of the margin accounts. Dunham owed $353,021.96; Weir owed $60,177.68; Blackwood owed $10,403.74 and Wadden owed $1,086,072.00.

[33] The Weirs acknowledge execution of the promissory note with NBC and the receipt of $100,000.00. NBFL presented no evidence, other than the note itself, to establish a debt. The Weir evidence (the only evidence on the point) is that the amount was, by agreement, an advance on NBFL's settlement of the Weirs' claims against NBFL (Weir and Blackwood). The money was advanced as a loan (without interest), because NBFL was in the process of suing others from whom it intended to seek some recovery. NBFL wanted others to share in payment of the Weirs' losses. The promissory note was executed at a request of NBFL to cover any bank audit inquiry about the advance. NBFL claims payment of $100,000.00 plus prejudgment interest, less the amount of any award (if any) of damages against NBFL.

[34] The counterclaims of the Dunlop Clients are premised on the wrongful acts of Clarke and NBFL's failure to supervise him. They allege fraud, negligence, and breach of contract. They allege NBFL is liable for its own actions and non-actions, and is vicariously liable for the wrongdoing of Clarke.

[35] For the first time in this litigation, in its post trial brief, NBFL admitted that it failed to adequately supervise Clarke. It admitted that it was under a duty to review the activity of Clarke's "540" account, an account of 2317540 Nova Scotia Limited, a corporation owned and controlled by Bruce Clarke, a broker employed at NBFL's Halifax office. The numbered company ("540") opened a margin account with NBFL that was designated by NBFL as a "pro" account because it was controlled by one of its brokers, a designation that mandated extra supervision by NBFL management. The effect of this admission is that, if Clarke is found to have acted unlawfully; that is, fraudulently, negligently or in breach of his contractual obligations to the Dunlop Clients or to any of them in connection with the 540 account, NBFL is liable to those Dunlop Clients for Clarke's action both on the basis of NBFL's own negligence and breach of contract, and on the basis of vicarious liability for the acts of Clarke who, it is not contested, was acting throughout in his capacity as broker employed by NBFL.

[36] In a nut shell, NBFL's submission is that the shareholders' equity in KHI, which at one point appeared to exceed 100 million dollars, based on the market price of its shares, disappeared in August 2001 because KHI was not properly funded and ran out of operating capital before the e-learning projects it was developing became marketable. The timing of its fall coincided with the receivership of ITI. In effect, the Dunlop Clients did not lose the value of their investments in KHI

by reason of NBFL's margin calls in August 2001 or by reason of any wrongdoing of Clarke.

[37] Alternatively, NBFL submits that the Dunlop Clients have failed to prove that the "market making" carried out by Clarke was unlawful or, if it was unlawful, that it caused the losses claimed by the Dunlop Clients.

[38] Finally, NBFL submits that if the Court finds that Clarke's activities at the relevant times were unlawful and constituted illegal market making, Wadden and the late Michael Barthe, two of the four remaining Dunlop Clients, were aware of and participated in the illegal market making and are jointly liable with NBFL for any liability of NBFL to any of the other Dunlop Clients.

[39] NBFL submits that KHI's existence was based on Potter's earlier success in developing and selling another e-learning technology corporation - ITI Education Corporation, to Torstar Corporation in 1998. KHI, which was new to the e-learning technology business, had real risks and unlimited prospects. One of its risks was whether it could raise sufficient capital to execute its business plan. Its gross revenues soared with the acquisition of existing technology companies, such as Wadden's Micronet, and its contract to supply e-learning technology services and hardware to the Nova Scotia school system, as well as its partnership with corporations like IBM Canada and other reputable national institutions.

[40] Early in 2001, KHI's revenue dried up at the same time as its new e-learning programs were taking longer to develop and KHI's banker was reducing its line of credit. In short, KHI collapsed because it ran out of cash. Between August 14 and 16, KHI shares were still selling in the range of $5.10 per share. On August 16, 2001, Torstar announced that it was writing off its investment in ITI and appointing a receiver. It had been Potter's reputation for success in ITI that had fuelled shareholder excitement in KHI. The Torstar announcement precipitated, says NBFL, the dramatic fall in KHI's share price to $4.10 on August 17 and $0.72 by August 22. It was only then that NBFL called in the margin debt owed by many KHI shareholders to it on the security of the KHI shares.

Craig Dunham

[41] Craig Dunham and Steven Wilsack sold their Apple-based technology business, Innovative, to KHI on July 30, 1999, in exchange for 300,000 KHI shares (150,000 each) and contracts to continue running Innovative for KHI. Dunham had access to these shares at the rate of 30,000 shares per year (the rest were held in escrow).

[42] NBFL says that Dunham was an educated and experienced business man. He had experience with brokerage accounts, although NBFL does not suggest he was an experienced investor.

[43] The agreement to sell Innovative to KHI was subject to certain adjustments. In the spring of 2000, Dunham was required to pay KHI $141,347.50 as his share of those adjustments. At the same time he was constructing a new residence, which he expected to build with the proceeds of the sale of KHI shares. He had no money to do either. Gerard McInnis, KHI's controller, outlined in a February 4, 2000 e-mail, a plan whereby KHI would advance to Durham and his partner some of the

shares held in escrow that "will be placed in trust with Bruce Clark[e] who will sell into the market on an orderly basis", with the proceeds being paid to KHI to discharge the debt owed by Dunham and his partner. Dunham did not know Clarke at this time, but contacted him to carry out the McInnis plan. All communication between Clarke and Dunham from February 2000 to August 2001, except one meeting and two or three phone calls, was by e-mail.

[44] In March 2000, Dunham opened a margin account with Clarke for the purpose of selling 30,000 KHI shares that KHI was advancing to Dunham's margin account to pay KHI the $141,347.50 that he owed KHI, with the balance of the sale proceeds to be withdrawn by Dunham. In April 2000, KHI closed the Innovative Retail Store in New Minas that was run by Dunham. Rather than move to Halifax, Dunham resigned from KHI. Shortly thereafter he received from KHI another 30,000 KHI shares and in the summer of 2000 his remaining 90,000 KHI shares. These shares were transferred by KHI into Dunham's margin account with Clarke at NBFL.

[45] NBFL submits that Dunham understood the effect of opening a margin account and that he was borrowing money in a margin account from NBFL for personal and other purposes.

[46] NBFL acknowledges that on three occasions Dunham gave Clarke specific instructions to sell KHI stocks and that Clarke ignored these instructions. Following these instructions would have produced about $52,000.00 for Dunham's account. Dunham received the records of purchases made into his account and sales made from his account. He knew that Clarke was not following his instructions but he made no complaint either directly to Clarke or to NBFL.

[47] NBFL submits, in short, that Dunham ratified Clarke's failure to follow instructions. NBFL acknowledges that Dunham asked for advice from Clarke in diversifying his account, but at the same time notes that Dunham often gave instructions to Clarke with regards to purchases of technology stocks in respect of which he relied upon his own research.

[48] NBFL's submissions do not directly address Dunham's communications with Clarke to the effect that Dunham was told he should sell KHI shares and diversify his holdings or Dunham's evidence that he was relying upon Clarke to give him advice about, and carry out, the diversification of his portfolio.

[49] Finally, NBFL submits that Dunham failed to prove that Clarke's failure to follow instructions caused Dunham's claimed losses. Other than the three specific instructions to sell, which were not followed, Dunham received the benefit of the advances made on the margin account that he held with NBFL.

[50] NBFL identifies and refutes Dunham's claimed losses:

i) With respect to Dunham's claim that he lost the value of the 120,000 KHI shares (worth $6.95 as of June 20, 2000), NBFL argues that no <u>specific</u> instruction to sell all shares was ever given.

ii) With respect to Dunham's claim for lost income at the rate of $40,000.00 per year from

June 30, 2000 (when his resignation from KHI became effective) to December 31, 2002, NBFL notes that Dunham did not seek alternative employment. Furthermore, there was no evidence relating his conduct, in resigning from KHI and not working, to anything that NBFL or Clarke did or failed to do.

iii) With regards to Dunham's claim for recovery of the interest charged on his margin account in the amount of $34,418.00, NBFL again notes that other than in respect of purchases that Dunham had instructed Clarke to make from the proceeds of the sale of KHI shares (about $52,000.00) all advances on the margin account were for Dunham's personal benefits.

iv) With respect to Dunham's claim for losses of $123,000.00 (which NBFL quantified as $113,000.00) that Dunham spent developing a website called "Fantasy Stock," which he says he lost because he ran out of money he would have had if his portfolio had been diversified, NBFL notes that Dunham spent $83,000.00 before he mortgaged his house, and only spent $30,000.00 on the project after he mortgaged his house for $350,000.00. In effect, neither NBFL's nor Clarke's wrongdoing caused this loss.

v) With respect to Dunham's claim for certain legal and professional expenses, NBFL notes that there was no evidence relating these fees to NBFL's or Clarke's activities.

vi) With regards to the claim for interest paid on credit cards and on the mortgage on his home (about $177,000.00), NBFL says there is no factual basis connecting these interest claims to NBFL or Clarke's conduct; rather, what sparse evidence exists suggests they were incurred in respect of Dunham's efforts to re-enter the computer business through his corporation, Highbury Traders.

Lowell Weir, Blackwood Holdings and Carol McLaughlin-Weir

[51] With respect to the claim by NBFL on the Promissory Note, NBC acknowledges that if the Court determines that NBFL is liable in damages to Weir and Blackwood, then the amount owing under the Promissory Note should be deducted from those damages.

[52] In respect of the claim by Weir, NBFL states that Weir only had two personal investments in Knowledge House shares, 5,000 KHI shares in his LIRA account and, on February 28, 2001, 28,175 shares received on conversion of his Knowledge House Limited Partnership Unit for $145,000.00 into shares. NBFL states that Clarke and NBFL were not involved in Weir's decision to purchase the Limited Partnership Unit, which Weir stated he did on the advice of his lawyer Blois Colpitts ("Colpitts").

[53] On January 19, 2001, Weir e-mailed Clarke telling him he was not comfortable with the investments that he, his wife and members of his family had in KHI and if the per-share price fell below $5.00 he was to liquidate and sell all their KHI shares. NBFL submits that Weir was a sophisticated investor who watched the price of KHI shares carefully, and whose first complaint to

NBFL about its failure to sell when the price fell below $5.00 came after the price of KHI shares had collapsed. In effect, Weir had ratified Clarke's conduct in not liquidating the Weir family holdings in KHI shares.

[54] NBFL also notes that the 28,175 KHI shares (converted from a KHI Partnership Unit) were placed in a margin account. There were restrictions on the sale of those KHI shares and Weir used the margin debt to buy a car for his wife and to make RRSP contributions of about $19,000.00.

[55] NBFL states that if the Court finds that NBFL is liable for Clarke's failure to liquidate the Weir's 31,175 shares as instructed, the loss to Weir was $165,875.00, which should be offset against the margin debt of $60,177.00 owed by Weir to NBFL and the $100,000.00 advance by NBC on the Promissory Note.

[56] NBFL notes that Blackwood opened a margin account with NBFL in 1998 and began borrowing on this margin account to purchase various securities. Blackwood held 10,000 KHI shares in its NBFL margin account as of March 1999 but sold 2,000 in December 2000 and 1,000 in March 2001. NBFL states that if this Court finds NBFL liable for Clarke's failure to liquidate Blackwood's remaining KHI shares pursuant to the January 19, 2001, e-mail (other than the 1,000 on March 28, 2001), that the loss to Blackwood was $35,000.00 less the margin debt of $10,404.00 used by Blackwood Holdings to purchase other investments.

[57] NBFL notes that Carol McLaughlin-Weir testified that she met with Clarke in May 2001 to discuss her children's account and give instructions to liquidate KHI shares. She testified that Clarke advised against selling shares because KHI was going to sign another government contract and the price would rise to $8.00 per share. As a result, she revoked her instructions to liquidate KHI shares. On this basis, NBFL says it is not liable for Clarke's failure to liquidate the shares pursuant to the January 19, 2001 e-mail.

[58] Weir had testified that on September 4, 2001, he entered into an agreement with NBFL through its Halifax branch manager, with respect to NBFL's margin call against Blackwood account, to the effect that no action would be taken on the Weir's accounts while he was away in Europe on business. NBFL says the evidence shows that Weir returned from Europe on September 14, 2001. NBFL did not act on its margin call and liquidate shares in the Blackwood account until September 19, 2001, five days after Weir returned from Europe; it says that it did not breach the agreement.

[59] NBFL denied that it was vindictive and mean in the manner in which it exercised its right to liquidate the Blackwood shares to satisfy the margin debt. NBFL further states that the Weirs had many opportunities to mitigate their loss and failed to do so. NBFL further submits that the damages claimed by the Weirs in respect of the liquidation of Weirs' shares in Enervision, a publically traded company that Weir ran and had a significant investment in, was not caused by the manner in which NBFL liquidated Blackwood's shares pursuant to its margin call.

Barthe Estate

[60] NBFL states that Barthe was a wealthy, successful and sophisticated businessman worth hundreds of millions of dollars. He purchased a residential property and made other investments in Guysborough County, Nova Scotia. Some of these investments were made jointly with Lutz Ristow ("Ristow").

[61] Barthe became interested in investing in KHI as a result of discussions with his neighbour in Nova Scotia, Jack Sullivan ("Sullivan"), an officer of KHI, who introduced him to Potter. Barthe conducted his own due diligence on KHI. He arranged for an analysis by an accountant who had formerly been employed by his German corporation, and by his Nova Scotia accountant, and by his lawyers.

[62] He was first approached by Sullivan in 1999. In May 2000, he received a proposal to make a substantial purchase of new shares from KHI's treasury, which proposal he did not act on. On August 3, 2000, he entered into an agreement negotiated directly with Potter and Colpitts to purchase 250,000 KHI shares on the open market at $6.80 per share, for a total of 1.7 million dollars. He received an option to purchase additional shares from Potter for $4.00 per share. At this time, he did not have an NBFL account.

[63] He contacted Colpitts, KHI's counsel and a Director, to ask how the agreement should be implemented. He was advised by Colpitts to contact Clarke and open an account at NBFL. Barthe transferred 1.7 million dollars to an account opened in his name on August 28, 2000. Clarke executed Barthe's instructions to purchase the shares, sent Barthe confirmation slips for each transaction, and regular updates on his progress. Clarke was able to purchase shares for less than the $6.80 price in the agreement. For the 1.7 million dollars, Clarke purchased 259,000 shares for Barthe and paid himself commissions of $13,848.00.

[64] After August 30, no other transactions took place on Barthe's NBFL account before the KHI share price collapsed.

[65] NBFL notes that there were no restrictions as to whom the sellers to Barthe would be, and that, by reason of the August 3rd agreement between Barthe and Potter, it was clear that Barthe was agreeing to purchase KHI shares from KHI insiders.

[66] In October 2000, Barthe and Ristow decided to jointly purchase KHI shares from KHI's treasury. The purchase was negotiated directly with Potter and Sullivan. The terms of the private placement, set out in the Subscription Agreement, were approved by the Toronto Stock Exchange. Barthe confirmed an understanding that there were no assurances that the money that he and Ristow were injecting into KHI would enable it to continue its operations. The Subscription called for four payments of $812,500.00 directly to KHI's Royal Bank account. The shares were being held in escrow for six months after the payments were made. Ristow made the first two payments, the third and the fourth payments were due from Barthe on May 15 and August 15, 2001. These payments were not made through Barthe's NBFL account.

[67] NBFL submits that Barthe and Ristow were offered directorships with KHI and had

information available to them that was available to directors. Ristow was formally appointed to the KHI board on June 29, 2001; he and Barthe were treated as if they were Directors from December 2000. They were well aware of the cash flow problems of KHI at the time of the subscription agreement of November 15, 2000.

[68] NBFL submits that there was no evidence that Barthe would not have invested in KHI had he knew that its share price was supported by the activities of Clarke and/or others. On the contrary, when Barthe was advised that the stock was being supported, he did not complain. He even expressed a willingness to help, except for the fact that he did not at that time have the financial ability to do so.

[69] NBFL submits that not only did Barthe not complain that he had been deceived or express concern when he was asked to support KHI's share price, neither he nor Ristow complained that they would not have bought KHI shares if they had known the price had been supported.

[70] NBFL argues that because at one point Barthe was offered the position as an alternative Director in the event Ristow could not attend Director's Meetings and because he had access to insiders' information that he is liable to NBFL for any wrongdoing arising from stock manipulation by Clarke.

Calvin Wadden

[71] NBFL states that Calvin Wadden is a well-educated, experienced businessman with extensive employment history in banking and finance. He and Raymond Courtney ("Courtney") founded Micronet. Micronet purchased 100,000 KHI shares in December 1998 (later split between Wadden and Courtney, with Wadden placing his 50,000 shares in 3019620 Nova Scotia Limited, which opened an investment account with his best friend and broker Eric Richards at Financial Concepts Group ("FCG")).

[72] On June 30, 1999, Wadden and Courtney sold Micronet to KHI for 2.2 million shares (1.1 million each) and jobs as executives at KHI. The shares were held in escrow to be released over five years. The shares were valued at that time at $2.65 each.

[73] In 1999, Wadden and Ms. Wadden invested further into KHI:

i They purchased 111,000 additional KHI shares on the market;

ii He purchased a partnership unit for $150,000, converted in January 2001 into 28,125 KHI shares; and,

iii She purchased 62,500 shares as part of a private placement to raise operating capital for KHI.

[74] In January 2000, the Waddens acquired 100,000 common shares from Don Snow ("Snow"),

who was selling the bulk of his shares to Charles Keating ("Keating"), to assist in Snow monetizing his investment into KHI, and an additional 20,000 shares on the market.

[75] Other than the shares obtained from the sale of Micronet, most of these purchases were financed by margin debt, issued on the Wadden's accounts at FCG. As of February 28, 2000, 80% of the Wadden family assets were in KHI equity, offset by 1.144 million dollars in margin debt to FCG and $300,000 in margin debt at CIBC. At this time, FCG determined it would advance no further margin debt to the Waddens.

[76] In March 2000 Wadden's best friend Eric Richards ("Richards") left FCG for BMO; the Waddens decided to move their accounts with him.

[77] In the meantime, Wadden opened a margin account through Clarke at NBFL to access cash. In a March 7, 2000, e-mail, Wadden asked Clarke to advance $300,000.00 to CIBC to pay off a loan secured by 220,000 KHI shares and to cause those shares to be transferred to his new margin account at NBFL. After opening this account, Wadden had made cash withdrawals of $607,500.00 by June 20 and purchased other shares on margin.

[78] NBFL notes that in Wadden's direct evidence, at a time when KHI was entering into larger deals and KHI's share price was progressing from $6.00 to $7.00, Potter advised his partners that KHI's 'orderly market account' was offside and Potter asked each of the major partners to put up 100,000 shares to maintain the orderly market account onside. Wadden immediately agreed. Wadden attended at Richard's office to obtain the only share certificate available to him. It was for 220,000 KHI shares. He then returned to KHI's office to give it to Potter. Potter asked him to sign the back of it and give it to his executive secretary; he did. He acknowledged advising the executive secretary that Potter said to send this certificate down to Clarke at NBFL.

[79] Calvin Wadden's lawyer Brian MacLellan Q.C., who was retained by Wadden on July 17, 2000, testified that Wadden described the account to him as "mother's account", "box account" and "orderly market account" and understood that he was being asked to "support the market" with his unencumbered stock in KHI.

[80] NBFL submits that Wadden knew that the account was to be used to buy and sell KHI shares. NBFL fails to note that Wadden was unaware that the shares were being deposited in Clarke's 540 account. At trial, Clarke testified that the 540 account was his own account. It was not an account of KHI nor operated by Clarke on behalf of KHI. NBFL's submission is that it is irrelevant to Wadden's consent to participate in the "box account" that he did not know that the account was in Clarke's 540 account name, but it is important that Wadden understood (from the time of the transfer of the CIBC held shares to his NBFL account) that shares pledged as security for an account could not be returned unless the debt was paid off or he posted substitute security.

[81] NBFL makes the point that while in Florida with his partner Courtney, immediately after arranging for his 220,000 KHI share certificate to be delivered to NBFL, Courtney told Wadden that he was not prepared to go along with Potter's request that 100,000 of his KHI shares be placed in

the "box account" but would agree to put $100,000.00 into the account. There is no evidence that, after returning from Florida until May 2000, Wadden asked Potter whether the other partners had contributed, or asked Potter for the return of the extra 120,000 shares he deposited into the account.

[82] Making the point that Wadden did not object to, or alternatively, did understand that he was advancing 220,000 KHI shares as security for an orderly market account, NBFL notes a May 11, 2000, e-mail in which Wadden stated that he would like to take Potter and Courtney up on their offer to "equally support the orderly market account with Bruce and that freeing up the 120,000 [shares] will definitely make things easier for me".

[83] On June 7, 2000, 120,000 KHI shares were deposited to Wadden's NBFL account from one of Potter's numbered company's account. Immediately thereafter Wadden made cash withdrawals from this NBFL margin account, which margin debt totalled 1.026 million dollars as of June 30, 2000.

[84] NBFL characterizes the relationship between Wadden and Potter as becoming strained after June 30, 2000, when Potter failed to find a buyer for 250,000 of Wadden's KHI shares. This relates to Wadden's evidence that at the time he agreed to purchase 100,000 of Snow's shares in January 2000 (to assist in Snow monetizing his investment in KHI), Potter had promised to find him a buyer for 250,000 of his shares. Shortly after June 30, Wadden took steps to sell KHI shares from his account at BMO Nesbitt Burns. BMO would not allow him to do so. This led to Wadden's retainer of a lawyer, MacLellan, on July 17, 2000.

[85] On July 20, 2000, MacLellan sent a fax to Clarke requesting that Wadden's 100,000 shares in the orderly market account be returned. He stated that this was a follow-up to Wadden's own request of July 14 and July 17. Clarke was unable to return the 100,000 shares as they were held as security for margin loans owing to NBFL by the 540 account. After Wadden resolved his disputes with Potter in late August 2000, Ken MacLeod ("MacLeod"), another shareholder and director, caused 100,000 KHI shares to be deposited into Wadden's account.

[86] On August 31, Wadden signed a letter acknowledging the return of all 220,000 KHI shares that had been deposited in the 540 account. On September 5, Wadden took delivery of the 100,000 KHI share certificate. On October 4, he deposited the certificate into an account he opened at TD Waterhouse and immediately, on the security of that share certificate, made cash withdrawals from that margin account to purchase other shares.

[87] NBFL suggests that there is no legal consequence to Wadden's complaint that the 220,000 shares he deposited into the 540 account on or about March 7 were not the same 220,000 shares that were returned to him on June 7 and August 29, 2000. It submits this claim has no relevance to whether Wadden in fact consented on March 7 to the deposit of the 220,000 KHI shares in the orderly market account operated by Clarke (through the 540 account).

[88] With respect to Wadden's claim that NBFL refused his sell instructions, it submits that the only evidence of a refusal to sell was a request to sell 3,000 shares at $6.50 made on the afternoon

of August 11, 2000.

[89] NBFL notes that, in respect of the July 19, 2000, telephone conference call between Wadden and Clarke from the boardroom of MacLellan's office, MacLellan and Greenwood were present. Wadden has no record to back up his claim that he gave Clarke instructions to sell KHI shares, and neither MacLellan nor Greenwood has notes or confirm that Wadden instructed Clarke to sell KHI shares during that phone call. Follow up correspondence between MacLellan and Clarke did not refer to any instructions to sell.

[90] NBFL acknowledges that on August 11, when Wadden instructed Clarke to sell 3,000 shares at $6.50, Clarke called Colpitts and asked if the trade could be done. On the basis of that phone call, Clarke refused to execute the sale instructions. NBFL notes that if Clarke was in breach of his obligation to Wadden with respect to that instruction, the proceeds would have been $19,500.00 less commission. This loss could have been mitigated if Wadden had sold the shares after he resolved his issues with Potter. There were no instructions that would have prevented him from doing so after August 2000.

[91] In pre-trial submissions, Wadden complains that NBFL breached its obligations to him with respect to the 28,125 KHI shares Wadden received on January 4, 2001, in exchange for his limited partnership unit.

[92] NBFL notes that, at the trial, Wadden testified that in late December he received a call from Potter in which Potter spoke about market pressure on KHI share prices. Potter advised Wadden that he was using the shares he was receiving as a result of the conversion of the limited partnership unit as security to purchase more KHI shares. Potter asked if Wadden would do the same and Wadden agreed.

[93] On January 4, 2001, Wadden e-mailed Colpitts as follows: "Please forward my share certificate for the converted LP to Bruce as soon as possible. I will be depositing to my margin account and will be able to help Bruce take 20,000 shares of KHI out of the market if we can do this today." In fact, the share certificate was deposited to Wadden's NBFL account and Wadden did purchase 20,000 shares on margin.

[94] NBFL says the only evidence before the Court is that Wadden consented to the transaction. If these market support transactions were lawful, on the basis that the purchases were made in the expectation that the shares would increase in value, then Wadden has no claim against NBFL. Alternatively, NBFL argues that if the Court finds that the motive behind the transactions was to manipulate the market illegally, then this is further evidence of Wadden's willing participation in the manipulation and he is liable on the third party claims by NBFL with respect to any liability it may have to Dunham, Weir, Blackwood and the Barthe estate.

[95] Finally, NBFL argues, in respect of its claim against Wadden in the Main Action, and in its Third Party claims, that if the Court finds that the market support was an unlawful activity, Wadden participated. NBFL submits that Wadden's participation, or at least his knowledge, as a KHI insider,

commenced by February 3, 2000, when he received a copy of an e-mail from KHI's controller to Clarke referring to shares that were going to become available "to support the market as needed or fill any orders you have pending" following which Wadden had discussions with Clarke. As previously noted, Wadden further deposited 220,000 shares into an account at NBFL with Clarke on March 7, 2000, in order to help support the orderly market account. On March 9, 2000, Wadden sent an e-mail from Florida to Clarke entitled "Trading Account", in which it is clear that Wadden understands his participation involved an orderly market account and efforts to find purchasers for KHI shares.

[96] In a telling e-mail from Potter to Wadden (copied to Colpitts) dated November 19, 2000, Potter advised that he was hoping to close a 3.25 million-dollar treasury issue to "our German friends [Barthe and Ristow] in the next day or two at a price of $6.50". Potter added: "If the market is driven down in advance of this issue, it is quite likely that the investors will not close". Potter urged caution with respect to one of Wadden's friend's pressure to find a buyer for his shares.

[97] In the fall of 2000, prior to this e-mail, Wadden had been a consistent seller of KHI shares but immediately after this e-mail he purchased 8,300 KHI shares. In December 2000 and January 2001, Wadden and his wife purchased approximately 55,000 KHI shares on margin. As noted earlier, Wadden agreed that the 28,125 KHI shares he received on conversion of the limited partnership unit would be used to support the market and, in fact, purchased 20,000 KHI shares in January to take pressure off the retail market for KHI shares.

[98] This is consistent with two e-mails from Potter to Wadden at this time. In one dated January 1, 2001, Potter advised:

> ... there is significant selling pressure on KHI on December 29 ... if you can be of any assistance helping to find some buyers, that would be great. We have been and will continue to be working on this in the coming days but I am concerned that the selling may exceed any support bids we can engender in the next few days.

[99] Again, on January 31, 2001, Potter e-mailed Wadden: "From the look of the market it seems we have had success in stabilizing the market and I hope that we can look forward to better days ahead." Wadden referred in cross-examination to "we" as including all of the founding partners, directors, Colpitts and Clarke.

[100] In February the founding shareholders met at Colpitts' office and pledged to support the market price of KHI shares. Wadden was placed in charged and paid a monthly fee for performing that function. E-mails expand on how Wadden undertook this job. In a February 9 e-mail to Potter he stated:

> I have been speaking with Ray, Blois and Ken throughout the day and they have been in supporting the market. Ray and I would really like to get the stock to $5.45 and try to solicit more support from the group going forward. If we can get to $5.45-$5.50, I would like to see each of us put 5,000 shares

> into the support side and try to inch up towards $6.00 to $6.50 until we get some positive news on the street.

[101] On February 13, Wadden sent an e-mail to Steven Wilsack (Craig Dunham's partner), in which he tells Wilsack that he told "the whole table" that Wilsack was not in fact selling but rather buying and it helped him to convince others to support the KHI share price and put the stock in the $6.00 plus range. He added: "I can honestly say I is the reason the damn stock ain't at $4.00. I am working for the shareholders."

[102] In February Wadden took a trading course and subscribed to a stock watch program and was spending a considerable amount of time in front of his computer "tracking and trading stocks". Wadden's market support activities included more than KHI. It showed a clear knowledge and understanding by Wadden that he was trying to assist insiders in more than one company to keep the market price of publicly traded stocks elevated.

[103] NBFL makes the point that after March 2, 2001, Clarke's 540 account did not trade in KHI shares. NBFL does not mention that the obvious reason for this was that Clarke had run out of margin in that account to continue the efforts that had persisted since at least early March 2000, when Wadden had deposited his 220,000 KHI share certificate and Potter had placed $100,000.00 cash into the 540 account.

[104] NBFL argues that if providing market support was unlawful, clearly Wadden was involved.

B.2 Dunlop Clients Submissions

[105] The Dunlop Clients submit that the KHI share price collapsed from above $5.00 to nil in less than two months, not because of a cataclysmic event threatening KHI. KHI had just announced an anticipated, substantial contract with the Province of Nova Scotia.

[106] On the contrary, KHI collapsed because NBFL and BMO were increasing their purchases of KHI shares, while other brokers were reducing their ownership. Weir was rebuffed by NBFL when he noticed this and asked Clarke that shares owned by him and his family be sold if the price touched $5.00.

[107] When the shares fell below $5.00, counsel submits that margin calls by NBFL occurred. These margin calls occurred before the collapse of KHI price and the margin call was the cause of the collapse.

[108] A second cause of the losses to the Dunlop Clients was Clarke's misdeed respecting the trading in KHI shares, including through his 540 account, which NBFL failed to stop. Counsel argues that the evidence shows that Clarke used the 540 account to borrow millions of dollars from NBFL on margin, using money and shares provided by KHI insiders to support the KHI share price. This is the substance of NBFL's allegations in the action it commenced known as the Main Action.

When the various non-NBFL parties attempted to have NBFL's Main Action dismissed or, alternatively, the other actions in which NBFL pleaded that Clarke was innocent of any wrongdoing, NBFL advanced its own research and investigations to support its allegation against Clarke and other alleged KHI's insiders of misdeeds respecting the trading in KHI's shares.

[109] In this respect, counsel refers the court to affidavits filed in NBFL's pretrial motions, the Brian Awad Memoranda, and the tendered discovery evidence of Mr. Rousseau, an Executive Vice-President at NBFL in charge of its network of brokers.

[110] The Court notes that some of the "evidence" relied upon by counsel in his submissions was not tendered at trial and is not before the Court as evidence.

[111] Dunlop submits that NBFL's pretrial machinations and shifting theories of the misconduct of Clarke and others negate NBFL's pretrial submissions to the effect that there was no wrongdoing by anyone, including NBFL. He contrasts this with his clients' consistent allegation that Clarke acted wrongly in several respects, which he summarized in his post-trial submissions in nine categories: (1) conflict of interest; (2) breach of confidence; (3) failure to inform or warn; (4) unsuitability; (5) over concentration in one stock; (6) improper financial dealings with clients to the detriment of others; (7) misrepresentation; (8) failure to follow and execute sale orders; and (9) unauthorized trading.

[112] Counsel submits that NBFL itself was negligent in failing to properly supervise Clarke and, in addition, is vicariously liable for Clarke's wrongdoing. All of Clarke's nine misdeeds are relevant to Dunham's claim; all but the fifth (over concentration in one stock) are relevant to the Weirs' claim; all but the fourth, fifth and ninth apply to the Waddens' claims; and that four of those misdeeds, the first, third, sixth and seventh, apply to the Barthe claims.

[113] Counsel relies upon the IDAC settlement agreement with NBFL for the truth of its contents, and the evidence of Clarke, to prove Clarke's wrongdoing and NBFL's negligence and breach of contract in not supervising him.

[114] Dunlop notes that, at the end of the plaintiffs' case, despite filing a lengthy list of proposed witnesses, NBFL called no witnesses. The Dunlop Clients submit that the Court should draw an adverse inference against NBFL because they called no evidence and because of Clarke's evidence with respect to his handling of the 540 account, his dealings with KHI insiders and with NBFL's management, as well as the nine specific claims of wrongdoing by Clarke. In this regard, counsel refers the Court to the **Law of Evidence**, **3rd Edition**, by Alan Bryant *et al*, para 6.449, *Falkenham Backhoe Services v Nova Scotia,* 2008 NSCA 38, para 48; *Constitution Insurance v Coombe*, 1993 CanLII 5461 (ONSC), in which, at para 15, the Court cites Chief Justice Gale in *Northern Wood Preserves v Hall Corporation Shipping* (1973), 2 OR (2d) 335.

[115] In all of their claims, the Dunlop Clients plead negligence and breach of contract. In the Dunham claim, counsel claims also that NBFL breached its fiduciary duty. Rousseau's discovery evidence established NBFL's heightened duty to supervise Clarke and the 540 account. NBFL

produced no evidence that it supervised Clarke.

[116] The Court has already noted that, after Dunlop's post-trial submissions were made, and for the first time, NBFL acknowledges, in its post-trial submission, that it failed to supervise Clarke in respect of the 540 account. NBFL did continue to claim that Clarke did nothing wrong.

B.2.1 The Wadden Claim

[117] Dunlop submits that the wisdom of Wadden's sale of his interest in Micronet for shares in KHI is not in issue. As of March 7, 2000, 440,000 of Wadden's freely tradable KHI shares were "lodged with NBFL" and had a market value of about three million dollars.

[118] How 220,000 ended up in Clarke's 540 account is important. Wadden says that he agreed to assign these shares, at the request of Potter, as security for a KHI account that was "off side" and needed for a short term support. The existence of the KHI account at NBFL was not a secret. Wadden knew nothing of the 540 account that his shares actually went into.

[119] While admitting that Clarke in fact used Wadden's shares as security to buy and sell KHI shares through the 540 account, Wadden relies first on NBFL's position that Clarke did nothing wrong with the 540 account. Alternatively, if Clarke acted wrongly, that Wadden, whose credibility was not impeached, had no personal contact with Wadden about how his 220,000 KHI shares were to be used; did not know that these shares were being used to support Clarke's 540 account; refused to sign a document drafted by Clarke acknowledging a loan of shares to Clarke and hired a lawyer to get the share certificates for these shares back. All of this establishes that Wadden did not voluntarily loan his shares to a broker's private account.

[120] Counsel argues that Clarke acknowledged taking instructions from Colpitts and sometimes from Potter on whether to execute sell instructions from Wadden. When Wadden put NBFL on notice of Clarke's wrongful use of his KHI shares, NBFL accepted absurd explanations from Clarke rather than check the conduct of Clarke in respect of his 540 account.

[121] Counsel argues that only then did Wadden "capitulate" and get some of his KHI shares released. What counsel meant by "capitulation" is not explained in his submission.

[122] Wadden claims the value of 440,000 shares lodged with NBFL in March 2000, when their market value was $6.80 per share, or $2,992,000.00. Because NBFL argued that neither it nor Clarke did anything wrong, it cannot be argued that the market value for KHI shares was not the price on the TSX of $6.80 per share.

[123] Absent any evidence that Wadden should not have been allowed to trade freely in these 440,000 shares, but was, in fact, prevented from doing so, and absent evidence that the TSX stock price for KHI shares was not their real market value, the Court should not speculate that the market would not have absorbed the 440,000 KHI shares for less than $6.80 per share.

[124] Counsel cites *Hodgkinson v Simms* [1994], 3 SCR 377 for the proposed remedy for Wadden's capital losses.

[125] Between Clarke's wrongful taking of instructions from Colpitts to prevent the sale of the 220,000 KHI shares in Wadden's margin account and the wrongful taking of the 220,000 KHI shares in the 540 account, counsel argues that Wadden is entitled to an award for damages equal to the value of the TSX public stock price for those shares in March 2000.

B.2.2 The Dunham Claim

[126] Craig Dunham's claim against NBFL is for negligence and breach of contract as well as breach of a fiduciary duty. The claim is based both on NBFL's own breaches of duty, and vicariously for Clarke's wrongdoing.

[127] Dunham claims that Clarke, and therefore NBFL, breached a fiduciary duty to Dunham. On the totality of the evidence, it is clear that Dunham placed himself totally in Clarke's hand in a manner described in *Varcoe v Sterling*, 1992 Carswell Ont 1156 (ONSC) at paras 86 and 90.

[128] Clarke knew that Dunham was a novice investor who relied totally on Clarke's skill and knowledge to guide him and to diversify his account. Instead, Clarke acted contrary to Dunham's bests interests in an intentional manner such that Dunham not only lost the value of the 150,000 KHI shares placed in the care of Clarke but incurred significant consequential losses.

[129] Counsel argues that nothing in Clarke's conduct could reasonably have warned Dunham that Clarke was in a conflict of interest position and acting deceitfully toward him.

[130] Counsel cites *Kerr v Baranow*, 2011 SCC 10, at paras 70 and 71, respecting the flexibility given to courts to grant equitable remedies. Dunham submits that Clarke ruined his life.

[131] Dunham claims that the market value of his KHI shares, as they came in Clarke's "orbit of influence" was $800,000.00. But for Clarke's deceit and failure to disclose his interest in the 540 account as well as his relationship and activities on behalf of KHI's insiders, Dunham would not have placed his remaining KHI shares with Clarke and would have been able to liquidate them.

[132] Counsel argues that, in a 2005 decision removing NBFL's then counsel in this litigation, Justice Scanlan had admonished NBFL to settle with the truly innocent investors. Counsel characterized Dunham as, without doubt, one of the clearly innocent investors with whom NBFL should have settled. Dunham's submission was made before counsel was aware of NBFL's post-trial acknowledgment that it had failed to properly supervise Clarke and his 540 account. Counsel argues that NBFL should be liable for substantial punitive damages as described in *Whiten v Pilot Insurance*, 2002 SCC 18, for the manner in which it strenuously contested Dunham's claim for several years, during which time Dunham lost his home, his credit, his business and his business reputation.

[133] NBFL knew it had no defence to Dunham's claim, even while it advanced conflicting pleadings and claims, including claims first that Clarke and others had conspired to cause the loss to NBFL and its client and, on the other hand, that neither NBFL nor Clarke had done anything wrong.

[134] Counsel stresses that NBFL's tactics and stratagems protracted the litigation, not unlike the treatment of the Blackburns in *Blackburn v Midland Walwyn*, 2003 Carswell Ont 684. In that case, the Court tripled the costs award. Counsel notes that unlike the *Blackburn* case, the NBFL managers in this case have not been otherwise punished.

[135] NBFL's reduction in its margin rates for KHI shares were affected suddenly and without regard to the consequences on its clients, including those like Dunham. This irresponsible conduct merits denunciation.

[136] Failure to honour its contractual duty of good faith is distinct from breach of contract, (*Whiten*, para 79), and forms an additional basis for punitive damages. Counsel refers to para 112 to 125 in *Whiten* for the measure of punitive damages.

[137] Applying these principles, counsel submits a substantial award of punitive damages is warranted because NBFL was so oppressive and affected so many over so extensive a period.

B.2.3 The Barthe Claim

[138] The late Michael "Ben" Barthe, made two investments in KHI after Clarke commenced his machinations with the KHI stock in March of 2000.

[139] First, Clarke contracted to purchase KHI shares for Barthe, who was referred to Clarke by a KHI insider Colpitts. Counsel submits that Clarke had a concomitant duty when he contracted to act for Barthe in the purchase of shares to disclose his involvement in the 540 account as well as his work for KHI's insiders in maintaining the KHI share price. He did not disclose these to Barthe.

[140] NBFL's defence that Barthe was not induced by Clarke to buy KHI stock and that the purchase of KHI shares was not an unsuitable investment for Barthe, is not an answer to the "but for" test. Counsel submits that if Clarke had told Barthe what he knew, Barthe would not have purchased the KHI shares. Compounding Clarke's non-disclosure was Clarke's continued manipulation of the market price of the KHI shares, while Barthe purchased shares.

[141] Barthe invested $3,315,000.00 in KHI shares. He lost the value of his shares, except a minimal recovery, and the interest on those shares.

B.2.4 The Weir/Blackwood Claims

[142] Lowell Weir gave explicit instructions to Clarke to sell all KHI shares held by him, his company and his family in January 2001 in the event that the KHI share price dipped below $5.00.

It did and Clarke did not sell his shares.

[143] When Weir received a share certificate for 28,125 KHI shares on the redemption of his KHI limited partnership unit, these instructions required Clarke to liquidate those shares.

[144] The loss to Blackwood by Clarke's failure to sell at $5.00 its KHI shares was $42,000.00. The loss to Weir himself was $26,250.00 for the shares he held as of January 2001 and $157,500.00 for the 28,125 shares received into his NBFL account shortly afterwards. Weir claimed these sums plus interest.

[145] The claim by Weir and Blackwood is based upon Weir's clear instruction to sell, which instruction was not carried out. Weir says it was not complied with because of Clarke's illegal trading both through the 540 account and otherwise. NBFL was negligent and in breach of its contract with Weir to failing to properly supervise Clarke.

[146] Weir claims that when KHI collapsed and NBFL knew, or should have become aware, of Clarke's illegal activities, Weir and Blackwood should have had their claims for losses quickly resolved. Instead, it has taken over 10 years.

[147] Weir's credible evidence with respect to his communications with the head office of KHI was uncontradicted by any evidence at trial. It was to the effect that NBFL's head office agreed to compensate him once NBFL had recovered from those others that it had sued for their part in the wrongdoing, that the $100,000.00 was an advance on an eventual settlement of Weir's claims against NBFL, (which advance was documented as a loan for audit purposes only), and NBFL employees made subsequent threats to teach him a lesson, and generally acted in bad faith. All these things merit punitive damages against NBFL. The effect upon Weir and his family from the liquidation of his margin account with NBFL, and that of Blackwood, which included the forced sale of his shares in Helical (formerly Enervision), created collateral damages in the form of the loss to him of his interest in Helical and his business reputation. These merit punitive damages.

B.3 Supplementary Submissions - December 2012

[148] At trial, the Dunlop Clients sought to have the Court receive undisclosed evidence that he considered relevant and important to the proceeding. NBFL objected vehemently to any disclosure of the subject matter of the evidence Dunlop proposed to tender. Counsel advised that NBFL would seek a mistrial if the subject matter was disclosed. The request by Dunlop was made both before the Dunlop Clients had closed their case and at the end of the hearing of all parties' evidence.

[149] Specifically Dunlop requested that his clients be entitled to reopen the case if the evidence he was prevented from introducing at the trial could, at a later date, be introduced. The Court advised that it would entertain a motion to receive new evidence within a reasonable time after

the close of the evidence, if that occurred before the court had rendered a decision.

[150] On December 4, 2012, a Settlement Agreement entered into in June 2005 between NBFL and its Halifax manager Eric Hicks on the one part and the Nova Scotia Security Commission, the Investment Dealers Association of Canada, and Market Regulation Services Inc., respecting the conduct of NBFL and Hicks in relation to its dealings with the subject matter of this litigation, and which, by order of the Commission, had been kept secret until approved by the Commission, was approved by the Nova Scotia Securities Commission and made public.

[151] On December 5, 2012, Dunlop wrote to the Court requesting that I grant his request to reopen the case if the evidence that was referred to as the "big secret" became public before I rendered my decision. He asked that the court reconvene so the NBFL / Hicks settlement agreement could be tendered as evidence and submissions be advanced as to the consequences of the agreement.

[152] On December 6, Hodgson, counsel for NBFL, replied in part:

> For purposes of the Record, NBFL objects to the admissibility into evidence of the Agreement. However, this is an issue which has already been fully argued and upon which your Lordship has already ruled. Accordingly, (unless your Lordship has reconsidered his Decision) NBFL accepts that the Agreement will be entered into evidence as an Exhibit.
>
> All counsel are in your Lordship's hands. However, given the time of the year, I am wondering if it might be more expeditious for Mr. Dunlop to simply provide written argument for "the consequences" of the Settlement Agreement ... and for NBFL to provide its written Submissions ...

[153] Hodgson's reference to my decision, was my decision respecting the admissibility of a Settlement Agreement between NBFL and IDAC, arising from failure by NBFL to supervise other branch operations during the time frame of the alleged wrongdoing by Clarke, which decision is reported as 2012 NSSC 76. On December 6, Dunlop replied to Hodgson's letter thanking him ". . . for agreeing that the Settlement Agreements be entered as exhibits for your consideration . . . [and] I am in agreement with Mr. Hodgson's suggestion that we deal with the matter by way of written argument rather than try to schedule a court appearance."

[154] On the same day, the Court wrote to counsel, in part as follows: ". . . based on counsel's agreement on procedure, I am prepared to accept written submissions as to the "consequences" (your words) or use that may be made of the settlement agreement." I set time lines for written submissions. Dunlop's submissions were received on December 14, and NBFL's on December 21, 2012.

B.3.1 Dunlop Clients Supplementary Submissions

[155] In June 2005, NBFL and its Halifax manager Eric Hicks, entered into a Settlement Agreement with the Nova Scotia Securities Commission Staff, the Investment Dealers Association of Canada ("IDAC") and Market Regulations Services Inc. ("MRS"), with an attached Statement of Allegations. The Agreement dealt with the subject matter of this litigation and the prior publicly-available settlement agreement between the Commission and Clarke. The Agreement provided that

it was to remain confidential until approved by the Commission.

[156] The NBFL/Hicks/NSSC/IDAC/MRS Settlement Agreement was approved by the Commission and became public on December 4, 2012. The Dunlop Clients tendered the Settlement Agreement, the decision of the Nova Scotia Securities Commission ("Commission") dated December 4, 2012, approving the Settlement Agreement signed June 2005, together with the Nova Scotia Securities Commission decision dated April 17, 2012, amended September 30, 2012, and two decisions of the Nova Scotia Court of Appeal respecting the Settlement Agreement - the Court's decisions of January 31, 2012 (2012 NSCA 12) and September 21, 2012, (2012 NSCA 99).

[157] These decisions discuss the process by which the Settlement Agreement was kept secret for seven years. They explain why the Dunlop Clients were unaware of the Settlement Agreement and agreed facts in the Statement of Allegations until shortly before the joint trial of these proceedings was commenced. The decisions also explain why the Dunlop Clients were prevented from introducing evidence in this litigation of the Settlement Agreement and the agreed Statement of Allegations until after the trial was completed and initial post-trial submissions in this proceeding were made.

[158] They explain why it is appropriate that this Court, not having yet rendered a decision, entertains the request to admit into evidence, and consider, if admitted, the purpose, and how the Settlement Agreement approved by the Commission on December 4, 2012, should impact this proceeding.

[159] In substance, the Agreement provides that NBFL and Hicks agree that the Settlement Agreement was entered into on the basis of the facts contained in the Statement of Allegations of NSSC Staff attached to the Settlement Agreement. The parties to the Agreement agree that the facts and conclusions are for the purpose of the Settlement Agreement only. The agreement on the facts and conclusions in the Statement of Allegations is "without prejudice to [NBFL] in any other proceedings of any kind, including . . . any civil or other proceedings". The Agreement sets out, as mitigating factors, NBFL's full co-operation with the investigation, and the fact that "NBFL has conducted a thorough and rigorous examination of its internal procedures and policies resulting in significant changes to its compliance regime in order to enhance its ability to supervise and to detect compliance violations by its employees in their trading activities." Finally, "this Settlement Agreement and its terms are to be treated as confidential until approved by the Commission and only thereafter if, for any reason whatsoever, [it] is not approved by the Commission."

[160] The agreed Statement of Allegations attached to the Settlement Agreement contains 34 paragraphs that mimic in substance evidence heard orally in this litigation. The December 4, 2012, decision of the Commission summarizes the factual basis admitted to by NBFL as its violations of the *Securities Act*. The Commission summarized the facts as follows:

> 3. ... relates to the Respondents' actions, or lack thereof, in connection with certain activities of Bruce Elliot Clarke, a former employee of NBFL. Mr. Hicks was Mr. Clarke's immediate supervisor at NBFL. Mr. Clarke entered into a settlement agreement with the Commission in 2004 relating to his actions involving Knowledge House Inc. which were a violation of Nova Scotia securities laws and

contrary to the public interest.

...

11. The violations of the Act admitted to by NBFL and Mr. Hicks occurred between 1999 and 2001.

...

17. It is clear that the violations specified in the Statement of Allegations attached to the Settlement Agreement were serious violations. The violations demonstrated, among other, a lack of attention to internal policies, a failure to detect a pattern of manipulative trading, a failure to establish and implement proper internal control procedures, a failure to ensure that the NBFL branch office confirmed with prudent business practices and failure to properly supervise certain staff members. The Respondents have admitted the facts set out in the Statement of Allegations, and acknowledge that during the relevant period they violated Nova Scotia securities laws, and engaged in conduct contrary to the public interest as set out in the Statement of Allegations.

[161] The Statement of Allegations relates to the activities of Clarke, commencing in 1999, as an investor advisor for a number of KHI insiders and entering into an arrangement to act jointly to maintain the market price of KHI shares. Clarke carried this out through several means, including, in particular, trading in the 540 account, with cash and share transfers from KHI insiders and margin debt from NBFL. Deposits of money and shares from KHI insiders into the 540 account, enabled Clarke to buy significant quantities of KHI shares on margin in a manner described in para 33 of the agreed Statement of Allegations, resulting in a pattern of manipulative trading that NBFL failed to detect and prevent.

[162] In their December Supplementary Submissions, the Dunlop Clients appear to accept as given that the Settlement Agreement constitutes acknowledgment of facts in the Statement of Allegations for this litigation, despite para 4 of the Agreement.

[163] Counsel focuses on the non-disclosure by NBFL of the existence of the Settlement Agreement, and the effect on this litigation.

[164] Counsel argues that the Settlement Agreement made in June 2005 was improperly concealed for seven years, contrary to the *Securities Act*, as determined by the Commission in 2012. The *Civil Procedure Rules*, both the old (1972) and the new (2009), require parties to fully disclose the existence of all relevant documents, and to disclose the contents of all relevant documents for which privilege is not expressly and specifically claimed. NBFL never disclosed the existence of the Settlement Agreement, nor claimed non-disclosure of their contents on the basis of privilege.

[165] Demand for disclosure was made by the Dunlop Clients on NBFL. NBFL should have acknowledged its existence and claimed privilege.

[166] The Escrow Agreement that NBFL relied upon to not disclose the existence of the Settlement Agreement had no legal validity, as determined by the Commission, a Supreme Court Justice, and the Nova Scotia Court of Appeal. Any *bona fide* but mistaken belief that NBFL could

legally not disclose the existence of the Agreement ended with those decisions.

[167] NBFL's refusal to disclose the existence of the Agreement, and the admissions contained in the Agreement, including the express acknowledgement of Clarke's manipulative trading in KHI's shares and NBFL's failure to supervise him properly with regards to the activities in his 540 account, both of which is central to this litigation, have had an obvious impact on the claims, and ability of the claimants to pursue a remedy, against NBFL for more than 10 years.

[168] Having hidden the existence of the Settlement Agreement since 2005, NBFL was able to argue conflicting theories as to the wrongdoing of itself, of Clarke and of other parties, for which NBFL had already accepted responsibility. In a decision not to strike NBFL pleadings by Justice Scanlan [2005 NSJ No. 13], Justice Scanlan had written: "Until a Court determines whether there was stock manipulation, NBFL will not know what its rights or liabilities may be . . . NBFL says at this point, and perhaps not until the Court decides what occurred, does NBFL have full knowledge of the factual situation so as to enable it to assert its rights with certainty."

[169] Similarly, in another decision by Justice Scanlan [2005 NSJ No. 186], Justice Scanlan admonished NBFL, whom he noted was blinded by the regulatory investigation, ". . . to not sacrifice 'innocent investors' or use their financial might to crush litigants into submission in a situation in which it may result in an injustice."

[170] Counsel cites several later motions in this litigation where NBFL took a position about the facts contrary to its admissions in the Settlement Agreement with the Commission, IDAC and MRS. All of these Court decisions show a reliance upon NBFL's representation that it did not know the facts and should be permitted to continue with conflicting pleadings with respect to the facts surrounding Clarke, the 540 account, and the use of that account to manipulate KHI shares.

[171] Counsel argues that the concealment of the Settlement Agreement was highly improper. It seeks several remedies arising from the concealment, including striking of NBFL's pleadings, solicitor - client costs to all parties, and exemplary and punitive damages.

[172] Counsel submits that NBFL has been cited for its bad faith in these proceedings previously. This is not its first misconduct. Counsel cites *Church of Scientology of Toronto v Maritime Broadcasting* (1979), 33 NSR (2d) 500 (NSCA), in comparing NBFL's conduct to contempt.

[173] Counsel submits that NBFL's conduct since 2005 amounts to a concerted effort to shield evidence of its wrongdoing from the Court and the Dunlop Clients. For remedies, he refers to *Homer Estate v Eurocopter SA*, 2003 BCCA 229, cited in *Grewal v Nijjer*, 2011 BCCA 505, *Aecon Buildings v Brampton,* 2010 ONCA 898 and *Ameron International v Sable Off shore Energy Ltd et al*, 2011 NSCA 121.

[174] Counsel argues that NBFL's wrongful non-disclosure of the existence of the Settlement Agreement put all parties through seven years of unnecessary litigation, many parties of whom were

not deep pocketed litigant and were those to whom Justice Scanlan referred to in his 2005 decisions.

B.3.2 NBFL's Response to Supplemental Submissions

[175] Counsel for NBFL notes that at the opening of the trial Dunlop raised the issue of the existence of a secret document and his proposed motion to have the document entered as evidence in this proceeding. NBFL vigorously objected to identification of the document or its contents at that time. The Court indicated that it would hear any motion that counsel may bring in order to avoid the threat of a mistrial (raised by NBFL). At the close of the Dunlop Clients' case, Dunlop again sought to introduce evidence respecting the secret document if it became available at a later date. NBFL's counsel consented to Dunlop being permitted to reopen the case so that the issue of whether any additional documents could be admitted into evidence and, if so, on what basis or for what purpose.

[176] The secret document they were speaking about is the Settlement Agreement between NBFL and Eric Hicks, of one part, and the Commission Staff, IDAC and MRS, of the other part. The document became public when approved by the Commission on December 4, 2012.

[177] NBFL objects to the admission of the Settlement Agreement and Commission's Orders approving it. It does so on the basis that the Settlement Agreement states that NBFL's agreement to the facts is without prejudice to it in any civil or other proceedings.

[178] NBFL states in its December 2012 brief that it assumes that this Court's decision during the trial to admit into evidence another Settlement Agreement between NBFL and IDAC (2012 NSSC 76) will dispose this Court to enter into evidence this Settlement Agreement and Commission Orders. On that basis, counsel makes the following additional submissions:

1. The Settlement Agreement does not contain any admission that Clarke manipulated KHI stock. Dunlop's December 2012 submission did not deal with the contents of the Settlement Agreement; rather, it constituted an unwarranted attack on NBFL and its counsel for not revealing the existence of the Settlement Agreement and claims for new relief.

2. Respecting the admissions made by NBFL, it submits that in order to find that Clarke manipulated the KHI share price, the Court must find both that Clarke's trading in the 540 account caused KHI share price to be artificial; that is, different from what would have been based on supply and demand and, additionally, that Clarke intended to cause KHI share price to be artificial.

[179] NBFL states that it did not admit in the Settlement Agreement that Clarke manipulated the share price or that Clarke's trading in the 540 account caused KHI share price to be artificial or that Clarke intended to cause KHI share price to be artificial. NBFL submits that para 33 of the Statement of Allegations attached to the Settlement Agreement reflect what Clarke admitted, which it describes as making purchasers for the insider group and their accounts and through the 540 account, in order to maintain KHI share price within a certain range. What NBFL admitted was that it failed to detect the purchases Clarke made for the insider group in their own accounts and in the

540 account to maintain the KHI share price within a certain range. NBFL admitted nothing more.

[180] NBFL simply admitted that it failed to ensure that the Halifax Branch conformed with prudent business practices and serve its clients adequate as well as failed to properly supervise Clarke and detect Clarke's involvement with the KHI's insiders and the 540 account.

[181] NBFL submits that the admissions in the Settlement Agreement do not establish that NBFL came to a definitive conclusion as to whether Clarke's trading cause KHI's share price to be manipulated or that he intended that to occur. Specifically NBFL did not know, nor was it indicated in Clarke's Settlement Agreement, that Clarke intended to cause KHI's share price to be artificial. NBFL submits that it would require expert analysis of Clarke's trading to establish Clarke's intent.

[182] NBFL states that Dunlop's reference in its brief to a PricewaterhouseCoopers Report and its contents was inappropriate. It was not in evidence in these proceedings. [I agree.]

[183] NBFL's admissions in the Settlement Agreement should not impact this Court's decision for five reasons:

a) The evidence, which is set out in NBFL's post-trial brief, does not support that Clarke's 540 account trading resulted in an artificial price.

b) The evidence, the best evidence being Clarke's eight days of oral evidence at trial, does not support that Clarke intended to cause the price to be artificial.

c) What NBFL admitted to in the Settlement Agreement about the 540 account (the accumulation of KHI shares and the deposits of cash and shares into that account from insiders) was clearly apparent from the documents in evidence at trial. Besides the testimony of Clarke and Wadden, others who conducted transactions with the 540 account, including Potter, Courtney and MacLeod, were known to the Dunlop Clients and could have been called by the Dunlop Clients to testify.

d) NBFL's admissions regarding the failure to supervise the 540 account activity were already admitted in NBFL's post-trial brief.

e) The Dunlop Clients submitted in their post-trial brief that NBFL's failure to supervise the activity in the 540 account was apparently before the trial and in the trial evidence.

[184] NBFL submits that it did not conduct the trial so as to leave the Dunlop Clients to believe it would contest what they say was obvious. Its witness list did not include Hicks, Roby or any other witnesses who could testify as to the supervision by NBFL of the 540 account; furthermore, its pre-trial brief did not address the issue and, at trial, it called no evidence respecting the issue.

[185] NBFL admits in the Settlement Agreement that it failed to monitor Clarke's

communications using his personal e-mail address. This was not one of the nine alleged breaches of NBFL's duty to the Dunlop Clients, enumerated by Dunlop in his post-trial brief. The fact of Clarke's use of his personal e-mail was in evidence at trial. NBFL's e-mail policy and excerpts from its compliance manual were in evidence and admitted. In effect, the Settlement Agreement adds nothing to this issue. Furthermore, there is no evidence that the failure to monitor Clarke's use of his personal e-mail address caused the Dunlop Clients any loss.

[186] NBFL states that it entered the Settlement Agreement with the regulators in good faith. It was a term of the Agreement that it was held in escrow and was not to be put before the Commission until the final disposition of all regulatory proceedings relating to KHI trading activities.

[187] It is not unprecedented for Commission proceedings to be confidential. The proceedings against Wadden and MacLeod, including the allegation that they and others manipulated KHI's share price, were kept confidential, on the motion of their counsel Dunlop, from May 19, 2006 to October 15, 2010. It was only disclosed with Wadden and MacLeod's consent. NBFL argues that the Commission determined that the Escrow Agreement was invalid in April 2012, but, even then, ruled that it remains protected by settlement privilege until approval by the Commission. The Commission dismissed allegations of impropriety against NBFL and the Staff at that time. Its decision was upheld by the Nova Scotia Court of Appeal.

[188] Dunlop's request for an order for immediate disclosure of the Settlement Agreement, and its contents, both in November 2011 and September 2012, was not granted by the Nova Scotia Court of Appeal.

[189] NBFL objects to Dunlop's accusation that it and its counsel acted in bad faith. Counsel states that the allegations involve issues that are beyond the purview of these proceedings. Limited to the purposes of these proceedings, NBFL says that it was not a foregone conclusion that the Settlement Agreement would be approved and, if it had not been, it would have remained confidential forever.

[190] Counsel cites Justice Hood's consideration of the use that could be made of the Clarke Settlement Agreement in *Barthe v NBFL,* 2009 NSSC 305. Possibly in retaliation for Dunlop's allegation against NBFL and its counsel for acting in bad faith (and in contempt of Court), NBFL resurrected its concern, raised earlier in these proceedings (by it and others), that Dunlop may have been in a conflict of interest with respect to the relations of his client's *inter se*. These conflicts were conceded and written consents were obtained to Dunlop acting for them.

[191] NBFL also calls out Dunlop for referring in his December 2012 brief to the contents of privileged settlement conferences in these proceedings with Justice Moir.

[192] Finally, NBFL takes issue with Dunlop's inference that NBFL and the Commission were in cahoots. It states that the "sharing of information" by NBFL was pursuant to investigation orders of the Commission, which compelled NBFL to provide the information.

B.3.3 Analysis - Settlement Agreement

[193] In summary, both the Dunlop Clients' brief and the NBFL brief respecting the admission and use that should be made of the Settlement Agreement with attached admissions of facts made by NBFL in that Agreement, focussed on allegations by each of the other's bad faith.

[194] The Settlement Agreement, including the attached Statement of Allegations is admissible for the same reasons as set out in this Court's decision of February 17, 2012 (2012 NSSC 76) respecting the IDAC/NBFL Settlement Agreement.

[195] However, the Court agrees with many of NBFL's submissions in its December 2012 brief respecting what admissions were made and not made, and what use should be made of them.

[196] As noted in para 183, NBFL submits that its admissions in the Settlement Agreement should not impact this Court's decision for five reasons. I agree with the third, fourth and fifth reasons; that is, the accumulation of KHI shares and the deposits of cash and shares into the 540 account from KHI insiders is clear and apparent from the documents and other evidence at trial. NBFL in its post-trial brief admitted its failure to supervise the 540 account activity. Its failure to supervise the activity in the 540 account was apparent in the trial evidence.

[197] NBFL submits that its admissions in the Settlement Agreement should not impact this Court's decision because the evidence at trial does not support that Clarke's 540 account trading resulted in an artificial price or that Clarke intended to cause the price to be artificial.

[198] I do not rely on NBFL's admissions in the Settlement Agreement, and in particular, paras 12, 27 and 33 of the Statement of Allegations, to conclude that the admissions contained in that Settlement Agreement, with respect to Clarke are true. Commencing in late 1999, certain KHI insiders entered into an arrangement to act jointly to maintain the price of KHI shares. Clarke agreed to assist those insiders in carrying out this arrangement and Clarke made a large number of purchases of KHI shares on margin through the 540 account. The purpose of the trades was to maintain the price of KHI shares within a certain range with the collateral effect of maintaining the value of those shares upon which the amount of margin debt in the accounts of the shareholders was based. Additionally, during the relevant period (from at least March 2000 to July 2001), Clarke entered into a large number of transactions, almost exclusively purchases, for the insiders, both through the 540 account and through the accounts of the insiders, for the purpose of facilitating that arrangement. This arrangement had the effect of supporting the market price for KHI shares on behalf of KHI insiders. This pattern of trading by Clarke and the insiders for whom he acted was a pattern of manipulative trading, contrary to securities regulations and the duty Clarke owed to those clients who invested in KHI shares.

[199] It is an unreasonable interpretation of the Settlement Agreement and the Statement of Allegations, to which NBFL agreed as part of that settlement, to suggest that the arrangement between Clarke and certain KHI insiders was not to act jointly to maintain the price of KHI shares within a certain range. Further, the records of transactions by Clarke, which constituted large

numbers of purchases of KHI shares in the 540 account, and on behalf of KHI insiders, reveal both the intent and effect: facilitating the maintenance of the share price within a certain range in a secretive manner that breached securities laws, exchange rules, and NBFL's own corporate policy, and the common-law relating to contracts, torts and equity. The trial evidence of Clarke, a knowledgeable, experienced professional, whose disbelieved plea of ignorance and innocent intent, is drowned out by his actions as revealed in the documents and trading records tendered at trial.

[200] The volume of transactions carried out by Clarke, both in the 540 account and on behalf of KHI insiders, was substantial. Most of the transactions in the 540 account were purchases and the few sales were for the purpose of facilitating KHI insiders in finding new wealthy investors, and maintaining the share price above a minimal level, while KHI attempted to create a viable business.

[201] The description of Clarke's conduct in the Statement of Allegations at paras 12, 27 and 33 use the word "manipulative" only once; however, the totality of the admission, which adds nothing new to (nor distracts from) the trial evidence upon which I rely, is that Clarke, acting jointly with KHI insiders, traded in significant numbers of KHI shares, both in his own 540 account and as the agent and broker for KHI insiders for the purpose of secretly facilitating market support, to the detriment of those who relied on the open regulated public market. They include those to whom Clarke and NBFL owed a duty of care in contract, tort and equity.

[202] The activities of Clarke in trading KHI shares, viewed in hindsight on the basis of the documentary evidence tendered at trial, do not require expert interpretation to draw the obvious inference of fact. Without Clarke's 540 account trades, and the other trades he facilitated for KHI insiders in their efforts to buy time, while creating a viable business and seeking new investors, had an effect upon the market price for KHI shares that was not known to the public and to Clarke's clients. Clarke's trading activities were not authorized by the laws and regulations governing investment dealers, and NBFL's own policies and procedures. The market support resulting from the joint activities of Clarke and insiders was of such magnitude that it clearly created an artificial price for KHI shares that would not have existed, but for Clarke's activities. How much that artificial price deviated from what otherwise would have been the price - the true market price, was not the subject of any evidence in these proceedings. In the circumstances, it is unlikely that it could have been calculated with any precision.

[203] While there is no presumption that a person intends the natural consequences of his acts, the trier of fact may infer a state of mind, such as intention, from engaging in conduct the natural consequences of which, taken in context of all the evidence, is the certain result. The intent of Clarke is obvious from his actions. His statements of ignorance and innocent intent were not credible, and belie his obvious intent - to use the shares and money given to him to purchase on margin KHI shares in the 540 account, and to facilitate trades among insiders, for the purpose of propping up the KHI share price secretly; in short, to conduct and facilitate manipulative trading in KHI shares.

[204] The Court does not rely upon the Statement of Allegations in the Settlement Agreement. The admissions in the Settlement Agreement are obvious through assessment of the other trial evidence.

[205] The existence of the Settlement Agreement and circumstances by which it was kept secret may be factors relevant to the assessment of punitive damages.

C. Clarke's/NBFL's legal relationship with the Dunlop Clients

C.1 The starting point

[206] The Dunlop Clients' claims against NBFL are based on the relationship between each of them and Clarke - Clarke's alleged wrongful acts (for which NBFL is vicariously liable), and NBFL's failure to properly supervised Clarke and his 540 account.

[207] NBFL does not dispute, and no evidence was tendered to rebut, the evidence that throughout the time relevant to this litigation Clarke acted as a stock broker, employed by and under the control of NBFL at its Halifax branch.

[208] If Clarke breached any of his legal obligations to the Dunlop Clients, it is not disputed by NBFL, and there is no evidence to contradict the conclusion, that NBFL is vicariously liable for Clarke's breaches of his legal duties to the Dunlop Clients.

[209] Separate from vicarious liability, NBFL admits in its post-trial brief, and the Court heard no evidence to the contrary, that it failed to properly supervise Clarke with respect to his dealings in the 540 account. NBFL's original pleadings in the Main Action that Clarke was on "a frolic of his own", thereby negating vicarious liability, was not pursued by NBFL in the evidence or its submissions.

[210] NBFL maintains that the Dunlop Clients failed to establish that Clarke acted in breach of his duties to them.

[211] The starting point for the assessment of Clarke's liability to each of the four Dunlop Clients is an analysis of the legal relationship between Clarke and each of them.

[212] The relationships between Clarke and each of the four Dunlop Clients are not identical.

C.2 The Law Respecting Broker - Client Relationship

[213] The relationship between an investment advisors and their clients is one of agent and principal, but the precise nature of the duties owed by an investment advisor to his or her principal depends on the circumstances. Most investment advisor-client relationships fall in the middle of a spectrum between the investment advisor as a mere "order taker" and the investment advisor as a fiduciary (*Kent v May* (2001), 298 AR 71 (QB) at paras 51 to 53, aff'd (2002), 317 AR 281 (CA)). A fiduciary relationship is not presumed and must be established based on evidence (*Elderkin v Merrill Lynch, Royal Securities Ltd*, (1977), 22 NSR (2d) 218, 1977 CarswellNS 184 at 34; *Hodgkinson v Simms*, [1994] 3 SCR 377, 1994 CarswellBC 438 at paras 44, 135).

[214] At a minimum, investment advisors must follow their client's instructions, subject to refusal for illegality (*LaFlamme v Prudential-Bache Commodities Canada Ltd*., [2000] 1 SCR 638 at 646), abide by the terms of any applicable contractual agreement, and not permit a conflict of interest to arise. Any extension of the investment advisor's duties beyond these bare minimums is a question of fact (*Reed v McDermid St. Lawrence Ltd.* (1990), 52 BCLR (2d) 265, 1990 CarswellBC 291 at para 14 (CA)).

[215] While not every investment advisor-client relationship will rise to the level of a fiduciary one, it is helpful to consider the test for finding a fiduciary relationship in order to place the relationships in question on the relevant spectrum. In *Hunt v TD Securities Inc.* (2002), 229 DLR (4th) 609; 2003 Carswell 3141 at para 40 (ONCA), leave to appeal to the SCC refused 2004 CarswellOnt 1610, the Ontario Court of Appeal interpreted the Supreme Court of Canada's decision in *Hodgkinson* as disclosing five factors to consider when determining whether a fiduciary relationship exists:

i) Vulnerability - the degree of vulnerability of the client that exists due to such things as age or lack of language skills, investment knowledge, education or experience in the stock market.

ii) Trust - the degree of trust and confidence that a client reposes in the advisor and the extent to which the advisor accepts that trust.

iii) Reliance - whether there is a long history of relying on the advisor's judgment and advice and whether the advisor holds him or herself out as having special skills and knowledge upon which the client can rely.

iv) Discretion - the extent to which the advisor has power or discretion over the client's account.

v) Professional Rules or Codes of Conduct - help to establish the duties of the advisor and the standards to which the advisor and the standards to which the advisor will be held.

[216] The fifth factor is a useful starting point, since Professional Rules or Codes of Conduct may inform the relevant standard of care (*Morin v Blais,* [1977] 1 SCR 570; *875121 Ontario Ltd v Nesbitt Burns Inc.* (1999), 50 BLR (2d) 137, 1999 CarswellOnt 3247 at para 86 (Ont Supr Ct J)). For this reason, I reference the relevant sections of National Instrument 31-103, Registration Requirements and Exemptions (NI 31-103).

[217] Even where the *Hunt* factors do not support a full fiduciary relationship, an investment advisor must still know the client (NI 31-103, s. 13.2), an obligation of paramount importance that is met in part, by the client completing a New Client Application form or "Know Your Client" ("KYC") form. These forms provide the investment advisor with some indication of the client's investment knowledge, experience, risk tolerance and objectives (*Abrams v Sprott Securities Ltd* (2001), 13 BLR (3d) 78; 2001 CarswellOnt 547 at para 29; *Parent v Leach*, 2008 CarswellOnt 3217 at para 89; *Varco v Sterling* (1992), 7 OR (3d) 204, 1992 CarswellOnt 1156 at para 101 (Ont Sup

Ct J); *Merit Investment Corp v Mogil*, 1989 CarswellOnt 2708 at para 43 (Ont SC (H Ct J)).

[218] An investment advisor (and his/her firm) also has an obligation to identify and mitigate any existing or potential conflicts of interest (NI 31-103, s. 13.4).

[219] As previously mentioned, applying the factors outlined in *Hunt* and *Hodgkinson*, and translating them into an applicable standard of care, is a fact-based exercise that is not amendable to a rigid formulaic approach. The Court must look at the cumulative effect of all factors together. For example, a client's history of not following the investment advisor's advice may not be an indicator of expertise or a lack of vulnerability that overrides other factors that suggest vulnerability (*Gale* at para 4). Conversely, use of margin investing or other more sophisticated investment approaches, while potentially indicative of expertise in some cases, may not be in other cases where a client shows a long history of reliance on her investment advisor (*Osborne v Harper,* 2005 BCSC 1202). In each case, the Court must balance the various factors to ascertain the applicable duties owed by an investment advisor to his client.

[220] The authors, **Joseph Groia** and **Pamela Hardie**, in *Securities Litigation and Enforcement*. Toronto: Thomson Carswell, 2007. [Grioa], at pp. 168 to 169, write:

> The relationship of broker to a client is based primarily in contract as principal and agent. This relationship changes as trust, confidence and reliance are placed by the client in the broker, such that it may also give rise to a higher duty of care or a fiduciary duty.
>
> In *Kent v May*, the Court described that relationship as follows:
>
>> Essentially, therefore, one should consider the relationship to be a spectrum. At one end is a relationship of full trust and advice. The broker effectively makes all the decisions because of the great reliance and trust reposed in him or her by the client ...
>>
>> This is exacerbated where the account is discretionary, such that the broker has authority to make trades with the client's consent or even knowledge ... Obviously there is a fiduciary relationship at this end of the spectrum ... At the other end is a relationship where the broker is merely an "order-taker" for the client, the client does not rely on any advice from the broker, and the broker has no discretion ... Relationships at this end of the spectrum lack the elements of a fiduciary relationship ... Most cases fall somewhere in the middle.

[221] The authors **John A. Campion** and **Diana W. Dimmer** in *Professional Liability in Canada*, 4th ed. Toronto: Carswell, 1994 (looseleaf to 2011) c. 10; c. VII [Campion], at p. 10-1, describe the relationship as follows:

> Providers of financial advice are providing financial planning information and other investment services in exchange for consideration, be it a flat fee or a commission. While this has the appearance of a commercial relationship, it is a relationship which demands a high level of trust in the advisor and the delivery of confidential and personal information. [The footnote at this point reads: Even in the barest "order taker" styled stockbroker/client relationship, the "Know Your Client" rule requires the broker to have a large body of private information on the client at his or her disposal.] This fact alone

> dictates a stringent code of conduct which governs all persons who provide financial advice. The opportunity for self-dealing and breaches of trust are legion and the courts have been vigilant in the protection of investors.

[222] At page 10-2, Campion cites *Robinson v Funded Investments Inc. (2006)*, 2006 CarswellOnt 4477, for the observation "... every brokerage case is fact specific due to the unique relationship that the broker has with each client." They describe the three general types of services provided by stockbrokers.

[223] When stockbrokers act as simple order takers, a function necessary as the Canadian securities industry is a closed system, the transaction ". . . creates a simple principal-agent relationship. The scope of any fiduciary duty is restricted to the actual transaction or series of transactions."

[224] When a stockbroker performs the additional role of investment advisor, he / she ". . . assumes a much larger role in suggesting investments to the client. In this situation, a fiduciary relationship may or may not exist, depending on the residual discretion vested in the client to control his or her own portfolio and the level of trust placed on the advisor. In all cases, this is a question of fact. In addition to fiduciary duties, an investment advisor is also potentially liable for negligent misrepresentation."

[225] The third type of function exists when the stockbroker acts ". . . as a manager of an investor's account where the manager exercises a discretion which is independent of the investor's direction. This form of financial advice invariably attracts fiduciary obligations . . ."

[226] Several causes of actions against brokers are recognized. The most common is: breach of fiduciary duty, negligence (including negligent misrepresentation) and breach of contract. Because of the nature of the professional relationship, principles of agency law, which impose an ongoing duty on the part of the broker to act "scrupulously, fairly, openly and honestly", are relevant and important. (See Campion, p. 10-2)

[227] There are other possible causes of action. A frequent one, where the allegation involves market manipulation, is fraud or fraudulent misrepresentation and conspiracy. Fraud is not only a relevant cause of action, when the action of the defendants is directed to the plaintiff, but has developed in the United States since the 1940s even absent the ability of a plaintiff to prove actual reliance on a misrepresentation to him or her, through the theory of "*fraud on the market*". It is this cause of action, arising out of s. 10(b) of the *Securities Exchange Act of 1934* that founded class actions by plaintiffs with regards to unpublished market making or stock manipulation, where the plaintiffs had no direct connections to the defendants. *Fraud on the market* was not pleaded by any of the Dunlop Clients.

[228] Because fraud, in the form of illegal market manipulation, was pleaded by NBFL against Wadden and Barthe, and by some of the Dunlop Clients against Clarke, and because much of the evidence before the Court centred on the machinations by Clarke directly and through the 540 account, which had the effect of manipulating (in this case attempting to maintain) an artificially

high market price for the shares of KHI, the Court spent some time reviewing the case law respecting stock manipulation.

[229] For this, the Court has also reviewed several additional texts, including: **Nicholls, Christopher C.** *Corporate Finance and Canadian Law*. Toronto: Carswell, 2000, pp. 97 - 99; Petraglia, Philip and Lazar Sarna. *Corporate Securities Law in Canada*. Markham: Butterworths, 2005, ch. XVII; **Soderquist, Larry D**. and **Theresa A. Gabaldon.** *Securities Law, 2nd ed.* New York: Thomson West, 2004, Borden Ladner Gervais LLP. *Securities Law and Practice, 3rd ed.* Toronto: Thomson Carswell, 2009 (loose leaf) ch. 21 and 23; **Loss, Louis** and **Joel Seligman**, *Fundamentals of Securities Regulation, 4th ed.* New York: Aspen, 2004 ch. 9, 10 and 11; and **Poser, Norman S.** "Stock Manipulation and Corporate Control Transactions", (1986, 40 U.Miami.L.Rev, 671); Biron, Caroline and Oliver C. Bouton. "Recent Developments in Broker's Liability in Canada", in **Todd L. Archibald** and **Randall Scott Echlin, EDS**., *Annual Review of Civil Litigation 2011*. Toronto: Thomson Carswell, 2011, pp. 303-344; and **Powell, John L.**, **Roger Stewart** and **R. Jackson**. *Jackson & Powell on Professional Liability,* 6th ed. London: Sweet & Maxwell, 2007 & 4th supp. to 6th ed., October 2010. c. 15.

[230] Three of the four groups of Dunlop Clients (Dunham, Weir and Wadden) expressly plead breach of fiduciary duty, negligence and breach of contract by Clarke and NBFL.

[231] In addition, Wadden expressly pleads that Clarke, on his own or possibly with third parties including Potter and Colpitts, unlawfully manipulated the KHI share price. Weir adopts and incorporates Wadden's claim that Clarke, alone or with others, manipulated the KHI share price.

[232] Barthe, in his action, pleads breach of contract by NBFL and Clarke, as well as negligence by NBFL in failing to supervise Clarke, who, Barthe alleges, was involved in a stock manipulation scheme with Potter. He relied upon and incorporated NBFL's pleadings of a conspiracy to manipulate KHI's share price against Clarke and Potter in the Main Action.

[233] The Dunlop Clients: Dunham, Weir and Wadden allege that Clarke failed to follow instructions to sell KHI shares. All three allege that Clarke held various conflicts of interest between his duty to them as clients, with actions and interests of himself, of the 540 account and of KHI insiders such as Potter. Dunham and Wadden allege that Clarke disclosed confidential information to others, including Potter and Colpitts, and sacrificed the interests of Dunham and Wadden for himself and others.

[234] Dunham alleges that Clarke breached such fundamental duties as a failure to diversify Dunham's account in light of Dunham's instructions and his obvious naivety with respect to investing. Wadden alleges that Clarke counselled him to purchase KHI shares when he knew or ought to have known that the price was being artificially maintained.

[235] All of the Dunlop Clients allege that NBFL failed to monitor or supervise Clarke and his various dealings in KHI shares, including through the 540 account.

[236] All of the Dunlop Clients say that NBFL is vicariously liable for the wrongdoing of Clarke, their employee.

C.3 Stock Manipulation

[237] Market manipulation "is probably as old as the securities markets" **(Louis Loss, Joel Seligman & Troy Paredes**, *Fundamentals of Securities Regulation*, 6th Ed, Vol 2 (New York: Wolters Kluwer Law & Business, 2011) at 1485.

[238] Despite this history, comprehensively defining the outer boundaries of what constitutes "market manipulation" has proven difficult (Norman S Poser, "Stock Market Manipulation and Corporate Control Transactions" (1986) 40:3 University of Miami Law Review 672). In *Santa Fe Industries, Inc. et al v Green et al*, 430 US 462 at 477 (1977), the Supreme Court of the United States remarked, in *obiter*, that in the securities context, *manipulation* is "virtually a term of art."

[239] This definitional imprecision has led some to argue that the concept of market manipulation should be abandoned, particularly since it often turns on the subjective intention of the alleged manipulator (Fischel & Ross, "Should the Law Prohibit *Manipulation* in Financial Markets?" (1991) 105 Harv L Rev 503 at 506-507). The response of legislators, however, has not been to abandon prohibitions against market manipulation, but instead to pass and amend laws to address the impact of rapid "technological advances in the securities industry" (Mark Borrelli, "Market Making in the Electronic Age" (2000-2001) 32 Loy U Chic LJ 815 at 907) and emergent fraudulent schemes resulting from a combination of human ingenuity, greed, and questionable ethics.

[240] The reason for these ongoing legislative efforts is twofold. The primary purpose of securities legislation is to protect investors, but it also serves to maintain efficient capital markets and public confidence in these markets (*Pezim v British Columbia (Superintendent of Brokers*), [1994] 2 SCR 557). The rationale behind these protections is that they enhance "the pool of capital available to entrepreneurs" (*Kerr v Danier Leather Inc.*, 2007 SCC 44 at para 32) thereby providing an essential prerequisite for our capitalist system.

[241] Before reviewing the existing law, it is helpful to have an understanding of the types of manipulative schemes that are frequently employed, such as wash sales (and related matched orders), dissemination of false information, scalping, false market signals from high volume trading, and parking or warehousing stocks (**Mark R. Gillen**, *Securities Regulation in Canada*, 3rd Ed (Toronto: Thomson Carswell, 2007); **Alan R Bromberg** & **Lewis D Lowenfels**, *Securities Fraud & Commodities Fraud*, Vol. 3 (New York: McGraw-Hill Inc., 1991)). More than one are evident in this litigation.

[242] A *wash sale* "is a trade in which there is no change in the beneficial ownership of the security (i.e., the buyer is also the seller or the buyer and seller are acting jointly)" (**Gillen**, *Securities Regulation* at 423). A *matched order* is a transaction where one party enters an order for a security knowing that another party, acting in concert, will simultaneously enter a corresponding offsetting order for substantially the same size and price (**Bromberg**, *Securities Fraud* at 7:58).

[243] *Dissemination of false information*, positive or negative, sometimes in the former case referred to as *touting*, is self-explanatory. Scalping "involves the purchase of a particular security just prior to touting the security in some form of investment commentary or news media" (**Gillen**, *Securities Regulation* at 425).

[244] *False market signals* occur when one or more persons, "who control a large portion of the securities of an issuer" sell a large volume of the security in order to profit from the artificially depressed price (**Gillen**, *Securities Regulation* at 425). Relatedly, *warehousing* and *parking* involves, respectively, transactions where the recipient ultimately intends to sell a security back to the original seller at the same price, and transactions where a broker-dealer temporarily transfers securities to a customer's account.

[245] These manipulative schemes can often be combined. A classic manipulative scheme is described in as follows:

> The group [of manipulators] first secures an option to purchase at a price higher than the then market quotation a large block of a stock which possesses actual or potential market appeal and an easily controllable floating supply. It is the task of the pool manager and operator to raise the market price above the option price, and, if the supply on the market remains constant, this can be accomplished only by increasing the demand. The most effective manner of inducing others to purchase is to have a favorable ticker tape record which indicates to prospective purchasers that others consider the security to be underpriced. The manager opens a number of accounts with various brokers and, fortified by a knowledge of the condition of the market obtained from the book of a specialist, enters both buying and selling orders with a preponderance of the former so that the price is made to rise slowly upon an increasing volume of transactions. In the cruder form of operation many of these transactions will be washed sales in which the operator is both buyer and seller of the same stock; in others known as matched orders he enters orders to sell with the knowledge that some confederate is concomitantly entering orders to purchase the same amount of stock at the same price. As the price slowly rises, a complex publicity apparatus is set into motion to aid the stimulation of demand: The directors of the corporation whose stock is being manipulated, who may be members of the pool, issue favorable, but not wholly true, statements concerning the corporation's prospects; brokers, likewise interested in the operations, advise customers through market letters and customers' men to purchase the stock; subsidized tipster sheets and financial columnists in the daily papers tell glowingly of the corporation's future; "chisellers," "touts," and "wire-pluggers" are employed to disseminate false rumors of increased earnings or impending merger. As the market price passes the option price, the operator exercises his option and, increasing his sales over purchases, carefully unloads upon the public the optioned stock as well as that acquired in the process of marking up the price. But the operator does not necessarily rest with this gain. If he is able to distribute his holdings, he may sell short, and the stock, priced at an uneconomically high level and bereft of the pool's support, declines precipitately. As it approaches its normal quotation the pool covers its short position, thereby profiting both from the rise which it has engineered and the inevitable reaction ("Market Manipulation and the Securities Exchange Act" (1937) 46 Yale LJ 624 at 626-628).

[246] Manipulative schemes also frequently depend on the nature of the market for a given security. For example, "[m]arket manipulation [that depends on volume signals] is more likely to work where there is a relatively low volume of trading in the security" (**Gillen**, *Securities Regulation* at 426). This is because sophisticated investors, who can adequately research the fundamentals of a company, are less likely to invest in thinly traded stocks, leaving relatively unsophisticated investors, who depend on price and volume as proxies for research, as the main market participants

(**Gillen**, *Securities Regulation* at 426).

Statutory Responses to Market Manipulation

[247] In Canada, responses to market manipulation can be found in the *Criminal Code*, RSC 1985, c C-46, provincial securities statutes, such as the *Securities Act*, RSNS 1989, c 418, and self-regulatory rules, such as the Investment Industry Regulatory Organization of Canada's National Instrument 23-101 – *Trading Rules*.

[248] Section 383 of the *Criminal Code of Canada* prohibits certain types of transactions that are intended to manipulate the price of a stock:

> **Fraudulent manipulation of stock exchange transactions**
>
> Every one who, through the facility of a stock exchange, curb market or other market, with intent to create a false or misleading appearance of active public trading in a security or with intent to create a false or misleading appearance with respect to the market price of a security,
>
> (a) effects a transaction in the security that involves no change in the beneficial ownership thereof,
>
> (b) enters an order for the purchase of the security, knowing that an order of substantially the same size at substantially the same time and at substantially the same price for the sale of the security has been or will be entered by or for the same or different persons, or
>
> (c) enters an order for the sale of the security, knowing that an order of substantially the same size at substantially the same time and at substantially the same price for the purchase of the security has been or will be entered by or for the same or different persons,
>
> is guilty of an indictable offence and liable to imprisonment for a term not exceeding ten years.

[249] Section 3.1(1) of National Instrument 23-101 – Trading Rules addresses manipulation and fraud:

> A person or company shall not, directly or indirectly, engage or participate in any act, practice or course of conduct relating to securities or derivatives of securities that the person or company knows or reasonably ought to know
>
> (a) results in or contributes to a misleading appearance of trading activity in, or an artificial price for, a security or derivative of a security; or
>
> (b) perpetrates a fraud on any person or company.

[250] In 2006, the *Securities Act* was amended to include the following in s 132A:

> A person or company shall not, directly or indirectly, engage or participate in any act, practice or course of conduct relating to securities or derivatives of securities that the person or company knows or reasonably ought to know
>
> (a) results in or contributes to a misleading appearance of trading activity in, or an artificial price for, a security or derivative of a security; or

> (b) perpetrates a fraud on any person or company.

[251] Given the paucity of Canadian jurisprudence on what constitutes market manipulation, it is also helpful to consider the comparatively rich US jurisprudence on this subject. In doing so, one must be cautious to recognize that in the US, the basis for civil claims alleging damages from market manipulation is frequently statutory. This means that the US jurisprudence is not immediately portable to Canada, but it does not mean that it is irrelevant.

[252] The US *Securities Exchange Act of 1934*, 15 USC §78a, contains a number of provisions that prohibit market manipulation of securities prices on securities exchanges and in the over-the-counter market. In particular, s. 9(a)(2) makes it unlawful to use the mails, other means of interstate commerce, or a national securities exchange:

> To effect, alone or with 1 or more other persons, a series of transactions in any security other than a government security, any security not so registered, or in connection with any security-based swap or security-based swap agreement with respect to such security creating actual or apparent active trading in such security, or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others.

[253] The prohibitions on market manipulation contained in the *Exchange Act* are also buttressed by *Rule 10b-5*, *Employment of manipulative and deceptive devices*, which was promulgated by the Securities Exchange Commission pursuant to the *Exchange Act*. That *Rule* is often central to US jurisprudence on market manipulation and reads:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

Permissible Market Manipulation

[254] Despite these prohibitions against market manipulation, there are certain manipulative activities that are nonetheless permitted if they are found to be for the purpose of "stabilization".

[255] A common example of permissible "stabilization" occurs in new offerings of securities that are already traded on an exchange (**Larry D. Soderquist** and **Theresa A. Gabaldon**, *Securities Law*, 2nd Ed (New York: Thomson, 2004) at 181). During such transactions, underwriters, who sell securities to investors on behalf of the issuers, face a risk that the market price will drop to such a degree that it erases the "underwriting spread" and creates a loss for the underwriters. Since

underwriters provide an essential service to the functioning of capital markets, the securities regulators permit underwriters to "stabilize" the market in the security being issued in order to artificially maintain its price until the offering is completed (Soderquist, *Securities Law*).

[256] Another permissible type of manipulation is trading by *market-makers*. The Ontario Securities Commission (OSC) has defined a *market-maker*:

> as a person, normally approved by the stock exchange on which the shares are listed, who buys and sells shares of an issuer as principle or for his own account on a continuous basis with a view to creating or maintaining an orderly market for the shares. Their function is to take the other side of a transaction when none is apparent, that is, to buy a stock when someone wishes to sell and there are no apparent buyers and vice versa. The market-maker also attempts to prevent undue variations in the price of a stock by selling into a rising market or buying in a declining market. These are called stabilizing trades because they attenuate the buying or selling pressure. Destabilizing trades, on the other hand, work the opposite way, that is they are buys in rising market and sales in a declining market which tend to exacerbate the pressure. The purpose of a market-maker is to provide liquidity and to maintain an orderly market.

[257] When a *market-maker* is simply taking the other side in a transaction, their trades will not be manipulative *per se*, but when their trades "prevent undue variations in the price of a stock," they are in effect manipulating the market. According to the OSC, selling in a rising market and buying in a declining market are both permissible forms of stabilization.

[258] The SEC takes a more narrow approach, defining *stabilization* as "the buying of a security for the limited purpose of preventing or retarding a decline in its open market price in order to facilitate its distribution to the public" (SEC, Exchange Act Release No. 2,446 Mar 18, 1940). Nonetheless, the SEC permits market-makers to enter sell-side orders to provide liquidity and to maintain an orderly market, presumably on the basis that such transactions are neither stabilizing nor destabilizing.

[259] It is fair to see that major securities regulators "view stabilization as a necessary evil" (Soderquist, *Securities Law* at 183).

[260] The specific rules that apply to market-makers depend on the exchange where the security is traded. For example, the Toronto Stock Exchange (TSX), on which KHI traded, requires all market-makers to be designated upon application by a Participating Organization, usually an investment bank. The Participating Organization then designates one of its employees to be the formal market-maker, who is then subject to the TSX rules concerning market-making.

[261] Where over-the-counter trades are concerned, some securities legislation requires an application to the provincial regulator to become a market-maker. For example, in Ontario, s. 155 of the *Securities Act*, RRO 1990, Regulation 1015 reads:

> A registered dealer, other than a security issuer, mutual fund dealer or scholarship plan dealer, may apply to the Director for approval to act as a market-maker in a COATS security of a class that trades in Ontario.

Test for Market Manipulation

[262] The test for what constitutes market manipulation depends on the statutory framework and context in which a case arises. For example, market manipulation in the context of a criminal charge is obviously tied closely to the wording of the criminal statute. Market manipulation allegations in the context of a provincial regulator's "public interest power" is more relaxed and linked to the provincial legislation. Market manipulation in the context of a civil action depends on whether it is an action pursuant to the common law or a statutory action where available. In any event, the jurisprudence discloses some common elements of what constitutes market manipulation.

[263] Market manipulation requires a manipulative or deceptive scheme (*Anderson v British Columbia (Securities Commission)*, 2004 BCCA 7, leave to appeal to the SCC denied [2004] SCCA 81, [*Anderson*]; *Santa Fe Industries, Inc. et al v Green et al*, 430 US 462 (1977)).

[264] There must be an intention on the part of the person(s) employing the scheme to defraud, that is, there is a *mens rea* requirement of *scienter* (*R v Jay*, [1966] 1 CCC 70 (Ont CA); Ernst *& Ernst v Hochfelder et al*, 425 US 185, (1975)). In the context of an anti-manipulation provision that is similar to s 132A of the *Securities Act*, the British Columbia Court of Appeal held that subjective knowledge of the relevant facts is required when proving market manipulation - recklessness is not sufficient (*Anderson* at para 28).

[265] In *Anderson*, the Court also imported into the market manipulation context the test for fraud outlined by McLachlin J (as she then was) in *R v Theroux*, [1993] 2 SCR 5 at 20:

> … the actus reus of the offence of fraud will be established by proof of:
>
> 1. the prohibited act, be it an act of deceit, a falsehood or some other fraudulent means; and
>
> 2. deprivation caused by the prohibited act, which may consist in actual loss or the placing of the victim's pecuniary interests at risk.
>
> Correspondingly, the mens rea of fraud is established by proof of:
>
> 1. subjective knowledge of the prohibited act; and
>
> 2. subjective knowledge that the prohibited act could have as a consequence the deprivation of another (which deprivation may consist in knowledge that the victim's pecuniary interests are put at risk).

[266] The BC approach has been followed in Ontario (*Al-Tar Energy Corp, Re* (2010), 33 OSCB 5535, 2010 CarswellOnt 3966). Given the similarity between s 132A of the *Securities Act* and the BC and Ontario legislation, it also makes sense to follow this approach in Nova Scotia.

[267] A manipulative purpose may be inferred from circumstantial evidence, but caution must be exercised not to review individual trades in isolation (*Sears Canada Inc., Re*, 2006 CarswellOnt 6994 (OSC) at para 28; *Federal Corp.*, 25 SEC 227 at 230 (1947); *MacLean v Huddleston*, 459 US 375 at 390 to 391 (1983).

[268] Circumstantial evidence might take a variety of forms such as purchasing blocks in successively higher prices, deliberate activity to dry up overhanging supply, agreements to withhold large amounts of the security from the market, concomitantly timed disclosures (accurate or otherwise), "guaranteeing purchasers against loss, or arranging for the issuer to declare a dividend at a critical juncture in the manipulation (**Loss**, *Fundamentals of Securities* at 1500).

[269] While creation of an "article price" for a security may be evidence of manipulation (*Sears Canada* at para 127), and a crucial requirement for the establishment of damages in a civil action, a successful scheme is *not* an element for the offence of market manipulation (*Rex v de Berenger*, (1814), 3 Maule & S 67, 105 Eng Rep 536 at 537). As Lord Ellenborough explained in *de Berenger*:

> …the crime lies in the act of conspiracy and combination to effect that purpose, and would have been complete although it had not been pursued to its consequences, or the parties had not been able to carry it into effect.
>
> The creation of "a misleading appearance of trading activity" alone is sufficient "because it misleads other buyers and sellers (*Sears Canada* at para 127).

Position of the Parties

[270] While much evidence was tendered in this case regarding Clarke's activities, neither the Dunlop Clients nor NBFL provided much assistance in their post-trial submissions on the law concerning market manipulation. The Dunlop Clients cited material that was disclosed by NBFL, but *not* entered into evidence, as "proof" of the manipulation. This material is irrelevant since it was not entered into evidence. The Dunlop Clients provided no submissions on the boundaries of market manipulation or how the evidence that was tendered meets the test for market manipulation. NBFL provided submissions on some of the case law concerning market manipulation, but its submissions were highly selective.

[271] NBFL submits that expert evidence is required to establish the industry standards that NBFL is alleged to have breach through their admitted lack of supervision and/or vicarious liability for Clarke's actions. NBFL further submits that expert evidence is required to establish that Clarke's actions were not consistent with that of an ordinary market-maker. In the alternative, NBFL argues that the Dunlop Clients have failed to establish that Clarke's actions resulted in an "artificial price" and that he intended to create an "artificial price."

[272] NBFL cites *Connolly v Walwyn Stodgell Cochran Murray Ltd* (1993), 121 NSR (2d) 278 [*Connolly*], *820823 Ontario Ltd v Kagan*, 2003 CarswellOnt 1446 (Ont Sup Ct J), and *Cole v Merrill Lynch Canada Inc*, 2005 CarswellOnt 9962 (Ont Sup Ct J) for the proposition that expert evidence is necessary to establish the industry standards that the Dunlop Clients say NBFL breached.

[273] *Connolly* stands for the proposition that a plaintiff must identify the particular standard that he alleges the defendant breached. The Court of Appeal in that case remarks that no expert evidence was adduced to establish unsuitability, but this is not the same as saying that expert evidence must be adduced in all cases; in any event, the Court of Appeal's remarks is *obiter* because the Court also found that the plaintiff in that case failed to plead unsuitability.

[274] In *Kagan*, the Ontario Superior Court of Justice held that the Court should be vigilant about admitting unnecessary expert evidence, but went on to find that expert evidence of investing account management was likely not within the knowledge of the trier of fact and was therefore helpful, though not determinative, in determining the standard of care.

[275] In *Cole*, the Court followed *Kagan* and held that investment advisor handbooks and internal bank policies were evidence of the standard of care, but that expert evidence was necessary to properly apply those standards, especially when the bank's internal rules were somewhat flexible and therefore open to interpretation.

[276] Recently, in *Johansson v General Motors of Canada Ltd*, 2011 NSSC 352, the Court reviewed the onus on the plaintiff, in an action for negligence, to establish the specific standard of care that she says was breached. The Court cited favourably a decision of the Ontario Court of Appeal, *Krawchuk v Scherbak*, 2011 ONCA 352. There, the Court held, at para 125:

> External indicators of reasonable conduct, such as custom, industry practice, and statutory or regulatory standard, may inform the standard. Where a debate arises as to how a reasonable agent would have conducted himself or herself, recourse should generally be made to expert evidence.

[277] At para 36, the Court also accepted the two exceptions, outlined in *Krawchuk*, to the requirement that the plaintiff must adduce expert evidence of how to apply the standard of care when there are ambiguities in what constitutes "reasonable conduct":

> Failure to produce this type of evidence is not always fatal to a plaintiff's claim. In Krawchuk, the Ontario Court of Appeal outlined two exceptions to the general rule that expert evidence is required in the articulation of a professional's standard of care. The first exception is where the matters are non technical and therefore within the ordinary knowledge of the trier of fact (*Krawchuk* at para. 133).
>
> The second exception is where the defendant's conduct is so egregious that it would be obvious to an ordinary person that the "conduct has fallen short of the standard of care, even without knowing precisely the parameters of that standard" (*Krawchuk* at para. 135).

[278] The Nova Scotia Court Appeal, in overturning the defendants' non-suit motion in *Johansson*, 2012 NSCA 120, dealt with the type of evidence of industry practices and regulatory benchmarks that are required of a plaintiff, and those circumstances where expert evidence is and is not required to establish the standard of care and the application of that standard to the facts.

[279] The trial court had held that expert evidence was required unless the issues were non-technical or the defendants' conduct was egregious. The Court of Appeal effectively held that evidence of industry practices and regulatory benchmarks, in addition to expert evidence, may be persuasive and probative, but not necessary. The analysis runs from paras 90 to 124 of that decision. Particularly relevant statements include, at para 105:

> . . . it is for the jury to balance those factors and weigh the evidence related to the application of the standard of care. It is for the jury to decide whether in the circumstances of a particular case evidence of industry practice or regulatory benchmarks, on the one hand, or evidence surrounding the defect, on the other, should tip the scale. It is not for the judge to wade into the factual waters with a finding that a particular factor, such as industry practice, . . . will outweigh the others.

[280] At paragraph 110:

> . . . a plaintiff may lead evidence that the defendant failed to comply with industry practice, and that evidence may assist to establish a *prima facie* case. Or the defendant may lead evidence of compliance with industry practice. Either way, the evidence is to be weighed, with other evidence, by the jury at the conclusion of the trial. But evidence of industry practice does not necessarily trump other evidence and settle the negligence issue in the jury room. . . .

[281] At paragraph 111, in commenting on the fact that there was no evidence of how the defendant performed against the regulatory benchmark, Fichaud, J.A. noted that the case was not a private prosecution for an offence under the legislation, but rather a negligence action where the trier of fact is to assess the reasonableness of the defendant's conduct.

[282] At paragraph 115, Fichaud, J.A., recognized that the standard of care for each professional is defined by reference to his or her profession and that evidence related to the standards of the defendant's particular professions "is in order". But, he goes on to cite *Ryan v Victoria*, [1999] 1 SCR 201 (SCC), to note that expert evidence of industry standards would be relevant but is not legally mandatory in certain circumstances. It is a matter of whether the issue so technical that the trier of fact cannot reasonably determine the standard of care or the application of it to the facts without expert evidence.

[283] It is true that the Dunlop Clients have not tendered expert evidence on how to apply the standard of care expected of Clarke and NBFL. In my view, on the basis of *Krawchuk*, this failure is not fatal to the Dunlop Clients' claims. I am satisfied that the conduct is "so egregious" that expert evidence is not essential for determination of whether the market manipulation in this case was a breach of what is expected of a reasonable investment advisor or order taker.

[284] NBFL cites *Cycomm International Inc., Re*, 1993 CarswellOnt 922 (OSC) for the proposition that expert evidence is necessary to establish market manipulation. In *Cycomm*, the OSC held that disagreement between two experts "highlighted the difficulty in characterizing **the trades in question** as manipulative or market-making" [emphasis added]. The OSC did not find that expert evidence was obligatory in all cases.

[285] In Canada, expert evidence is not required as a matter of course. To the contrary, expert evidence is only admissible where it is necessary *R v Mohan*, [1994] 2 SCR 9.

> What is required is that the opinion be necessary in the sense that it provide information "which is likely to be outside the experience and knowledge of a judge or jury": as quoted by Dickson J. in R. v. Abbey, supra. As stated by Dickson J., the evidence must be necessary to enable the trier of fact to appreciate the matters in issue due to their technical nature. In Kelliher (Village) v. Smith, [1931] S.C.R. 672, at p. 684, this court, quoting from Beven on Negligence (4th ed. 1928), p. 141, stated that in order for expert evidence to be admissible, "[t]he subject-matter of the inquiry must be such that ordinary people are unlikely to form a correct judgment about it, if unassisted by persons with special knowledge." More recently, in Lavallee, supra, the above passages from Kelliher and Abbey were applied to admit expert evidence as to the state of mind of a "battered" woman. The judgment stressed that this was an area that is not understood by the average person.

[286] “In many cases, the proffered [expert] opinion evidence will fall somewhere between the essential and the unhelpful” *R v Abbey* (2009), 97 OR (3d) 330 (CA), leave to appeal to SCC refused, (2010 CarswellOnt 4827). While expert evidence may have fallen toward the essential end of the spectrum in *Cycomm*, I am not satisfied that the same can be said in this case. In *Cycomm*, the sole evidence of manipulation was the trading pattern in question. In this case, there is a substantial amount of non-technical evidence of manipulation. The allegation of market manipulation against Clarke does not depend solely on his trading pattern. I am satisfied that I can, as the trier-of-fact, appreciate the matters in issue without recourse to expert evidence.

[287] In the US, “expensive securities-fraud actions will ordinarily have at their disposal experts of the highest caliber to test each other,” (Patrick J Coughlin, Eric Alan Issacson & Joseph D Daley, “What’s Brewing in *Dura v Broudo*: The Plaintiff’s Attorneys Review the Supreme Court’s Opinion and Its Import for Securities-Fraud Litigation” (2004) 37 Loy U Chi LJ 1 at 40) but the rule is that such experts *may* be employed not that they *must* be employed (*United States v Bilzerian*, 926 F.2d 1285 at 1294 (2nd Cir. 1991); *Blackie v Barrack*, 524 F.2d 891 at 909 (9th Cir. 1975); *Huddleston v Herman & MacLean*, 640 F.2d 534 (5th Cir. 1981), aff’d in part and rev’d in part on other grounds, 459 US 375 (1983)). In the US, like in Canada, triers-of-fact, whether juries or judges, are empowered and trusted to make complex evaluations of fact (US Fin Sec Litig, 609 F.2d 411 at 429-430 (9th Cir. 1979); *Morgan v District of Columbia*, 824 F.2d 1049 at 1062 (DC Cir 1987); *SRI Int’l v Matsushita Elec Corp*, 775 F.2d 1107 at 1130 (Fed Cir 1985); *Cotton v Witco Chem Corp*, 651 F2d 274 at 276 (5th Cir 1981)).

[288] NBFL also cites *Cycomm* for the proposition that companies may act as their own market-makers. In *Cycomm*, the security at issue traded on the Alberta Securities Exchange (ASE). The OSC noted that the ASE had no rules regarding issuers acting as market-makers in their own securities. The OSC further noted that in the case of venture markets, like the ASE, investment banks may be reluctant to act as market-makers, but may require a market-maker before recommending a stock. The OSC held that “[a] company **in these circumstances** may feel it has no alternative but to act as its own market-maker” and would go about doing so by opening an account at a brokerage and granting a broker discretion to buy-and-sell its shares as a market-maker [emphasis added].

[289] The problem that NBFL faces is that even if companies can act as their own market-makers, there is not even an air of reality to the argument that Clarke was acting as a market-maker on behalf of KHI. There is no documentation whatsoever to establish this role. Moreover, the TSX, on which KHI traded, requires formal registration of any market-makers. Clarke was not formally registered as the market-maker for KHI. In fact, another individual, Mr. Watson from BMO, was already registered as the official market-maker.

[290] NBFL’s final argument is that Clarke’s trading activity was not manipulative either because he failed to create an artificial price and/or because he had no intent to create an artificial price. I find that Clarke’s activities were manipulative and were intended to be manipulative.

[291] From a very early stage, Clarke had a personal pecuniary interest in KHI and a close relationship with Potter, the CEO of KHI, and Colpitts. In October 1997, for reasons that Clarke was

unable to explain, Potter gave Clarke an option to purchase 100,000 common shares of KHI at $0.50 per share. In July 1999, with KHI trading at $4.20, Clarke exercised his option, placing $420,000.00 worth of KHI stock, for which he paid only $51,808.22 (with interest), in a joint margin account held by himself and his wife.

[292] Clarke also traded KHI in another margin account, the 540 account, which was opened in the name of his numbered company, 2317540 Nova Scotia Limited. It was this account where Clarke conducted the majority of his trading activities in KHI. Clarke testified at trial that all decisions concerning this account were made by him, even though he admitted before the Securities Commission to using the account to execute trades on behalf of a KHI insider's group. Clarke testified that he admitted to this wrongdoing and paid a $150,000.00 fine because he was fed up with the ongoing Securities Commission process and did not have money to continue to pay his lawyers.

[293] Clarke testified at trial that Potter loaned him $100,000.00 to place in the 540 account to allow Clarke to buy KHI on margin. Clarke further testified that this was an informal loan and that the beneficial ownership of the KHI stock purchased would remain his. Clarke acknowledged that he received a share certificate for 220,000 KHI shares from Wadden via Potter or Colpitts and that this was placed in the 540 account. At the time, these shares were valued at $1.5 million and allowed Clarke to purchase further KHI stock on margin. Clarke could not explain why there was no documentation for this share transfer, but claimed that it was received as a loan.

[294] Clarke also had difficulty explaining the trading activity within his 540 account and joint spousal account. He testified that he was simply acting as a market-maker during times when KHI insiders were unable to trade in the stock. Clarke testified that Potter and Colpitts informed him of these restricted periods.

[295] Clarke further testified that he did not know that Watson was the designated market-maker for KHI. He refused to acknowledge that he was aware of the TSX market-maker designation process. I find Clarke's evidence on this point to be without credibility. During his testimony he was evasive. More important, Clarke was an experienced investment advisor with more than 25 years of experience in the industry. He testified that he was aware of the market-maker designation process for the Montreal Stock Exchange as a result of trading activity that he conducted before his involvement with KHI. Further, Clarke had previously been subject to discipline proceedings before the Montreal Stock Exchange and internally by NBFL's predecessor. It is simply not plausible for Clarke to submit that he was unaware that he had to be designated by the TSX as a market-maker for KHI.

[296] Clarke's trading activity within the 540 and joint spousal accounts does not support his claim that he was acting as a market-maker. Between March 2000 and July 2001, Clarke executed 707 trades in KHI. The vast majority of these trades were buy orders. Clarke bought KHI 636 times during this period and sold KHI 71 times. Combined, Clarke traded 1,281,000 shares of KHI during this period. This accounted for 29 percent of the total volume (4,390,000) of KHI shares that were traded during this period.

[297] A true market-maker takes both sides of the equation. For the most part, Clarke only bought

KHI, in what appears to have been a concerted effort to absorb excess supply of the stock. This does not immediately mean that Clarke was attempting to manipulate the market, but it is one indicium of manipulation, particularly when considered against the other evidence before the Court.

[298] Clarke was adamant that he, and he alone, controlled the 540 account. I find this assertion to be without credibility. Beyond the unexplained financing of the 540 account by Potter and Wadden, Clarke also took instructions from both Potter and Colpitts on how to operate the account. The documentary evidence shows that when Wadden and his counsel began efforts to recover control of the KHI shares that were deposited in the 540 account, Clarke sought advice and instruction from Potter and Colpitts.

[299] Clarke was also in communication with both Potter and Colpitts when arrangements were made for large purchases of KHI by outside investors. Clarke denied being aware of Derek Banks' intention to buy $1,000,000.00 worth of KHI, but I find this denial to be without credibility, particularly given Clarke's knowledge of other transactions.

[300] Clarke acknowledged that he became aware of Barthe's intention to invest in KHI through Colpitts. He was brought in by Potter and Colpitts to facilitate this investment on the open markets. Clarke opened an account at NBFL in order to receive Barthe's $1.7 million that would then be used to purchase KHI stock. Almost all of Clarke's communication for this transaction was through KHI insiders.

[301] The transactions that Clarke executed to purchase KHI on behalf of Barthe are particularly troubling. Clarke first sold 43,300 KHI shares at $6.50 from his personal account to an account owned by Colpitts. He then sold 73,300 KHI shares at $6.55 from Colpitts account to Barthe's account that Clarke had just set up. Clarke also sold KHI shares from other insiders to Barthe. Clarke could not explain to the Court why Colpitts account had to be used as a conduit for some of the shares that Barthe purchased. Clarke also could not explain why Barthe paid $0.05 per share more than what Colpitts paid for purchasing the shares from Clarke.

[302] I find that the manner in which KHI was sold to Barthe was a wash trade or matched trade for the purpose of creating a false impression of trading volume in KHI stock. There is no explanation as to why the 43,300 shares had to first be sold to Colpitts before they were sold onto Barthe. There is no explanation as to why there was a price differential. This leads to the inference that the trade was manipulative.

[303] Shortly after the sale of KHI shares to Barthe, Clarke contacted Potter to advise him that Barthe's purchase had taken a lot of buying pressure off of KHI. If Clarke was acting independently, there is no reason why he would be advising Potter on the trading activity in KHI.

[304] Another highly dubious trade occurred in September 2000. At that time, Clarke sold 150,000 KHI shares for $990,000.00. This was a very significant amount of shares given the trading volume in KHI. Clarke could provide no explanation or recollection of this share purchase. The documentary evidence suggests that this sale was particularly timely given that NBFL at that time was instructing Clarke to reduce his margin debt. This sale, combined with Barthe's purchase of

259,000 KHI shares, significantly reduced Clarke's margin debt at the precise time that was needed. I find that this timing was not coincidental.

[305] Counsel for NBFL presented documentary evidence to Clarke that showing that the 150,000 shares were purchased by David Fountain, who also purchased another 150,000 shares directly from the KHI treasury. This did not refresh Clarke's memory. The documentary evidence shows that Fountain purchased 150,000 shares from the treasury at $6.65 per share. The shares that Clarke sold were also sold for $6.65 per share. Given how thinly traded the KHI stock was, this suggests that Clarke's sale of 150,000 shares was an arranged sale by a KHI insider and not a coincidence.

[306] In October 2000, Clarke immediately resumed buying KHI shares on margin, which brought his margin debt from $419,000.00 to $1.4 million. Clarke testified that he had no recollection of why his self-appointed market-maker status required such an active period of purchases at that time. In what does not appear to be a coincidence, the price of KHI during this period was maintained at the precise level that ensured there would not be a margin call in Clarke's account.

[307] As will be seen in the detailed discussion of each Dunlop Client, Clarke also used his clients' accounts to buy KHI on margin. He ignored explicit instruction to sell KHI from these accounts. Instead, he advised Potter and/or Colpitts of who was considering selling KHI stock so that they could put pressure on these individuals not to sell. In at least one case, Clarke ignored an explicit standing order to sell KHI stock. The only time Clarke would sell KHI stock for his clients was when it was needed to prevent a margin call.

[308] In my view, the above, when taken together, is clear and convincing proof that establishes, on a balance of probabilities, that Clarke was attempting to manipulate the market in KHI. The Dunlop Clients have established that Clarke, along with Potter, Colpitts, and others, executed a manipulative scheme to maintain the price in KHI. This scheme started with KHI stock being warehoused in Clarke's accounts. KHI stock was also either parked in Clarke's accounts or sold to him at well below the market value as a quid pro quo for his involvement in the manipulative scheme. Clarke then proceeded to engage in a variety of transactions to send false market signals in the form of artificial trading volume. This included a series of matched orders. This satisfies the *actus reus* of market manipulation.

[309] In this case, the inference of Clarke's intent can be drawn from the circumstances. Clarke was an experienced investment advisor. He knew exactly what he was doing when he executed the various transactions detailed above. He knew that he was acting on behalf of insiders. He also knew that his actions were in conflict with his clients. Clarke's inability to recall his actions speaks of an individual who is facing the possibility of serious criminal sanctions as a result of his wrongdoing. Based on the specific transactions that Clarke executed and their non-coincidental timing, I am satisfied that the Dunlop Clients have established the requisite *mens rea* for market manipulation and I find that Clarke was clearly intending to manipulate the market.

D. Analysis of the liability issues of each of the Dunlop Clients against Clarke and NBFL

D.1 Liability to Dunham

[310] Craig Dunham attended university but did not graduate. He then worked as a bookkeeper, successively for a fast food restaurant, a chemical company and a personal tax return business (H&R Block). In 1991, he started work at Innovative Systems Inc., a small Annapolis Valley computer hardware and software retailer. In 1995, he and a partner, Steven Wilsack, bought the company.

[311] Innovative had the Apple distributorship, first for their part of Annapolis Valley and eventually for all of Atlantic Canada. They operated a store front, retail and service-business as well as a separate component that created an education/school network. In the original location, the company grew to sales of over one million dollars. The business expanded with three other outlets. Dunham's skills were as a jack-of-all trade but mainly in sales, some bookkeeping and some services.

[312] Innovative joined forces with Micronet, and a Cape Breton company controlled by Snow and MacLeod, to tender to the Province of Nova Scotia to sell, install and service computer software and hardware to Nova Scotia's school system on a long-term contract.

[313] By mid-1999, Innovative had 20 employees with gross sales of approximately 3.5 million dollars.

[314] Shortly after KHI purchased the Cape Breton business from Snow and MacLeod, and the Micronet business from Wadden and his partner (Courtney), Dunham and Wilsack were approached to sell Innovative (including their recently awarded contract with the Nova Scotia Department of Education).

[315] After minimal discussions, KHI offered to buy Innovative for one million dollars cash ($500,000.00 to each of Dunham and Wilsack) or, alternatively, 300,000 shares of KHI, valued at $4.00 per share (150,000 shares each), which shares would be released over a five-year period, during which period each would be employed by KHI at a salary of $90,000 per year. Dunham and Wilsack accepted KHI's offer. The offer provided that Dunham would continue to run the New Minas operation.

[316] Counsel for KHI in the transaction was Colpitts. Dunham appears not to have relied upon a lawyer to negotiate or conduct due diligence in respect of the sale of the business. He rather naively trusted KHI and its lawyer to act fairly. He did cause a lawyer to provide KHI's counsel with a certificate on behalf of the vendors.

[317] The terms of the agreement of sale provided for an adjustment of the share price after closing, based on an audit by KHI. As a result of the audit, Dunham was required to pay KHI $141,347.50. He had no money.

[318] To facilitate payment of his debt, it was suggested to Dunham by Potter and KHI's controller, Gerard McInnis, that he open an account with Clarke at NBFL. KHI released 30,000 of Dunham's KHI shares from escrow into an account opened by Dunham with Clarke at NBFL in order to permit Dunham to repay the amount he owed to KHI. Dunham did not initially understand that his account

would be a margin account, or that his KHI shares might not be sold, but rather that NBFL would lend to Dunham monies on margin secured by his KHI shares.

[319] It is clear that Dunham was initially somewhat trusting and naive. He relied on what he was told and did not read the documents used to open the margin account or his initial account statement. The margin account was opened with the receipt of 30,000 KHI shares on March 8, 2000.

[320] At 8:31 a.m. on March 23, Clarke emailed Dunham that he had completed the sale of Dunham's shares and raised about $196,000.00. Based on Clarke's e-mail, Dunham immediately authorized payment of his audit debt to KHI.

[321] When Clarke transferred $141,347.50 to KHI from Dunham's account on March 24, he had not sold a sufficient number of Dunham's KHI shares to pay that amount. By March 28, Clarke had sold Dunham's 30,000 KHI shares at prices of between $6.50 and $6.75, from which $141,347.50 had already been paid to KHI. The remaining $55,042.50 was paid to Dunham on March 28.

[322] With the exception of one interview and very few telephone conversations, all communication between Dunham and Clarke respecting the investment account managed by Clarke for Dunham were by e-mail. These e-mails are in evidence.

[323] A review of these e-mails clearly demonstrates that at the beginning of the relationship between Dunham and Clarke, Dunham was a naive, novice investor. He expressly said so, stating that he relied upon Clarke to diversify his account as he received KHI shares into the account.

[324] NBFL submit that Dunham was an educated, experienced businessperson and investor before he sold Innovative to KHI and opened the margin account with Clarke at NBFL.

[325] I disagree. Dunham had attended university but had not graduated. After university, he worked as a bookkeeper, for a fast food restaurant, then a chemical company. In 1990, he worked at H&R Block preparing personal income tax returns. He commenced employment at Innovative Systems in 1991.

[326] The documentary history of Dunham's investment experience, beginning in the 1990's, shows that Dunham made small investments in mutual funds through a mutual fund salesperson (David Chandler), who appears to have been associated with various fund companies over the years. At the end of 1999, Dunham held three mutual funds valued at about $12,000.00 in an RRSP plan, and, with borrowed money, owned with his spouse a non-registered portfolio of 27 mutual funds valued at about $61,000.00. Dunham's pre-NBFL investment history does not show knowledge, experience or sophistication in investing, let alone knowledge and experience in investing in the stock market as conducted by Clarke or in the operation of a margin account. A $61,000.00 investment account divided amongst 27 mutual funds, many of which were overlapping, is a clear sign of Dunham's lack of knowledge of basic investing principles. On the contrary, Dunham's investment history, like his emails to Clarke, show Dunham to be an unsophisticated person, trusting of his professional advisors, and without the personality to be an inquisitive, prudent or disciplined investor.

[327] Dunham's trust in Clarke was solidified when Clarke was able to liquidate his 30,000 KHI shares within a few weeks of them being deposited into Dunham's account in March 2000.

[328] In hindsight, it is obvious that this sale was accomplished solely because it facilitated the payment by Dunham to KHI of the audit adjustments of $141,000.00. The only other sales, three totalling 13,000 shares, on September 13, November 7, and December 19, 2000, occurred when Dunham's margin debt had grown so close to its upper limit, that his account was at risk of becoming "offside", an event that would have caused NBFL head office to take a closer look at a number of Clarke's clients margin accounts (including the 540 account) dominated by margin loans secured by KHI shares.

[329] The e-mail chain reflecting the relationship between Dunham and Clarke begins with Exhibit 1.3, Tab 71. Dunham communicated with KHI's controller, Gerard McInnis, as to how the audit adjustment owed by Dunham to KHI is to be raised through the release of 30,000 escrowed shares to Clarke. On February 26, 2000, Dunham copied this e-mail to Clarke. He writes in part:

> I would like to get this cleared ASAP as I need to sell additional shares to look after some personal debts beyond the adjustment to the purchase price.
>
> I assume you will need to have some legal notification from me to proceed?
>
> I am new to all this so please bear with me if I don't know all the proper steps.

[330] Three days later, on February 29, Dunham and Clarke exchanged five e-mails in relation to obtaining the 30,000 shares from KHI through KHI's lawyer to pay off the KHI debt and release money to Dunham for his personal needs. In one, Clarke writes that he had a quick discussion with KHI's controller and lawyer and adds:

> You had earlier indicated to me that you wanted to sell some shares to help tidy up some bills, or other payables, thus the above would not accomplish that. I can't say for certain, and you should check with Andrew [a KHI lawyer] but I think if the above payable to Knowledge House is settled it may free up some non-escrow shares that you could then sell and use the proceeds in any way you want to. Give the above some thought as to whether or not this is correct ...

[331] Dunham replied that he understood that:

> The shares will be sold on the open market until the debt is fulfilled. The remainder if any of that block of shares (30,000 shares) will be available to us. Using today's value this would leave me with some capital to clean up some personal debt.

He went on to advise Clarke that he expects to receive more of his shares, held in escrow by KHI, to improve his personal financial situation.

[332] On March 1 and 2, Dunham communicated by e-mail with Gerard McInnis. McInnis confirmed that KHI ("Dan Potter") had agreed to allow the release of another 30,000 of Dunham's KHI shares from the back end of the escrowed shares and closed with the sentence: "Again, we request you co-ordinate the sale of these shares into the market with Bruce Clark[e]."

[333] By March 28, 2000, the first 30,000 shares had been sold on the market; the debt to KHI had been paid and about $55,000.00 had been deposited into Dunham's account.

[334] On April 5, Dunham e-mailed Clarke:

> Hi Bruce,
>
> I thought I should drop you a note about the future share sales. I am planning to purchase or build a home this summer and will likely use proceeds from the sale of shares to pay for all or part of this. The plan is to then re-borrow against the property to reinvest so that I can benefit from the deductible interest on money borrowed for investments rather than lose it all to the bank out right.
>
> To this end, I was wondering if you were able to take me on as a client beyond the present arrangement? In talking to my loans officer, Archie Seamone at the CIBC here in Kentville, he recommended you highly. The idea would be to reinvest the loan proceeds with you.
>
> Let me know your thoughts.
>
> Thanks,
>
> Craig

[335] On April 13, Clarke e-mailed Dunham advising he had received a further certificate for 30,000 KHI shares in Dunham's name. Dunham replied the same day by an e-mail, which read in part:

> I also wanted to mention to you that there was no big hurry to sell these off, as I have looked after most of my immediate cash needs.
>
> I do want to start a more complete portfolio with you however. I may or may not be staying on with Knowledge House, so I could be taking possession of the remaining 90,000 shares as well, if I do chose to move on.
>
> While I believe KHI will continue to grow above the market I would still feel better if I diversified a little more. Archie Seamone recommends you highly and I would like your advise on some investment. I have approx. $1 Million dollars at the current stock price but I would like to grow this as I do have plans to build a house this summer, which will set me back about $300,000 by the time the lot, house and some landscaping is done. My plans are to pay this off through the sale of the shares and then borrow the same (or close) to reinvest. I would like you to advise me on this. Perhaps you know of some other companies that might offer returns a little better than average.
>
> Anyway, I look forward to working with you if you have the time to take me on.
>
> Thanks
>
> Craig

Clarke's reply of the same day says:

> Thanks for the e-mail, would love to get together to discuss your portfolio and house idea. Will give you a call in the next week or so to begin discussions.

[336] On April 18, Dunham requested a meeting with Clarke, which meeting was confirmed for April 25. It was the only in-person meeting between them. Dunham e-mailed Clarke on April 26 thanking him for the time on Tuesday as follows:

> It was good to have someone in the know reassure me that I was able to do things a certain way. I like the idea of the margin account it provides great flexibility.
>
> I would like to see some hard numbers on paper (email) to support my financial commitments.

He asked for $34,000 to be sent to his lawyer's account (for his new home construction) and continued:

> Further to our discussion of yesterday, would I be wiser to return my leased vehicle and repurchase same (or different) for cash under the same margin account? It would seem that most major purchases would be best handled this way. I would also like to know how or if this same set up will allow to have additional, readily accessible income or is it all going into the pooled funds.

[337] On May 15, 2000, Dunham again e-mailed Clarke advising that he was purchasing a new vehicle and asked for funds to be forwarded to the dealership in the amount of $39,000.00 to pay for it. He added:

> Also, things are winding up with KHI, and I have spent my last official day in the office last Friday. As discussed the transfer of all shares will be completed on June 30th. As for the margin account, you presently only have 30,000 shares in your possession so I assume this about uses up the borrowing until the other 90,000 shares are transferred.
>
> I am still a little unclear about how the accounts are looking after themselves at the moment. I understand if they are interest bearing or pay dividends then the assumption is [I] would be earning more on the total asset base than paying on the borrowed funds. But is there any interest being earned at the moment or am I accumulating interest charges without any offsetting debits along with the credits?
>
> Sorry to bother you with this, I still [need,sic] a little reassurance I guess. ...

[338] This e-mail referenced the fact that Dunham was not comfortable working for KHI, felt out of place and had resigned from the company. By reason of his resignation, Dunham understood that his remaining 90,000 KHI shares were to be released from escrow, and he believed that he was free to sell them.

[339] On June 8, Dunham e-mailed Clarke looking for $20,000.00 to pay the contractors who were starting on his new house. On June 28, Clarke advised Dunham that he did not have margin room until Clarke received from KHI the share certificate for the 90,000 shares.

[340] On July 6, 2000, Guy Roby, Senior Vice President, Compliance Department of NBFL, sent a letter to Dunham noting that his account was 100% invested in KHI shares and that such concentration is considered speculative, stating that NBFL believed that asset diversification is a reasonable way to decrease risk. Dunham testified he was not concerned with the letter because he believed he already had arranged with Clarke for the diversification of his account out of KHI shares as initially reflected in his April 13 e-mail.

[341] NBFL's submission concentrated on Dunham's understanding that he had opened a margin account; that he was borrowing against that account; and that Clarke was not selling KHI shares. It is not clear to the Court that Dunham really understood what the margin account until at least late July 2000 (as reflected in an e-mail from Dunham to Colpitts). His confusion, and questions to Clarke about how his account operated, continued from the time he opened the account. The confusion is evident in the "PS" to his e-mail to Clarke of June 28, 2000.

[342] Dunham continued to believe that Clarke would sell his KHI shares and diversify his account. Dunham's July 10 e-mail to Clarke asking him to buy shares of a technology company and to sell enough KHI stock to cover the purchase is tangential evidence. Clarke's one-line reply is that he had bought the shares. He did not, in fact, sell KHI shares; nor did he advise in his reply why he had not sold KHI shares.

[343] Through July 2000, KHI still had not released from escrow the remaining 90,000 shares that Dunham expected to receive upon his resignation on June 30. Dunham did not understand KHI's delay. He asked for Clarke's advice in an e-mail on July 26:

> I would also like to make another appointment with you to discuss my plans for these shares once we have control. I would like to set up the portfolio so there is a small income through dividend yielding stocks as well as hear your ideas on growth as well as set a smaller portfolio from stocks I have been interested in tracking.

[344] The reference to a "smaller portfolio" was Dunham's desire, communicated to Clarke, that he would like to invest a small portion of the proceeds from the sale of KHI shares in technology stocks, which he was following on his own. The size of this part of his portfolio, about which he intended to be involved, as opposed to the remaining portfolio that Clarke would invest for him, was about 10%. It is a theme throughout Dunham's e-mail correspondence with Clarke. It does not detract from Dunham's express communications to Clarke that he was relying on Clarke to diversify his account in a manner about which Clarke would advise.

[345] By July 28, Dunham's remaining 90,000 KHI shares had still not been released by KHI. He contacted Colpitts, the lawyer who had acted for KHI in the purchase of Innovative, for help. He expressed urgency to complete the release of his shares. He was relying upon the sale of KHI shares to finance his ongoing house construction.

[346] On August 1, Colpitts sent Dunham a "draft settlement agreement", a release respecting the end of Dunham's employment and relationship with KHI. Colpitts included a provision giving a KHI a right of first refusal to buy Dunham's shares, exercisable for 96 hours after Dunham's notice of any intent to sell.

[347] I conclude, from the totality of the evidence, including the exchanges between Dunham, KHI, and KHI's lawyers (Colpitts and his associate Burke), that KHI was following a pattern of conduct that would delay putting on the market for sale KHI shares, because there were fewer buyers than sellers. The delay in arranging for Dunham to get his remaining KHI shares, a simple process, which shares Clarke knew Dunham wanted to sell to pay his accumulating house construction bills and to diversify his portfolio, is one of the many small seemingly-innocuous actions that affirm the Dunlop

Clients' claim that KHI insiders were trying to delay and discourage share sales. This delay was to maintain KHI's share price while KHI insiders created a viable business and resultant market for its shares. Clarke acted as one of their instruments in that endeavour, by his purchases of KHI shares on margin in the 540 account, and by declining to attempt to sell Dunham's KHI shares, and create a diversified account, when it was obvious that Dunham trusted Clarke, and relied on his expertise and advice to diversify.

[348] On August 4, Dunham advised Clarke of the fact that he had executed Colpitts' release and given KHI 96 hours to respond to his notice of intention to sell. In that e-mail he continued: "Once this is complete (shouldn't be more than a couple of days) I would like to meet again to take specific actions on diversifying my account."

[349] In early September 2000, Clarke e-mailed Dunham that he had an opportunity to sell 5,000 KHI shares for about $6.50. What Dunham did not know was that Clarke was gathering shares to fill an order for the purchase of KHI shares by Barthe.

[350] Dunham very naively replied, the same day: "Thanks Bruce, But I think I will hold onto them for a few more months to see what happens with the price. I really sense that something is about to happen with this stock . . . especially given the volume in it lately." What Dunham did not know, and was not told by Clarke, was that the volume of trades Dunham observed was caused by Clarke's purchase of 259,000 KHI shares for Barthe from insiders, the volume of which trades would be apparent as they were executed on the TSX.

[351] Clarke asked Dunham to call him; he did. Shortly afterwards, Clarke e-mailed Dunham: "Further to our conversation I sold 5,000 KHI shares at $6.55 to give you net proceeds of $32,250 which will lower your current debit balance until you require additional funds."

[352] The Court is satisfied that Clarke was aware at this time that the only large volumes of trades in KHI shares were trades arranged by KHI insiders. At the time of this transaction, it was the substantial purchase by Barthe of KHI shares as a result of the sales efforts of Potter and Sullivan (KHI insiders). It was Colpitts, another insider, who had referred Barthe to Clarke to arrange for the purchase of shares, knowing that Clarke would arrange those shares to be purchased from those persons whose margin requirements required sale to Barthe.

[353] Throughout the rest of 2000 and into January 2001, Dunham continued to seek Clarke's advice respecting sale of KHI shares. Clarke either ignored the requests, which lead Dunham to believe that he was attempting sell his KHI shares, or otherwise mislead him.

[354] For example, in late September 2000, Dunham asked Clarke to sell KHI shares to buy Cross Off shares. Clarke's e-mail of September 29, 2000 reads: "We have purchased 20,000 Cross Off at $1.10 and have not sold any KHI, trying to work it into the market." I am satisfied that Clarke was not trying to sell Dunham's KHI shares into the market. At the same time, he was using margin to purchase KHI shares in the 540 account to maintain to the price. Clarke deliberated misled Dunham.

[355] On October 17, 2000, Dunham e-mailed Clarke: "to sell some KHI for a purchase of Nortel." Clarke replied: "Further to your e-mail we purchased 100 shares of Nortel at $97.75 per share, but, we are still working on the Knowledge House and will get back to you." I am satisfied that the answer was untruthful. He was not working on selling Dunham's KHI shares.

[356] On November 29, 2000, Dunham sent Clarke a lengthy e-mail about his need for cash to pay the holdback to his contractor. Dunham's request is not articulate, but it is clear that he is seeking advice on setting up his account to get some income, and specifically to diversify his account. The e-mail reads:

> Hi Bruce,
>
> my last payment (the holdback) is coming due within the week.
>
> what is my best option? Do I need to sell more shares for cash like before?
>
> I also need more money to live on over the next six to seven months as I get re-established in business. I am trying to set myself up in the brokerage business (import/expert, not stockes), but it will take time to get rolling. If there was a pool of money in bonds, GIC's or similar vehicle that was eligible for higher margin (maybe even dollar for dollar like cash), would that help? ... or is this what the cash generated from previous sales actually in? I'm hoping it is earning some interest.
>
> I figure I need about $50,000 to get me through to June 2001 (this includes the $35,000ish I need to settle with the contractor), by which time I am confident I will be earning some real money again. I also assume the market will turn around before then and allow us to diversify and make some real gains again.
>
> Give me a call or email me with your thoughts on what I should be doing. I can be available to meet most any time.
>
> You can reach me by e-mail, (phone ...)
>
> Thanks
>
> Craig

[357] The note on the exhibit (Clarke's copy of the e-mail), in Clarke's handwriting says that he called Dunham on December 4 and advised him to get a one-year mortgage as the market was no guarantee to give him the money he needed. Clarke's note says that Dunham agreed.

[358] On January 4, 2001, Dunham e-mailed Clarke:

> What progress have you made on getting me out of the KHI stock?
>
> I would much rather sit on cash than watch the stock continue to drop.
>
> What about seeing if KHI is interested in buying all the remaining shares, except maybe 5000, at $6. They did stipulate they wanted that option. And seeing as they are buying the options in the Limited Partnership they may be receptive. Is this something I would initiate?

> I've got to start diversifying and I want to take advantage of the coming market rebound. I don't think KHI will return what others can.
>
> Please call me to discuss this.

[359] On January 4, 2001, Dunham e-mailed Cate MacNutt to see if Knowledge House was interested in buying back his shares. He writes: ". . . I would however, like to get diversified in my stock portfolio. You stated in the contract that KHI would be interested in purchasing the shares back. What are the details of how this would work?"

[360] Cate MacNutt replied on January 9, with a copy to Clarke and Potter. Mixed in with her good news story about the progress KHI was making, she wrote: ". . . I spoke to Bruce Clarke respecting your inquiry and he will proceed with helping you diversify your portfolio, as reasonably as he can, in today's environment. . . . As far as the process regarding your shares, please work with Bruce who will manage it from our end. Bruce will keep in touch with you. If you have any questions, please call Bruce or email me or call xxx-xxxx."

[361] Within ten minutes, Dunham had e-mailed Clarke:

> Thanks for the follow up with Cate.
>
> I mentioned to Cate that I would like to hold on to anywhere from 5-10,000 shares, as I still believe in what they are doing too.
>
> I will forward to you via fax my list of stocks to purchase form the technology side of my portfolio. The other market segments I would like to speak to you about for recommendations. ...

[362] Nothing happened after January 9. On January 14, 2001, Dunham e-mailed Clarke:

> Hi Bruce,
>
> Please do not take offense, but I am wondering whether you have the time to manage my account to my liking.
>
> I have a difficult time getting through to you and nothing seems to happen with any real immediacy. Perhaps the lack of wide spread interest in the KHI stock is at the heart of this, but all the more reason to get out of it as my only investment.
>
> My most recent request to get out of the KHI stock seems to be stalled ...
>
> I have also requested several meetings with you but have yet to get a meeting.
>
> maybe my expectations are too high, but I feel I have a fairly large account and would like to have a better response from my broker. I would have expected you would be stressing that I diversity my portfolio and make recommendations for other stocks.
>
> Like I said in the opening line Bruce, I don't mean to offend with this note, I simply want to get my portfolio working for me. I have watched it lose value over the last year and have done nothing to help my position one way or the other. I really need to see some positive to grow this portfolio over the next few years.

Please call me ASAP to discuss how we proceed form here.

Thanks

[363] The e-mail exchanges clearly identify the basis of the Court's conclusion, confirmed by the oral evidence of Dunham, that he was a naive novice with respect to the investment industry; that he put himself in the hands of Clarke to cash in his KHI shares; and that he terminated his employment with KHI because of concerns about how KHI was operated. Further, Dunham relied on Clarke to give him good advice with respect to diversification of his portfolio. Because of a conflict of interest, Clarke did not disclose to Dunham that which he knew and had a duty to disclose. Clarke owed a duty in contract and as a fiduciary to help Dunham diversify his account. He did not do so because of his conflict of interest.

[364] A fiduciary relationship existed between Clarke and Dunham. His e-mails clearly demonstrate that he was placing trust, confidence and reliance on the skill, knowledge and advice of Clarke.

[365] It was not possible, as a matter of common sense, for Clarke not to understand that Dunham was placing complete trust, confidence and reliance upon Clarke's skill and knowledge.

[366] The text, *Securities Litigation and Enforcement,* beginning at p. 171, describes the factors applied by courts to determine when the relationship between a broker and client is a fiduciary relationship. The Supreme Court of Canada's 1994 decision in *Hodgkinson*, adopted the description of fiduciary relationship from *Varcoe v Stirling*, [1992] OJ No. 1501 (ONCA) and *Lac Minerals*, [1989] 2 SCR 594. The e-mail correspondence and the trial evidence of Dunham clearly establish that a fiduciary duty was owed by Clarke to Dunham, a vulnerable, naive and unsophisticated investor to follow up on Dunham's rudimentary understanding that he should have a diversified portfolio.

[367] Instead, he was diverted Dunham into a margin account, in which he continued to hold KHI shares as security for debt. Clarke had enough insight into the risks associated with a client holding KHI shares, particularly when this risky stock was almost his only stock, that, in failing to diversify his account (and sell KHI shares), he breached his fiduciary duty to Dunham. He did not give full disclosure of what he knew about KHI, including his own very significant investments on behalf of KHI insiders and in his 540 account. Clarke owed a duty of loyalty to Dunham. He did not disclose that he had a conflict of interest both in respect of his own holdings and his dealings on behalf of other KHI insiders. He had an obligation to act prudently, and with candour in his advice to Dunham. He did not.

[368] Dunham pleads not only that Clarke breached his fiduciary duty to Dunham, but was negligent (in his misrepresentations) and acted in breach of a contractual duty.

[369] In light of the Court's findings that Clarke was a fiduciary, and breached his fiduciary duty, it is unnecessary to determine any other basis for liability. However, I find that the same conduct that constituted a breach of Clarke's fiduciary duty to Dunham, also constitutes a breach of his contractual duty to Dunham, a duty created when Dunham retained Clarke as his investment advisor.

[370] I find that Clarke did not make negligent misrepresentations to Dunham. He intentionally failed to disclose, and by his silence, intentionally misrepresented the circumstances of KHI and the trading of KHI shares, because of his conflict of interest.

D.2 Liability to the Weirs and Blackwood

[371] The members of the Weir family held shares in KHI through accounts with Clarke at NBFL. However, the only parties to this litigation are, as defendants and plaintiffs by counterclaim in the Debt Action Hfx 174294, Lowell Weir and Blackwood Holdings Incorporated, a wholly owned subsidiary of Blackwood Consultants Limited, owned 87% by Carol McLaughlin-Weir; and, as defendants and plaintiffs by counterclaim in the National Bank/Weir action Hfx 246337, Lowell Weir and Carol McLaughlin-Weir.

[372] The factual matrix between the Weir family and Clarke / NBFL / NBC was not the same as that between Dunham and Clarke / NBFL. The difference affects the legal analysis.

[373] The basis of the Weir family claims against Clarke / NBFL is founded on breach of contract and negligence and fraud, not on a breach of fiduciary duty.

[374] Weir was a chartered accountant and sophisticated investor, being the principal in a publicly traded company. McLaughlin-Weir is a chartered accountant.

[375] Both McLaughlin-Weir and Weir testified at trial respecting their dealings with Clarke at NBFL, and with NBFL and its parent NBC after KHI collapsed.

[376] For the most part, their evidence was uncontradicted. The only evidence that might be considered contrary is some of Clarke's evidence.

[377] The Court found both Weir and McLaughlin-Weir to be credible and reliable witnesses. The Court accepts their evidence. Where it differs from that of Clarke, the Court prefers their evidence to that of Clarke.

[378] McLaughlin-Weir caused her consulting company to incorporate Blackwood in the late 1990s as a vehicle to invest excess earnings in her accounting practice. Blackwood opened an investment account in March 1998 with Clarke at Levesque Securities (later NBFL) on the recommendation of her lawyer Colpitts. On the advice of Clarke, the investment account was opened as a margin account. It was Blackwood's only investment account.

[379] McLaughlin-Weir testified that her intention with respect to the investment account and her directions to Clarke were to use it to make safe, dividend-producing investments. She was shown the "Know Your Client" form, signed by her in March 1998, on the opening of Blackwood's account. She says the form was completed by Clarke, not by her. She confirms that the account accurately set out her net worth at the time but it did not describe what she instructed Clarke to be her "investment objectives" and "risk factors".

[380] McLaughlin-Weir testified that she never advised Clarke, or agreed, that her "investment objectives" were 80% short-term, 20% medium-term and 0% long-term or that her "risk factor" was 0% low, 0% medium and 100% high. Her purpose in incorporating Blackwood was to invest cash for her retirement and for her children's education.

[381] McLaughlin-Weir signed the account as a margin account because she understood it was a good way to trade and borrow money to make more investments. She wanted her account to include dividends, interest income and stock with potential for growth appreciation.

[382] McLaughlin-Weir authorized NBFL to deal with Weir, her husband, as an agent in respect of the account.

[383] Her initial investment in Blackwood was approximately $50,000.00, of which $25,000.00 was invested in her husband's publicly traded company and $20,000.00 in corporate bonds recommended by Clarke. By the end of January 1999, Blackwood had purchased 10,000 KHI shares. She says this investment was on the advice of Clarke. Clarke at no time disclosed to her his own involvement or that of his numbered company (the 540 account) in KHI shares. By March 1999, the Blackwood portfolio was worth $90,000.00 with margin debt of $50,000.00.

[384] McLaughlin-Weir held three accounts in her personal name with Clarke at NBFL. One was a margin account and two were RRSP accounts. The largest RRSP account consisted mostly of TD Bank bonds. On June 29, 1999, her account statement showed a purchase of 5,000 KHI shares for $16,450.00. These shares were still in the account at the end of 2001. They were worthless after KHI collapsed.

[385] Blackwood purchased 10,000 KHI shares on March 2, 1999, for $21,750.00. This was on the advice of Clarke. By December 31, 1999, the shares were worth $62,500.00 and on March 31, 2000, $85,000.00 (and constituted 40.4% of Blackwood's account).

[386] On McLaughlin-Weir's instructions, Clarke sold 2,000 KHI shares on December 19, 2000 for $12,105.20 (net of commission) and on March 28, 2001 1,000 KHI shares for $5,055.10 (net). Seven thousand worthless KHI shares were held in the Blackwood account after KHI collapsed.

[387] McLaughlin-Weir states that as a result of a discussion between herself and her husband, her husband e-mailed Clarke on January 19, 2001, instructing him to sell all of the Weir family holdings in KHI if the price fell below $5.00. The Weirs were getting nervous about KHI because the price had slowly declined since March 2000. McLaughlin-Weir states that while the KHI price did fall below $5.00 after January 19, 2001, Clarke did not sell the Weir family holdings, including the 8,000 then held by Blackwood or the 5,000 held in her spousal RSP account.

[388] In early April 2001, McLaughlin-Weir received a letter from NBFL's compliance department noting that 67% of Blackwood's account was in KHI stock and advising that this concentration was considered speculative and that NBFL believed that asset diversification is a reasonable way to reduce investment risk. Upon receipt of the letter, on April 10, McLaughlin-Weir called Clarke to set up a meeting to talk about her children's investments accounts and to talk about the compliance

department letter. It took her several phone calls before she was able to set up the meeting with Clarke, which meeting, she says, occurred about the end of April 2001.

[389] Her intent when she went to the meeting and her instructions to Clarke was to do a better job with her children's investment accounts and to sell all her KHI shares. As the meeting was coming to an end, Clarke told her that he did not want her to sell her KHI shares because of an impending announcement of a contract with the Province of Nova Scotia and the KHI shares were going to go to $8.00 and she was going to lose $3.00 per share. Based on this representation, she revoked her instructions to Clarke to sell all her KHI shares. Clarke's reference to a pending contract between KHI and the Province of Nova Scotia was not public information, but was an accurate statement of a contract that Potter was working on and hoping to obtain. It is evidence of Clarke's status with KHI's insiders and how he used that status to assist in the scheme to prevent sale of KHI shares and maintain its market price.

[390] Based on Clarke's knowledge of the substantial efforts of himself and KHI insiders from at least March 2000 to maintain KHI share price with purchases using margin debt, and in April 2001 to maintain the market price above $5.00, to prevent margin calls and maintain the existing margin debt on KHI shares, this was clearly a fraudulent misrepresentation. Clarke knew of the great efforts made by himself until he ran out of margin room in 540 account in January 2001, and by other KHI insiders thereafter, to maintain the KHI share price above $5.00.

[391] On cross-examination, McLaughlin-Weir acknowledged that she received account statements in February and March 2001 which showed the share price of KHI shares had dipped below $5.00. She says it caused her no concern because by the time the statements were received, the price had increased to more than $5.00 again (unbeknownst to her, by the artificial efforts of KHI insiders).

[392] On cross-examination, McLaughlin-Weir stated that she did not understand KHI to be a high risk stock because of what Clarke had told her, and because of its performance after she bought its stock. She did not consider KHI to be too big a part of her portfolio at the end of 1999 because the only the reason it was a substantial portion was because it had increased in value, not that she had purchased too many shares.

[393] McLaughlin-Weir acknowledged that she had sufficient funds in her personal investment accounts at NBFL to pay the margin debt of Blackwood of about $10,000.00 but says she was not asked to do so until the Demand Letter of November 15, 2001. By then she had come to the belief that NBFL had mislead her. This is reflected in the letter she helped her husband draft, outlining the Weir's complaints about NBFL's conduct, which letter was sent to Eric Hicks on September 9, 2001.

[394] Weir worked first as a chartered accountant, then for 20 years in the food processing industry, before becoming president and a major shareholder in a "waste-2-energy" technology and fabrication business. At the time he joined the corporation, it was known as Castle Capital. It later changed its name to Enervision, and later still to Helical.

[395] In 1998 Weir opened two small RSP and one non-registered cash investment accounts with Clarke at NBFL (then known as Levesque Securities). When he opened those accounts, he had not

discussed either his net worth or his investment objectives with Clarke. The "Know Your Client" form completed by Clarke at this time was not based on anything Weir told Clarke and was incorrect.

[396] In February 1999, Weir transferred his LIRA account, consisting of bonds and blue chip Canadian stocks from the TD Bank to NBFL. In an interview at Weir's office at the time that account was transferred, Weir told Clarke that it was his pension money and that he wanted it to be kept safe. The "KYC" form completed by Clarke at that time was, says Weir, accurate. His investment objects were 25% income. His risk criterion was 40% low risk; 40% medium risk and 20% high risk.

[397] In December 1999, Weir was approached by his lawyer Colpitts to invest $150,000.00 in the Knowledge House Limited Partnership (KHLP). Weir says Colpitts flattered him with this "special opportunity" to invest and associate with some well-known business people. Colpitts arranged for him to borrow $100,000.00 from the Royal Bank toward the purchase of the KHLP units.

[398] Also, in December 1999, 5,000 KHI shares were purchased in Weir's LIRA account. Weir says that he only learned about this purchase after the fact. He did not cancel the purchase. He states that at no time did Clarke advised him of Clarke's own purchases of KHI shares, or of his activities on behalf of KHI insiders.

[399] Weir also began dealing with Clarke at NBFL on behalf of Castle Capital. The company had excess capital. Castle needed to park it in short-term investments until Castle needed the money. Clarke invested part of the money in KHI shares. Weir did not ask Clarke to cancel the purchase of KHI shares from that account when he learned of the purchases. Before trial, on NBFL's motion, this Court dismissed the action by Castle Capital (by then called Helical) against NBFL, not on its merits but on procedural grounds.

[400] In January 2001, the Weirs became nervous about their KHI holdings because of the steady decline in the share price since March 2000. On January 19, 2001, Weir e-mailed Clarke as follows:

> Bruce:
>
> I am very nervous on Knowledge House. If the stock falls below $5.00 I would like the holdings of Enervision sold immediately at market. In addition, I want the same to apply to the Knowledge House stock held by Blackwood Holdings and any other held by my wife and children and myself directly or through RRSP.
>
> Lowell

[401] Weir testified that on at least three occasions the price dipped below $5.00. Each time Weir called Clarke; Clarke made excuses as to why those trades were aberrations and he need not sell.

[402] The KHLP units purchased by Weir in December 1999 contained a call option in favour of KHI. It required unit holders to convert their units into common shares at KHI's option. The Offering Memorandum, and Subscription Agreement, provided that if KHI exercised the call option before December 30, 2000, KHI had to issue shares worth 120% of the original KHLP unit price.

[403] On December 21, 2000, KHI gave notice to the unit holders that it was exercising that option. Weir expected to receive share certificates for the partnership units by January 1, 2001. He intended to transfer some of the KHI shares as contributions into his and his wife's RRSP accounts before March 1, 2001. The shares did not arrive on January 1. For the next two months Weir hounded Colpitts to get his share certificate. At one point he called the Nova Scotia Securities Commission. Shortly after that call Colpitts called Weir and said the certificates were being sent to NBFL.

[404] On February 28, 2001, Weir contacted Clarke who told him that the share certificates for the Partnership Units had not yet arrived. Clarke suggested that he open a margin account and borrow temporarily on the margin account to make his RRSP contributions before the March 1 deadline. Weir opened a margin account on February 28 and on March 1, using margin, transferred about $18,000 to his and McLaughlin-Weir's RRSP accounts.

[405] The Court notes that, contrary to Clarke's advice to Weir on March 28, Weir's portfolio statement shows that on February 28, 2001, 28,125 KHI shares were deposited into Weir's new margin account.

[406] The Court also notes that Wadden and Potter appear to have received their share certificates, exchanged for the KHLP units, within the first week of January 2001, and to have placed these shares in margin accounts with Clarke at NBFL, where the margin available on those shares allowed them to buy more KHI shares as part of their scheme to maintain the KHI share price. This is reflected in Wadden's account statements, and in emails and phone messages. Wadden's email to Colpitts of 10:50 a.m. January 4, 2001, reads:

> Blois, Please forward my share certificate for the converted LP to Bruce as soon as possible. I will be depositing to my margin account and will be able to help Bruce take 20,000 shares of KHI out of the market if we can do this today.

Wadden's phone message to Colpitts of January 5, 2001, admitted for all purposes by agreement of Counsel, reads:

> Hello Blois, is Calvin calling. Just talking to Dan and he had give me an idea with the LP being converted back - there were shares available and he expedited those over to Bruce to allow some support from this account and just.... and I'm going to ask Bruce to do the same for mine if you can – this is an authorization I guess if that's okay with you to send them over and if you see maybe a pickup well maybe 20,000 shares in the market with that use in the leverage - I guess as long as National approves it, I'm going to give them a call right now and see if that's okay on his side and maybe you can give him a call when you get a second. Thank you.

[407] Wadden's Margin account at NBFL (11AK84-E) shows receipt into that account of 28,125 KHI shares on January 4, 2001. This is the number of shares issued when KHI exercised its call option to convert the KHLP units into shares.

[408] It appears that it might not have helped Weir to fulfill his RRSP obligation and his desire to sell some of the KHI shares to purchase his wife a new vehicle on their upcoming 25th wedding anniversary. The reason is that Clarke advised him, after he received the KHI share certificate, that the certificate came with a restriction preventing transfer of the shares for six months. The Court

notes that neither the terms of the Offering Memorandum nor the attached KHLP Agreement dated July 12, 1999, contained a term or condition that, if KHI exercised its call option and converted the Partnership Units for shares, the shares would be subject to any such condition.

[409] The attempt by KHI to add restrictions to any share transfer first appeared on the share certificate issued to Weir in exchange for the KHLP units. They were very likely unenforceable. More significant, for the purposes of this litigation, the delay in issuing the share certificate and the addition of the condition respecting transfer is collaboration of the Court's determination that it was the intent of KHI insiders, working with Clarke, to discourage and inhibit sale of KHI shares until KHI was able get its financial house in order and bring on board more wealthy individuals and institutional investors.

[410] This intent is reflected in several other communications between Potter and KHI directors and insiders in January 2001.

[411] They include Potter's letters to Barthe and/or Ristow on January 19, 20 and 28 [the latter actually sent February 4], and March 2, 2001.

[412] The first (which attaches a copy of an urgent January 15 memo to the Directors) reads in part:

> The immediate and critical problem is that we need to maintain daily market support for the stock while we are getting this financing done. You can see from recent trading in KHI on the [TSX] that the stock is under pressure. Our local sources of support to buy the stock on a daily basis are exhausted . . . there is a real and present risk that the stock price will collapse . . . This would be a classic case 'running out of steam' before reaching the finish line. . .

The second letter adds: "The support of the stock must begin on open of market, Monday morning, if we are to maintain the ability to achieve our goals . . . my capacity and our local supporters' capacity to support the market price of our stock has been exhausted."

The third reads in part: "I would ask that you consider immediately (Monday, Feb.5) providing instructions to Bruce Clarke at NBF to buy an initial 20,000 shares on the market to provide needed investor confidence and support."

The fourth reads in part: "But these [local] sources of market support are truly becoming exhausted. The stock has started to falter (Thursday) as a result. Accordingly I am repeating my earlier request . . . I sincerely hope that you will provide instructions and funding to this effect to NBF via Bruce Clarke at your earliest convenience today . . ."

[413] They include email exchanges and documents between Potter, Wadden, and other insiders as follows: from Potter, January 14, 2001, 10:10 p.m.; from Wadden, January 31, 4:03 p.m.; from Potter, February 1, 8:18 a.m.; from Potter, February 4, 6:48 p.m.; from Wadden, February 8, 5:18 p.m.; from Potter, 12:13 p.m.; from Wadden, February 13, 7:36 p.m.; from Wadden, February 14, 1:08 p.m.; from Potter, February 19, 7:46 a.m. and 3:24 p.m.; from Schelew, February 21, 8:11 a.m.;

from Potter to KHI Board (memo); February 21, from Colpitts (managed sell agreement); from Macleod, March 1, 9:12 p.m. and 10:13 p.m.; from Potter, March 2, 3:35 a.m.; from Wadden, March 2, 9:03 a.m.; from Potter, March 2, 5:05 p.m.; from Colpitts, March 6, 10:10 a.m.; from Potter, March 8, 8:12 p.m. and March 26, 9:47 p.m.; from Wadden, June 21, 7:43 a.m. and 10:47 a.m. and July 1, 10:17 p.m. and July 8, 2:49 a.m.. These messages show that Clarke was in the loop and executing trades to carry out the scheme.

[414] These circumstances, with many others, led me to find that Clarke, and KHI insiders, including Potter, Wadden, and Colpitts, were doing whatever it took to prevent and discourage, by deception if necessary, any KHI shares from being put on the market until a viable business plan was developed, and institutional or wealthy investors were found.

[415] In the Weir KHLP matrix, the clear intent of the actions of Clarke, and the insiders was to make it difficult for the Weir family to liquidate their KHI shares. The intent of the insiders is evidenced by other actions referred to in this decision. One example is the expressly-stated intent in the 8:50 p.m., November 19, 2000, email from Potter to Wadden and Colpitts about the pending private placement of $3,250,000.00 to Barthe and Ristow, and the need to keep the KHI share price from being driven below the issue price of $6.50.

[416] On June 5, 2001, Weir borrowed $40,000.00 on the margin account to purchase McLaughlin-Weir a vehicle for their 25th wedding anniversary. When the KHI share price collapsed in August 2001, Weir's margin account went from a surplus (based on the value of the 28,125 KHI shares) to a deficit of about $60,000.00.

[417] The Weirs were out of the country when KHI collapsed and only learned about it in the newspapers upon their return. Weir made several calls to Clarke, who did not return Weir's calls. On August 28, Clarke called him to advise that he owed NBFL margin debt on his own account and the Blackwood account. Weir acknowledges that he had sufficient financial ability to pay these margin debts but he told Clarke that he had questions about the propriety of the trading in KHI shares and the collapse of KHI that involved NBFL. Clarke told him to take this up with his manager Hicks.

[418] Weir arranged a meeting with Hicks, manager of the Halifax branch of NBFL, for September 4. In the meantime, he researched the trading records for KHI and became convinced that NBFL had participated in suspicious trading in KHI shares and had been negligent.

[419] Weir testified that at about this time he received a phone call from a gentleman claiming to represent NBFL, whose name he does not know, calling from area code 416, who spoke in a very abusive manner and directed him to pay the margin debts. This evidence is consistent with the written record Clarke made of a phone call he received from Hicks at 9:50 a.m. on August 31, 2001, which reads in part: "Eric called to say that from his trip to Montreal, a strategy has been put in place to recover all money lost. He said they (national people) will continue to call clients daily (2/3 times a day) until the client agrees to come and negotiate some arrangement to pay the debts."

[420] Weir described his September 4 meeting with Hicks. He says no one else was present. Hicks met him in the NBFL boardroom and during their discussion Hicks became very aggressive and abusive. Weir felt offended and left the boardroom to leave the building.

[421] Hicks approached him at the elevator as Weir was leaving, and apologized to Weir. They returned to the boardroom where they spoke for about an hour about Weir's suspicions of negligence and wrongdoing by NBFL. Weir, as president as Castle Capital, then called Enervision, was leaving the next day for Norway for a week or two to make or complete an important business contract. Weir wanted to ensure that nothing would occur with respect to the demand for payment of the margin debt owed in his and the Blackwood accounts. Hicks advised him to put an offer in writing to settle the matter and Weir agreed that he would do so while he was in Norway.

[422] Weir states that Hicks agreed that NBFL would do nothing to pursue its margin debt while they negotiated Weir's claim of negligence by NBFL. NBFL subsequently denied any agreement, but it produced no evidence at trial to negate Weir's evidence.

[423] As promised by Weir, he wrote to Hicks from Norway on September 9, 2001. His letter sets out a claim of negligence against NBFL and made a settlement offer that was open for acceptance to September 14.

[424] By letter dated September 14, 2001, NBFL's Montreal legal department acknowledged receipt of Weir's September 9 letter. The writer said: "Your request has been forwarded to the legal department under the direction of Mr. André Gibeault, Senior Vice President. Please be assured that your file is receiving our full attention. We will communicate our position to you in writing as soon as possible." The letter was copied to Joel Wiesenfeld, a lawyer at Torys. From this reply, Weir believed the "standstill" agreement was still in place.

[425] It is apparent that NBFL took Weir's September 9 written complaint re misrepresentations and lies by NBFL seriously. At 3:05 pm on September 11, 2001, Hicks told Clarke that NBFL was doing an investigation into the trading of ITI and KHI as they felt the shares of each were "managed" by a small group of insiders.

[426] Weir returned to Canada from Norway on or about September 14, 2001. His travel was held up by the 9/11 events.

[427] While in Norway, Weir, on behalf of Enervision, had entered into a major contract with the Oslo airport authority for the de-icing of air planes. This contract was publicly disclosed about September 19.

[428] On September 19, Weir received phone calls that Enervision shares were being dumped on the market. In fact, without further notice to Weir, and contrary to the standstill agreement with Hicks and NBFL, NBFL did, pursuant to its margin call, dump 325,500 Enervision shares held in the Blackwood account on the market on September 19, receiving about $6,500.00 or $0.02 per share.

[429] The same day Weir called Clarke and asked what happened. Clarke referred him to Mr. Gibeault in Montreal. He called Mr. Gibeault, told him about the standstill agreement, and asked if he was selling the Enervision shares. Gibeault denied that NBFL was selling the Enervision shares. Weir called Clarke back and Clarke confirmed that NBFL was, in fact, selling the shares. Weir called Gibeault again. This time Gibeault denied that there was a standstill agreement. Weir offered to send Gibeault the letter discussing the standstill agreement. After Weir had faxed it to Gibeault, Gibeault called him back and told there was no standstill agreement and hung up the phone. Weir testified that because he (Weir) was an insider respecting Enervision, and the company was in the midst of a "material event", he was prevented from mitigating the sale of Blackwood's Enervision shares by purchasing them back himself.

[430] On September 20 Weir sent a letter to Gibeault, the President of NBFL, and to the chairman of NBFL expressing dissatisfaction with the manner in which they had liquidated the Enervision shares.

[431] Weir states that NBFL's reply was a phone call from the same gentleman at the same area code 416 number who had previously called and abused him, stating that NBFL had taught Weir a lesson and next time he had better listen.

[432] On September 21, Weir wrote a second letter to Gibeault, Anthony and Turmel in response to their reply (not produced at trial) to Weir's September 20 letter. He copied the letter to Joel Wiesenfeld, the Torys lawyer who had been copied in NBFL's September 9 letter to him.

[433] Weir testified that at about 6:00 p.m. on September 21 he received a phone call (while driving in his vehicle) from Daniel Boucher. Boucher was with NBFL Investor's Services Department. He stated that he had been instructed to call Weir and ask for time. He acknowledged that the NBFL Credit Department should not have sold the shares. He stated that he was instructed to review the matter and was going to work on it all weekend and he would give Weir a call the next Tuesday, after he had completed his investigation.

[434] When Weir did not receive a call from Boucher by 5:00 on Tuesday, he called. Boucher told him that he had reviewed the matter and Weir would hear from their lawyer.

[435] On September 25, Wiesenfeld e-mailed Weir denying a standstill agreement existed and advising that he would he held liable for defamatory statements made about Hicks and NBFL. He stated that NBFL was conducting a review of his accounts and would not be forced into a hasty review and would provide an appropriate response.

[436] On October 4, Weir received a letter of demand for payment of his margin account from Alan Parish, a Nova Scotia lawyer. On October 16, 2001, Weir received a further letter from Wiesenfeld rejecting Weir's settlement offer. Shortly thereafter, Weir and Blackwood were sued by NBFL.

[437] Weir continued his efforts to settle with NBFL. He was a shareholder of National Bank of Canada. He attended the annual meeting in March 2002 and asked the chairman to investigate his

complaints. In August 2002 he met with the new CEO of National Bank of Canada, who referred him to the Bank's ombudsman. The ombudsman acknowledged he was aware of the situation and that the chairperson and CEO of the Bank wanted to resolve the matter. After the ombudsman spoke with Gibeault, he advised Weir that because there were legal processes in place, he could not deal with it. He said the Bank would give serious consideration to a new settlement offer. Weir sent one and received no response from Gibeault.

[438] On March 11, 2003, Weir went to Montreal for National Bank's annual meeting, scheduled for March 12. He wanted to speak to the President, who was busy at a board meeting. The President asked Mr. Houde and Ms. Caty to meet him. Houde was a senior vice president and general counsel; Caty was secretary of the Bank. They met all day on March 11. Houde was gone for a couple hours during the middle of the day; he returned and stated to Weir that Weir was an innocent victim. Houde apologized. He advised Weir that the Bank had formulated a new lawsuit against those who they believed were responsible, and they wanted the other responsible parties to share in the resolution of Weir's losses.

[439] Houde advised that the process would take three to six months. Weir was asked to make a proposal to the Bank as to a temporary measure until the Bank could get the other responsible parties into the process.

[440] The Court notes that the litigation Houde referred was the action known as the Main Action (206439), commenced by NBFL against Clarke and about twenty insiders for stock manipulation shortly after March 2003.

[441] At 10:00 that night (March 11, 2003), Weir e-mailed Houde a proposed interim arrangement. It contained three parts. One of them was that NBC or NBFL would provide Weir with the demand loan for $100,000.00, repayable in full out of the settlement of Weir's claim against NBFL. The Court notes that this proposal dealt with the effect of NBFL's sale of the Enervision shares out of the Blackwood account on September 19, 2001.

[442] Shortly thereafter, Weir and McLaughlin-Weir executed a Promissory Note for $100,000.00. Houde advised them that they had to document the $100,000.00 advance on the settlement as a Promissory Note to comply with the requirements of their auditors. The note provided for interest at 4.75%. Weir was required to provide NBC with a blank cheque on his wife's chequing account. Life insurance on the loan was automatically withdrawn by NBC for her account each month, but interest was not withdrawn. Weir says that, notwithstanding the execution of the Promissory Note, it was agreed that no interest was payable. No interest was ever actually taken out of McLaughlin-Weir's account by NBC pursuant to the agreement made on March 11/12, 2003, nor otherwise paid by the Weirs. I find that the agreement respecting the advance on the settlement did not include interest.

[443] Eventually NBC sued Weir and McLaughlin-Weir on the Promissory Note (Hfx 246337). That action was heard as part of this litigation.

[444] Weir says that the understanding from Houde was that in three to six months NBFL would settle with the Weirs, and the $100,000.00 was simply an advance against that settlement. After the action was commenced on the Promissory Note, Weir called both Houde and Caty, but was advised that both were no longer at the National Bank. He then contacted a Ms. Carr, a public relation officer at the Bank, who referred him to Michel Lebonte. He was advised to attend at Montreal with his lawyer to finalize a settlement. He attended at Montreal, but the matter did not settle.

[445] On January 19, 2001, Weir gave specific instructions to Clarke to sell KHI shares if they fell below $5.00. They did; Clarke did not sell. When Weir raised it with Clarke, Clarke persuaded Weir not to insist upon sale of the KHI shares. Based on Clarke's knowledge of KHI, and his own precarious margin debt position related to his purchases of KHI shares, it is clear and I find that Clarke breached many of his obligations to the Weirs and Blackwood. He misrepresented the circumstances of KHI, as he knew them to be. It was reasonable for the Weirs, both Lowell Weir and Carol McLaughlin-Weir, to rely on his advice. This advice caused them not to insist on execution of their sell instructions.

[446] There were more than 12,000,000 KHI shares outstanding. The stock was thinly traded. It is reasonable to infer that a large quantity of KHI shares may not have sold for about $5.00, but the Weirs did not own a large number of KHI shares. I infer that it is likely that the relatively small number of KHI shares held by Weir and Blackwood would have sold on the market for at least $5.00 per share.

[447] Blackwood held shares that should have been sold by Clarke. Because the market was being artificially supported, it is not known at this time whether those 8,000 shares or the 5,000 shares held by Weir in his LIRA account, or the 5,000 held in McLaughlin-Weir's RSP account, would have sold for $5.00. That is, however, because Clarke did not follow the directions of his clients and acted dishonestly toward them.

[448] On February 28, 2001, Weir received 28,125 shares into his margin account. At $5.00 per share, they were worth $140,625.00. The Court notes that they were issued at a higher value than $5.00. I find that Clarke was aware of the stock manipulation scheme of KHI insiders, and actively assisted in that scheme. I infer that Clarke did not believe that the restriction on the share certificate issued to the KHLP was *bona fide*.

[449] The Court notes that the complaints by Weir to the head office of NBFL related to its sale, contrary to the standstill agreement, of Enervision shares held by Blackwood Holdings. I accept Weir's evidence respecting the standstill agreement and its effect. It prohibited NBFL from liquidating the Blackwood account's Enervision shares until it responded to Weir's proposal. It had not done so when it dumped Blackwood's Enervision shares on September 19, 2001 (a settlement date of September 24). The Court disagrees with NBFL's submission that, if a standstill agreement existed, it expired on September 14, when Weir's September 9 offer expired. NBFL wrote on September 14 asking for time to reply and continued their discussions thereafter. I find that the standstill agreement was a binding agreement on NBFL at the time of their liquidation from the Blackwood account of 325,500 Enervision shares. Blackwood is entitled to recover for the

liquidation of Blackwood's Enervision shares contrary to the standstill agreement. NBFL should have known that the dumping of those shares would have had a serious damaging financial effect on both Blackwood and Weir.

[450] Weir made several complaints against NBFL. The correspondence exchanged between Weir and NBFL after September 9, 2001, centred on NBFL's sale of the Enervision shares contrary to the standstill agreement. The interim settlement negotiated between Weir and NBFL / NBC in March 2002 related to the Enervision claim. This is apparent from the e-mail Weir sent to Houde on March 11, 2003, which preceded the execution of the Promissory Note on March 19, 2003. The loan was an advance on the settlement of the Enervision claim.

[451] NBFL submits that any award of damages in favour of Weir and/or Blackwood Holdings should be offset by the $100,000.00 advanced. The advance of $100,000.00 was regarding NBFL's dumping of Blackwood's Enervision shares. It should offset the other claims of Weir and Blackwood.

[452] The Weirs claim punitive damages in respect of the conduct of NBFL toward them and Blackwood Holdings. This claim will be dealt with under the "remedies" portion of this decision.

D.3 Liability to the Michael (Ben) Barthe Estate

[453] As noted in part C.2 to this decision, and in the useful summary in the Biron/Boutin article (beginning at p. 318), the broker - client relationship is first one of agent and principal. The broker receives instructions from the client and must perform those instructions while acting with care, skill, diligence, honesty and good faith. Not to do so gives rise to an action for breach of contract and breach of a duty and standard of care in negligence. Statutes, regulations and codes of conduct of industry and employers also create duties and standards of care. They can infuse the common law contractual and negligence duties and standards of care.

[454] As noted, the duties of a broker depend upon the relationship between the broker and the particular client. In respect of Barthe, Clarke was simply an "order taker".

[455] Barthe made a deal with Potter to buy 250,000 KHI shares for 1.7 million dollars on August 3, 2000. Colpitts directed Barthe to Clarke to open an account to purchase the shares on the market. The Canadian securities system is a closed system and Barthe had to purchase through the stock exchange. Clarke executed the instructions to purchase shares and provided reports to Barthe with respect to his instructions, including the fact that he had carried them out.

[456] Barthe did not seek advice from Clarke.

[457] The basis of the claim for liability against Clarke (and NBFL) is that before Clarke received the instructions to execute the purchases on the market, Clarke was part of a conspiracy with KHI insiders to manipulate the public stock price. Clarke did not disclose to Barthe his personal involvement in the scheme to purchase shares on the market, mostly from insiders (which was not

a breach of his duty, as Barthe was aware that he (Barthe) would be purchasing shares from KHI insiders). Clarke did not disclose and Barthe had no idea that the public market price of KHI shares was artificially maintained by reason of the conduct of Clarke and some KHI insiders.

[458] The only potential liability of Clarke (and NBFL) to Barthe is if, as an order taker, Clarke's duty as Barthe's agent included that he either refuse to become agent for Barthe or to disclose to Barthe the stock manipulation scheme, because of his duty of honesty and good faith as an agent.

[459] Michael (Ben) Barthe passed away before he could be discovered. His wife, Barbara Barthe, and his friend Dr. Lutz Ristow, who, at one time, was a party to this proceeding, were discovered. No oral evidence was produced at trial on behalf of the Barthe estate. Several documents, including correspondence and e-mails to and from Barthe are in evidence. NBFL tendered short excerpts from the discovery evidence of, and interrogatories completed by, Barbara Barthe as representative of the Barthe estate. NBFL also tendered short excerpts of the discovery examination of Ristow as evidence against Barthe. The evidence was admitted by consent.

[460] Barthe was a wealthy German business man who sold his company (Rotring) to an American multinational for several million dollars in or about 1998. About the same time as he sold his business, he purchased property at Guysborough, Nova Scotia, where he began spending time and developing small enterprises in that rural community.

[461] Barbara Barthe's discovery evidence shows an absence of knowledge of the financial affairs of Barthe. She was unsure of the sale price of his business Rotring, including whether it was in US dollars or Deutsche marks (there was a big difference). There was no evidence as to the net proceeds from the sale of that business or his net worth after the sale of the business. Barthe reported his net worth on the KYC form, completed for Clarke on August 23, 2000, as five million dollars, at the time that he invested 1.7 million Canadian dollars in KHI. The Court accepts that his net worth was likely much more than the five million dollars declared on the KYC form.

[462] In 2001, Barthe's communications with Potter indicate that he had lost much money on the stock market and was having trouble raising his half (approximately 1.6 million dollars) of a private placement for purchase of shares for KHI treasury, which he entered into jointly with Ristow, for which his share of the payments was due in 2001.

[463] NBFL suggests that Barthe was a sophisticated investor. The Court is not satisfied that the evidence before the Court establishes that Barthe was a sophisticated investor. Ristow had no knowledge of Barthe's prior investment history nor was the evidence tendered from Ms. Barthe helpful in determining his investment prowess.

[464] One of Barthe's neighbours in Guysborough was Jack Sullivan, a shareholder and vice president of KHI. At the time, KHI was looking for wealthy investors. Barthe was interested in technology. It had dramatically changed the German business that he has recently sold. He was enthusiastic about the "new economy" and about "web education". Sullivan introduced Barthe to Potter.

[465] It appears that Sullivan or Potter provided Barthe with information about KHI, its finances, its shareholders and its business activities. Barthe caused a German accountant, who had worked for him at Rotring (Mr. Rehbein) to review the material. On April 17, 2000, Mr. Rehbein faxed Barthe a ten-page handwritten report on KHI, its share structure and business activities with some of its financial statements, which appears to summarize information supplied by KHI.

[466] Rehbein posed several questions for Barthe that he was unable to answer from the information provided. The materials reviewed by Rehbein do not suggest that they were derived from any sources independent of KHI. His conclusion in one sentence is: “As I see it, stock holds significant opportunities but equally many risks.”

[467] On May 31, 2000, Potter faxed Barthe a proposal to subscribe for 500,000 KHI shares from Treasury at $7.00 per share, with an option to purchase 500,000 more KHI shares within three years at $10.00 per share. Potter suggested that this option was a substantial discount to the anticipated KHI share price within five years.

[468] It appears that Barthe did not bite at this sales pitch. From a memo Barthe wrote on June 8, 2000, it appears that on that date Sullivan called Barthe to convey “confidential information” about KHI. The Government was going to spend a large sum on an education/training, of which KHI would be a significant beneficiary. The memo notes that Barthe was told that Potter was meeting with a New York broker on June 25 to obtain financing and begin the wide distribution of KHI shares. IBM and Intel were in the picture. KHI was ahead of its competition. Barthe should buy 500,000 KHI shares while he could.

[469] On June 11, Sullivan faxed Barthe a press release and reiterated that the deal Potter had offered him “is a bargain at this point in time. I anticipate it will begin to move very soon.” Still Barthe did not bite.

[470] On August 3, 2000, Blois Colpitts faxed Barthe a letter, to which was attached a Term Sheet and Option Agreement for Barthe to purchase 250,000 KHI shares for 1.7 million dollars and to receive an option to buy 150,000 KHI shares at $4.00 per share within two years. The seller, under the Term Sheet, was described as ‘Dan Potter or his designates’. The Option Agreement was explained to Barthe by Colpitts as involving the holdings of a former management individual. On August 4, Barthe returned to Colpitts a signed copy of the Agreement with four conditions to the effect that the shares and options be freely tradeable and clear of encumbrances.

[471] On August 14, Colpitts sent Barthe copies of the agreements signed by Potter. At the same time, Colpitts forwarded a copy of the agreement to MacLellan, Wadden’s lawyer. Potter was offering Wadden the opportunity to assume the Barthe agreement as a way to sell KHI shares and reduce his margin debt.

[472] On August 21, Barthe faxed Colpitts to advise that the 1.7 million was available for transfer and asking Colpitts how it was to be done. An August 23 fax from Clarke to Barthe referred to a phone call with Barthe as well as discussions with Potter, Sullivan and Colpitts Clarke included a

Cash Account Agreement to be completed together with instructions on wiring money to Clarke at NBFL.

[473] On August 24, Barthe sent Clarke the signed Cash Account Agreement and completed KYC, advising that the money would be received by NBFL by Monday, August 28. The same day Clarke contacted NBFL's credit department to approve the opening of the account immediately so that it would not lose Barthe's wire transfer. On August 25 Clarke faxed Barthe for more information and a copy of his passport. Barthe's 1.7 million dollars were received by NBFL on August 28. Clarke began immediately to purchase KHI shares. The purchase prices varied as if the purchases were on a truly open market.

[474] NBFL, in its submissions, makes note that Barthe was aware from the Term Sheet that he was buying shares from KHI insiders, even though the shares were being purchased on the TSX through NBFL.

[475] There is no evidence before the Court that Barthe knew that, from at least March 2000, Clarke had been purchasing KHI shares on the market using margin debt in the 540 account as part of the stock manipulation scheme, or that the 540 account's margin debt was made available by reason of the deposit ("loan") of $100,000.00 by Potter and the deposit of 220,000 KHI shares by Wadden (later replaced by 220,000 shares from Potter and MacLeod). There is no evidence that Barthe was aware of the scheme by which KHI insiders, and Clarke, were attempting to maintain the KHI share price. The evidence is that Clarke did not advise Barthe of any of this.

[476] The trading records of the various accounts of KHI insiders, such as those of Potter (including of his family and numbered companies) and of Colpitts, are not in evidence. Only the records of Wadden and his family as well as some of the records of Clarke (including the 540 account) are in evidence.

[477] Some stock manipulation is evident from these incomplete records as they relate to the sale of 259,000 KHI shares to Barthe, beginning on August 29, 2000.

[478] Clarke described the illiquidity of KHI shares in a June 29, 2000, proposal to Dennis Gagnon, Senior Vice President and Managing Director, Individual Investor Service at NBFL, and the need for immediately liquidity by some of those insiders. This is further evident in the follow-up to Clarke's memo - telephone call between Clarke and Daniel Bouchard on June 30.

[479] On July 17, 2000, the situation regarding the value of KHI shares got worse with the e-mail from Guy Roby, Senior Vice President, Compliance, NBFL. Roby advised Clarke that based on the heavy concentration of KHI holdings amongst Clarke's clients, and previous communications NBFL about seeking to reduce that concentration, he was recommending a substantial reduction in the loan value of KHI shares, which, at that point, was 50% of market price. Roby noted that this "could have a material effect on the clientele and maybe the market itself". At this time the 540 account owed margin debt to NBFL of 1.51 million dollars, secured by 452,200 KHI shares (nominally valued at $6.70 each).

[480] In Clarke's July 28, 2000, e-mail to Roby he untruthfully stated that "the large number of the shares that I hold in each company [at that time 900 ITI Education Shares and 452,200 KHI shares] is due in part by the fact that these shares came to us through the exercise of warrants, the releasing of shares from escrow, the set up of trust or numbered companies for tax planning, the exercising of stock options, etc." The truth was that the overwhelming majority of these shares had been acquired on NBFL margin debt premised on the loan from Potter to the 540 account of $100,000.00 cash and the loan of the 220,000 KHI shares (originally by Wadden, replaced later by MacLeod and Potter).

[481] On August 29, Clarke faxed NBFL's head office for approval of two trades connected with his client Barthe. The request reads:

> Wayne, For my client Blois Colpitts account 81-CDAE-7, I first will sell 73,300 KHI at $6.55 to my buyer, AC81-D7SA-7, M. Barthe. Secondly, I will sell from my personal account 00-8ANX-0, 43,300 KHI at $6.50 to Blois Colpitts account 81-CDAE-7 per his attached e-mail. Please call me with your approval. Thanks, Bruce.

[482] This fax refers to a Clarke account for which the trading records were not produced at trial. Clarke sold 43,300 KHI shares from his personal account to Colpitts at the same time as Colpitts sold 73,300 KHI shares to Clarke. Indirectly Clarke sold 43,300 KHI shares to Barthe from a personal investment account. At that time, Clarke's 540 account was maxed out on its margin debt and holding over 450,000 KHI shares. Clarke did not advise, or obtain the consent of, Barthe for what was in effect a matched order, involving him personally. Clarke forwarded the consent of Colpitts to NBFL's head office for approval of that sale, but not the approval of Barthe. NBFL negligently failed to catch the obvious conflict of interest and breach of its own policy respecting trades by its brokers.

[483] Barthe was expecting, pursuant to the August 3 Agreement with Potter, to purchase 250,000 shares at $6.80 per share. Each day from August 29 to September 9, Clarke faxed Barthe a report with the number of purchases that day and the net cost per share. Each day Barthe was buying shares for a different price, none of which were as high as $6.80. After the first day, Barthe thanked Clarke for the "birthday present" of 7,350 extra KHI shares. It is clear that Barthe was not advised that many of the purchases were arranged sales at arranged prices and was not the real market price for KHI shares.

[484] On September 8, 2000, Clarke e-mailed Potter a detailed record of the share sales to Barthe. He was keeping him in the loop with regards to who sold what shares.

[485] The 540 account did not appear to have participated directly in the sale of shares to Clarke. Clarke's apparent indirect participation was his personal sale of 43,300 shares to Colpitts at the same time that Colpitts sold 73,300 shares to Barthe.

[486] The Court notes a sale from the 540 account of 150,000 KHI shares at $6.65 at 14:52:00 p.m. on September 7, 2000. This sale was at the exact same instant 14:52:00 p.m. as another NBFL account sold 150,000 KHI shares for $6.65 each. The broker for the purchaser of the 300,000 KHI

shares was RBC Dominion Securities. The Court's review of the documents filed in these proceedings show the only record of purchases of KHI shares for $6.65 at that time were purchased by David Fountain of 150,000 shares on the market and 150,000 shares from the KHI Treasury in September 2000. As noted, Clarke incredibly had no memory of this significant and fortuitously-timed sale from his 540 account.

[487] Immediately after the sale of the 150,000 KHI shares from the 540 account, which had the effect of reducing the margin debt on the 540 account (which stood before the sale at $1,409,778.00), the 540 account went on a four-month buying spree of KHI shares until the 540 account ran out of margin debt again. The 540 account held 285,970 KHI shares after the September 7th Fountain sale. Over the next four months, it made 306 purchases of KHI shares with the margin debt re-ballooning to $2,160,141.00. The number of KHI shares held in the 540 account when it again ran out of margin debt by early February 2001 was 710,170.

[488] NBFL's submissions were primarily to the effect that Clarke did nothing wrong. It submits that the activity in the 540 account and by Clarke was a very insignificant portion of the trading KHI shares. I disagree. Other than the arranged sales by Potter to wealthy investors, the 540 account represented a significant portion of the market activity in KHI shares, from March 2000, when KHI insiders lent money and shares to the 540 account, until the end of January 2001, when the 540 account ran out of margin debt for the last time.

[489] Some of the TSX daily trading records respecting the activity in KHI shares were in evidence before the Court; particularly, the daily records from December 6, 1999 to December 29, 2000. The records do not identify the buyer and seller but identify the selling broker and the purchasing broker. NBFL operated through at least two brokerage accounts, Byron Securities Inc., Broker #63, and NBFL, Broker #80. These records show NBFL to be a significant trader in the buying and selling of KHI shares. It is not possible, from the evidence before the Court, to determine how much of that activity was directly by Clarke.

[490] As noted, all of Clarke's trading accounts have not been produced at trial. A review of his 540 account and Clarke's joint investment account (between him and his spouse) for the period March 2000 to the end of January 2001, shows 636 buy orders and 71 sell orders for a total 707 transactions. The largest was the 150,000-share sale on September 7, 2000. Of the total number of shares traded on the TSX between March 2000 and January 2001 (approximately 4,390,000), 1,281,000 or about 29% were purchases or sales in the 540 account or the personal joint trading account of Clarke and his spouse.

[491] Dr. Lutz Ristow lived and worked in Hamburg, Germany like Barthe. He had no business dealings with Barthe before their joint investment in KHI. He had no knowledge of Barthe's prior investment history. For 35 years, Ristow knew Barthe as a citizen as Hamburg, a very successful entrepreneur, a successful sportsman, and "a very fair gentleman".

[492] Ristow himself had been involved in real estate development in Germany, and had recently sold, and resigned from running, his publicly-traded real estate business. He had participated in a few private placements of shares in publicly-traded companies before October 2000.

[493] When visiting with Barthe in Guysborough in October 2000, Ristow was introduced to Sullivan and learned about KHI and its business model. He was impressed by Sullivan and his history as a school superintendent and saw the possibility of exporting KHI educational programs to Europe.

[494] On Thursday, October 19, 2000, at the time that he was returning to Germany from this visit, he and Barthe attended a meeting with Potter and Sullivan at the Halifax Airport for about two hours. Potter proposed that Barthe and Ristow purchase 800,000 KHI shares. They verbally agreed to a private placement of 500,000 new shares paid for in four installments.

[495] During the discussion, Barthe and Ristow asked about KHI's five-year plan and were advised that they would get that plan before November 5, 2000. The request for KHI's five-year plan was repeated in several follow up communication (beginning October 25) and always put off by Potter and KHI's vice president of finance, Gerard McInnis. It appears that, despite several requests and promises, the promised five-year plan was never delivered.

[496] The outline of the agreement made at the Airport is reflected in an October 22 memo that Potter sent to McInnis, Sullivan and Colpitts. Barthe and Ristow were to purchase 500,000 shares from Treasury for $6.50 each by a private placement payable in four instalments for a total investment of 3.250 million dollars. In addition, Ristow was to be appointed to the Board of Directors of KHI. The deal was contingent on Board approval and that it did not interfere with other KHI Board of Directors sales plans.

[497] On October 23, McInnis faxed Barthe a draft agreement in the form of a Term Sheet. On November 8, Potter faxed Barthe and Ristow confirming a November 15 closing for the deal and suggesting that Ristow open an account with Clarke at NBFL for the transfer of funds for the first of four equal instalments of $812,500.00. Potter then contacted Clarke who, on November 9, faxed to Ristow a letter and forms outlining the requirements for opening of an account and the transfer of funds to NBFL. On November 10, Ristow sent Clarke the required documents, including an account agreement and KYC form, as well as the first of the four instalments.

[498] Stewart McKelvey Stirling Scales ("SMSS") prepared the documents to conform to the TSX rules respecting private placements in public companies. The documents included an Escrow Agreement naming SMSS as the trustee to hold the KHI shares being purchased until all of the instalments were paid. SMSS arranged for the agreements to be executed on November 15 and carried out the necessary communications to obtain TSX approval.

[499] On November 17, Ristow asked Clarke to confirm that 125,000 KHI shares were then in his NBFL account. At this point the TSX had not approved the private placement.

[500] In a November 19, 2000, e-mail from Potter to Wadden, copied to Colpitts, relating to the demands of a friend of Waddens whose friend ("Steve") was trying to sell his KHI shares on the market, Potter stated that "we don't have any liquidity solutions for Steve at this moment, however, I'd be pleased to meet with him at[on] . . . Monday morning at our offices to put a plan together ..." The next paragraph of the e-mail is significant:

> As you know, we are closing on a $3,250,000 treasury issue to our German friends - we are hoping to get this completed (closed) on Monday or Tuesday, November 20 or 21. The price of this issue is $6.50 per share. If the market is driven down in advance of this issue, it is quite likely that the investors will not close. This would be most harmful for the company and all of its shareholders, including Steve. Hopefully, he can be convinced to proceed with care, prudence and caution.

[501] On November 21, Potter wrote to Barthe and Ristow advising that the TSX had approved the agreement but required all of the shares to be held in escrow with the trustee until the final payment, due on August 15, 2001. This would have been news to Barthe and Ristow. Potter enclosed documents reflecting this condition for execution by them. Ristow and Barthe signed and returned these agreements.

[502] On November 24, Potter advised Ristow to authorize NBFL to release his funds to SMSS and KHI. On November 28, Ristow did. On November 29, Clarke transferred Ristow's first installment to SMSS. On the same day, Gerard McInnis e-mailed Potter that Barthe was asking again for the five-year plan and the 2001 plan approved by the Board. This was their third request; the first was at the Airport meeting on October 19, and the second on October 25. McInnis' memo shows that he put Barthe off respecting the five-year plan and said that the 2001 plan was not yet presented. Barthe expressed displeasure and wanted access to the information.

[503] On December 22, 2000, Barthe again wrote Potter asking when he could expect to receive the five-year plan. He also asked when the February board meeting was scheduled for, and that he expected that Ristow would attend. On December 26, Potter wrote Barthe and Ristow that the 2001 plan and the five-year plan would be presented to the Board of Directors at a meeting January 18, 2001 and that there would be no meeting in February. In this letter, Potter asked Barthe and Ristow to provide a banker's letter of credit to guarantee their subscription agreement for the 3.250 million dollars.

[504] On January 4, 2001, McInnis sent Barthe and Ristow a draft 2001 business plan and said the five-year plan would be available January 18. On January 6, Barthe acknowledged the 2001 draft plan and said that he and Ristow wanted to review it and the five-year plan before "indulging in any further share acquisition ideas".

[505] On January 8, Potter promised to send the five-year plan before January 18. He again asked for the banker's letter of credit to support the subscription agreement and enclosed a draft RBC form for same. The same day Barthe and Ristow exchanged messages about the need for information from KHI, including KHI's expected results for the year 2000.

[506] On January 10 Ristow wrote Potter bluntly rejecting his request to collateralize the Subscription Agreement with a letter of credit, but stated he would agree to pay the second instalment due February 15 immediately. The same day, Ristow arranged for his Bank to transfer $812,500.00 to Clarke at NBFL.

[507] In correspondence between Clarke and Ristow, it appears that Ristow was still under the misconception that the KHI shares being subscribed for would be in his NBFL account, when in fact they were being held in trust by SMSS. On January 15, Clarke sent SMSS the second instalment of $812,500.00.

[508] On January 19, 2001, Potter sent Barthe and Ristow a January 15 confidential memo outlining KHI's need for three million dollars in new equity immediately and advising of the reduction of KHI's bank operating credit lines. The Court notes that this memo was sent after the second instalment was received. Potter asked Barthe and Ristow to immediately participate in this "rights offering" by purchasing 285,000 KHI shares and receive warrants that would entitle them to purchase more shares at $4.06.

[509] This letter was significant. It was the first time that KHI or anyone disclosed to Barthe and Ristow the fact that KHI was in desperate needs of new equity, and involved in a daily market support program because of the downward pressure on KHI's market share price.

[510] Barthe sent Potter two replies the same day. In the first he wrote that he had tried to call when he received this fax. He said he had lost a lot of money in the last three months; was trying to survive and could not help the company. He added, "Further, I am not sure at the moment how I can pay the shares in May and September. I will try to find a solution until then . . . My only hope is that you and your Canadian friends will be able to avoid the worst for this fine company." In the second fax, he confirmed that he would still be able to make the May and August, 2001 final two instalments on the private placement.

[511] The same day Sullivan called Ristow to promote the new "excellent opportunity" for investment in KHI. Both Sullivan and Potter separately followed up with written pleas to Barthe and Ristow on January 20. Potter emphasized the urgent need for new investment by Monday, January 22, and, as an inducement, offered to have Ristow replace him as chairman of the KHI Board and to become the controlling shareholder. At this point, Ristow was still not a Director of the Company.

[512] In the letter, Potter discloses, as in the January 19 fax, the fact that he and local supporters had been buying stock to maintain the market price but had exhausted their capacity to do so any longer.

[513] The Court notes that Clarke, in his 540 account, made his last purchase of KHI shares (save for one in mid-February from the proceeds of the sale of Cross-Off Shares) on or about January 19.

[514] The Court notes that at the same time, Wadden's broker at BMO (Richards), advised Wadden that, because of the drop in the KHI price on the two previous days, he had been forced to sell 2,000 KHI shares to keep Wadden's margin account at BMO onside.

[515] On January 21 and February 3, Potter called Ristow and asked him to instruct Clarke to buy 20,000 KHI shares on the market to provide market support. He again promised to have a revised 2001 business plan and budget to Ristow within a few days. Ristow did not provide Clarke with instructions to support the market. On the contrary, he appears, from the followup communications, to have avoided phone calls from Potter.

[516] The Court finds that at no time did either Ristow or Barthe, together or separately, agree to provide market support through purchases of shares on the market for the purpose of maintaining the KHI price.

[517] On February 12, Potter faxed Ristow again asking him to provide market support by purchasing 50,000 shares on the market. He appealed to the fact that Ristow was a substantial investor. By February 22, Ristow had not replied. Potter sent him a memo containing a reference to a "managed selling agreement" and market support arrangement amongst five other large shareholders.

[518] On March 2, Potter sent Ristow and Barthe another letter describing how the stock price was "holding up" because of the efforts of himself and other share holders, but that the stock was faltering. He asked them to provide support by buying 20,000 KHI shares on the market through Clarke. Potter copied the letter to Colpitts with the words "attached is another poke at Lutz /Barthe".

[519] On March 5, Barthe acknowledged the request "to take up some more KHI shares" and to give market support, but he did not have the means to do so.

[520] Based on Ristow's avoidance of Potter after the January 19 e-mail, in which reference is made to market support efforts, the Court is satisfied that Ristow at no time intended to support the market himself or support the efforts of Potter and other KHI insiders to do so.

[521] On April 4, Potter sent Barthe and Ristow a direction to pay the next instalment in the Subscription Agreement (due May 15). On April 18, Barthe e-mailed Potter asking for "the Board Members judgment concerning KHI's future development". He indicated that he had a "slight stroke". The Court notes that Barthe's health deteriorated thereafter and that he was soon hospitalized.

[522] On the same date, Potter replied to Barthe and Ristow with an update on KHI's affairs. The letter referred to the fact that KHI had deferred on its commitment to have Ristow elected to the Board, but advised that KHI planned to advance his name as a Director in the Information Circular, for the June 27, 2001, Annual General Meeting.

[523] On June 21, Ristow advised Potter that neither he nor Barthe could attend KHI's Annual General Meeting. The Minutes of the June 27 AGM show that they were not present, but Ristow was elected to the Board.

[524] By a letter dated June 29, received by Ristow on July 12, Ristow was advised of his appointment to the Board and provided with an Agreement, as part of his appointment to the Board, to accept the grant of 10,000 options of KHI shares.

[525] On July 19, Clarke was advised of Barthe's urgent hospitalization. He forwarded to Barbara Barthe information and a form to be completed to enable her to have a trading power of attorney on Barthe's NBFL account.

[526] On the same date, Ristow acknowledged receipt of the June 29 letter with the Option Agreement. He returned the Agreement signed and asked questions about aspects of the KHI Financial Statement that he did not understand. On August 9, Potter replied to Ristow that the KHI financial results were worst than expected on the Financial Statement because of the acquisition of the Knowledge House Limited Partnership into KHI in exchange for shares. This caused KHI to absorb the very substantial losses of KHLP. It is apparent from this exchange that Ristow had not been previously advised about the Limited Partnership, the exercise by KHI of the option to convert the partnership units to shares, and of the potential consequences on KHI and KHI's share value.

[527] On August 16, Torstar announced the write-off of its 25-million-dollar investment in ITI and the appointment of a receiver. ITI was the corporation Potter had created and sold to Torstar immediately before taking over KHI. The KHI shares went into a tail spin and, on August 23, the TSX required KHI to explain to the public what was happening to its shares.

[528] On August 21, Ristow was forwarded a copy of a Notice of a Board Meeting, scheduled for August 24. The Notice included information about the precarious nature of KHI's finances. Ristow did not travel to Nova Scotia to attend the meeting.

[529] On September 4 and 11, KHI sent Barthe copies of a memo seeking financial support for KHI. On Wednesday, September 12, Potter asked for a Director's Meeting for September 13, to obtain $200,000.00 to meet that day's payroll.

[530] On September 13, Potter announced that KHI was unable to continue operations. KHI closed its doors. On October 1, Potter sent Barthe and Ristow copies of a proposed filing KHI was making under the *Bankruptcy and Insolvency Act*.

[531] It is not clear from the evidence when Barthe and Ristow paid the two remaining instalments on their Subscription Agreement in the amount of $1,625,000.00. It is clear that they did pay this remaining commitment.

[532] In December 2001, on Barthe's instruction, NBFL sold Barthe's 259,000 KHI shares, netting $24,503.70. On January 25, 2002, Barthe's account received his share of the private placement

(250,000 KHI shares and 250,000 warrants). These shares were sold and Barthe's net proceeds from the sale were $10,867.50.

[533] In its post-trial brief, NBFL submits that Barthe was a sophisticated businessman. I agree; he was a sophisticated entrepreneur.

[534] Secondly, they say Barthe was a sophisticated investor who accepted the risks of investing in KHI. I do not agree that it was established that Barthe was a sophisticated investor. Neither his wife nor Ristow knew anything about his investments. Barthe himself, in communications with KHI, described his investment in KHI as substantial and noted that he had lost much money in the stock market.

[535] NBFL says Barthe conducted his own due diligence. The research he appears to have conducted was of two types. First was general reading in financial newspapers with respect to the new economy and e-learning. The second was to have his former employee, Mr. Rehbein, review the financial disclosure provided to him by Potter and Sullivan respecting Knowledge House. Mr. Rehbein raised several questions to Barthe and identified the risk of the investment. It is clear Barthe had no information regarding the KHLP before January 2001, or that KHI insiders, acting through Clarke, were manipulating the stock price of KHI.

[536] NBFL notes that Barthe had access to a local and German lawyer, as well as a local and German accountant. There is no evidence, direct or indirect, from any of them.

[537] Barthe, and later Barthe with Ristow, directly negotiated with Potter and KHI. The only particular evidence as to involvement of any of their professionals was that Mr. Winter was consulted about the first Term Sheet. Apparently, on his advice Barthe requested addition of four conditions to the effect that the shares and warrants were unencumbered and KHI was authorized to complete the agreement.

[538] There was no evidence that any legal or accounting professionals conducted independent investigations into KHI or were aware or could have been aware of the stock price manipulation that was going on from at least March 2000.

[539] I agree with NBFL's third point that Barthe negotiated his first investment directly with Potter and Sullivan. NBFL notes that the Barthe estate denied in its pleadings the existence of the Option Agreement that accompanied Barthe's first agreement with Potter to purchase 1.7 million dollars worth of KHI shares. There is no evidence of knowledge or notice of conspiracy to manipulate the KHI share price by Barthe. The Court fails to understand how the existence of the Option Agreement puts Barthe on notice of the stock manipulation scheme.

[540] NBFL's fourth point relates to the opening of the NBFL account by Barthe. NBFL submitted that Barthe contacted Clarke on August 23, 2000. Clarke's letter of August 23, 2000, does not say who contacted whom. It is clear that Barthe was referred to Clarke by Colpitts when he asked how he was to proceed. It is also clear that Clarke was kept in the loop by Potter and Colpitts with respect

to investors they were hustling. I do agree with NBFL that Clarke did execute Barthe's instructions to purchase the shares. He was paid commissions of $13,848.00 for doing so.

[541] I agree that there is no evidence of any other transaction in Barthe's NBFL account and there is no evidence that the identity of the sellers would have affected Barthe's decision to purchase KHI's shares in August 2000. Barthe would have been aware, by the term sheet, that Potter and/or his designates would be sellers.

[542] NBFL's fifth point is that Barthe knew that KHI was a start up company and that its market capitalization bore no relationship to its underlying economical fundamentals. NBFL is attributing the evidence of Ristow to Barthe. In discovery, Ristow testified, in effect, that he knew that start-up companies were often starving for cash and were unprofitable or marginally profitable, and that this was not determinative of their future prospects. In October 2000, Potter wanted Barthe and Ristow to buy shares from existing shareholders. Ristow wanted to purchase shares from the Treasury, in light of his understanding of the nature and needs of start-up companies.

[543] The Court agrees with NBFL's point that the November 2000 Subscription Agreement prepared by Colpitts, signed by Barthe, confirms that there is no assurance that the money that he and Ristow were injecting into KHI would enable KHI to continue operations.

[544] NBFL sixth point deals with the extent to which Barthe and Ristow became tied up as insiders in KHI through their private placement purchase of 3,250,000 shares of KHI from Treasury.

[545] NBFL submits that Ristow was to become a Director; Barthe was to act in his place as a Director. It cites an October 23, 2000, communication from McInnis to Barthe attaching a draft Term Sheet.

[546] The Court notes that Potter's memo to McInnis dated October 22, 2000, outlining his meeting with Barthe and Ristow at Halifax Airport on October 19, says: "It was agreed that, in due course after the completion of the first closing, Lutz would be appointed to the Board, with the understanding that if he is unable to attend certain meetings that Ben would be invited to attend in his place."

[547] The reality is that KHI deferred appointing Ristow as a Director until June 2001. While Barthe received many of the same communications and information that Ristow did, Barthe was at no time appointed a Director or given any legal status with respect to the Board of Directors or management of KHI. He was not appointed an alternative director (assuming there is authority in Nova Scotia company law for such an appointment). Barthe was never treated or expected to be treated as if he was a Director of KHI.

[548] As previously noted, Barthe and Ristow had been asking for the five-year plan since their first meeting with Potter and Sullivan on October 19, 2000, which lead to the private placement. They never did receive it, despite repeated requests for it, both before and after they were informed on January 19, 2001 of the market manipulation by KHI insiders. It appears that the only financial

disclosure received by either Ristow or Barthe was the 2001 financial plan sent to them on January 4, 2001. It was from this draft business plan that Ristow became concerned and asked questions of Potter, which lead to Potter's disclosure, after the January 19 second instalment was made on the private placement, that KHI had absorbed the significant losses incurred by the Knowledge House Limited Partnership.

[549] The Court finds that what Barthe and Ristow received as disclosure before the January 19, 2001, was no relevant financial disclosure and, in some cases, misleading or deceptive financial information.

[550] One of the most relevant points argued by NBFL in its post-trial brief respecting Barthe is their submission that there is no evidence that Barthe would not have invested in KHI had he knew that its share price was supported (or, in my finding, manipulated). They say the evidence is to the contrary. When Barthe was advised that the stock was being supported, he did not complain.

[551] After January 9, 2001, the documents before the Court clearly show that almost all of KHI's communications (both by Potter and Sullivan) were to Ristow, with some being copied to Barthe. It is equally clear that after January 9, 2001, Ristow was not returning or receiving phone messages and phone calls from Potter. The only communications from Barthe appear to be on March 5 and April 18, 2001.

[552] My inference from the totality of the communications between KHI, on the one hand, and Barthe and Ristow, on the other hand, is that, while they did not expressly accuse Potter and KHI of being dishonest and deceptive, the tone of their communications with KHI changed. Not only did Ristow not return calls, but he and Barthe declined to make further investments in KHI despite Potter's pleas. At no time did either took Potter up on his repeated requests that they instruct Clarke to start purchasing KHI shares on the market immediately.

[553] Ristow's description of Barthe in the discovery excerpt tendered by NBFL contains Ristow's description of Barthe as being a "very fair gentlemen . . . the type of person you would want to be friendly with."

[554] I conclude there are the reasons that Barthe (and Ristow) did not pick a fight with Potter and KHI after January 19, 2001, when they clearly changed their tone, and appear to have understood they had been taken was: (a) they were sophisticated enough to know that they were already heavily invested into KHI. Making accusations against Potter, who was describing himself and his local shareholders as being tapped out, was not going to get him out of KHI with his investment. Sitting on the sideline and hoping for recovery was the most practical option; and (b) it is clear from the tone of their communications that Barthe and Ristow were gentlemen. It would not have been their style to pick a fight with KHI or Potter that, at the end of the day, was not likely to have a realistic prospect of saving their already substantial investment in the company.

[555] I do not agree with the implication of NBFL's submission that Barthe condoned the manipulation of the stock price by Potter and other KHI insiders.

[556] There is no evidence that Barthe would have invested in KHI had he known that the share price had been manipulated when he made his first, 1.7 million dollar investment in August 2000, or when he and Ristow made their 3.250-million-dollar private placement in October/November 2000.

[557] As noted, there was no legal authority for the so-called "price support" or manipulation of the KHI market share price. Clarke was involved in with KHI insiders from at least March 2000, when they lent to Clarke money and shares for his 540 account.

[558] The first legal issue is: did Clarke breach his duty of care to Barthe by agreeing to be an "order taker" in August 2000 to purchase 1.7-million dollars' worth of shares of KHI when he knew and was part of the stock manipulation scheme?

[559] The second issue addresses NBFL's counterclaim: was Barthe liable to NBFL for failing to blow the whistle on KHI by reason of his receipt of financial information from KHI that was not generally available to the public and KHI's invitation to him to attend Board of Directors' meetings that Ristow was not able to attend in late 2001 (which never occurred)?

[560] Clarke had a duty to be honest and act in good faith toward his principal, Michael (Ben) Barthe.

[561] NBFL had an obligation to take reasonable steps to identify existing and potential material conflicts of interest between it, any of its brokers, and any of its clients.

[562] If NBFL had been supervising the activities of Clarke in his 540 account, it would have known about the loans of money and shares from KHI insiders to Clarke, and their use by Clarke, using NBFL margin debt, to prop up the KHI share price on the market.

[563] When NBFL did conduct its own investigation, after litigation began and in respect of its commencement of the Main Action, its Senior Vice President swore under oath that the illegal scheme to manipulate the KHI share price by KHI insiders and Clarke was clear. NBFL should have known this before late August 2000 when it took on Barthe was a client.

[564] There are different ways to avoid a conflict of interest. NBFL can stop providing service to a client. It can, in some circumstances, create internal communication barriers between the brokers who have conflicts and their client. Alternatively, it may disclose the conflict and obtain the client's consent to proceed. NBFL did none of these. Clarke did none of these.

[565] I have found that Barthe did not know of the market manipulation scheme until after January 19, 2001. I find that NBFL should have known of it, as it swore in Court motions dealing with the Main Action that it later learned, before Clarke agreed to purchase KHI shares for Barthe.

[566] Because of my finding that Clarke was part of the scheme to artificially maintain the KHI share price with KHI insiders, he clearly did not act honestly or in good faith in respect of his agreement to act for Barthe as an order taker to acquire KHI shares on the market.

[567] The liability of Clarke and NBFL to Barthe does not arise because Barthe sought and Clarke gave advice, nor because KHI, absent stock manipulation, was not a suitable investment for Barthe, nor because the shares purchased by Clarke came largely from KHI insiders.

[568] The liability is because Clarke was part of a fraudulent scheme to artificially maintain the KHI share price on the market and, for a fee, he agreed to buy approximately 250,000 KHI shares for Barthe, knowing that the price was being artificially maintained by him and KHI insiders.

[569] The investment by Barthe in the private placement in November 2000 is a different situation. The liability of NBFL to Ristow is not in issue, as Ristow is no longer a litigant in these proceedings. Ristow opened an account with NBFL to transfer money to KHI with respect to his contribution of $1,625,000.00, to the private placement. There is no evidence that NBFL or Clarke charged a fee for this service. It did not involve Clarke acting as an order taker, providing advice or providing any other service.

[570] It appears from the evidence that, while there is no direct evidence of when Barthe made his $1,625,000.00 payment to the private placement, he likely made those payments when they were due for payment on May 15 and August 15, 2001. Whenever Barthe made those payments, it is clear he made them after January 19, 2001, when he became aware for the first time that the KHI share price had been manipulated.

[571] With that knowledge, any payment by Barthe to the private placement cannot make Clarke or NBFL liable. Clarke's wrongdoing (for which NBFL is vicariously liable) and NBFL's negligence were not the cause of Barthe making the $1,625,000.00 on the last two instalments of the private placement after January 19, 2001.

[572] I find NBFL liable, both vicariously for Clarke, and by reason of its own negligence and breach of contract to Barthe, for the Barthe investment in August 2001 of $1,700,000.00 in KHI shares. The issue of remedy is dealt with later in this decision.

D.4 Liability to Wadden

[573] The evidence respecting the Wadden claims against NBFL arises from the exhibits and oral testimony of Calvin Wadden, his wife Andrea, his lawyer Brian MacLellan Q.C. and his friend Hal Greenwood. NBFL called no direct oral evidence.

[574] The reliability of oral evidence, with respect to historic events, is always problematic. In this part of the case, credibility played a prominent role.

[575] In *Re: Novak Estate*, 2008 NSSC 283, at paras 36 and 37, I wrote:

[36] There are many tools for assessing credibility:

a) The ability to consider inconsistencies and weaknesses in the witness's evidence, which includes internal inconsistencies, prior inconsistent statements, inconsistencies between the witness' testimony and the testimony of other witnesses.

b) The ability to review independent evidence that confirms or contradicts the witness' testimony.

c) The ability to assess whether the witness' testimony is plausible or, as stated by the British Columbia Court of Appeal in Faryna v. Chorny, 1951 CarswellBC 133, it is "in harmony with the preponderance of probabilities which a practical [and] informed person would readily recognize as reasonable in that place and in those conditions", but in doing so I am required not to rely on false or frail assumptions about human behavior.

d) It is possible to rely upon the demeanor of the witness, including their sincerity and use of language, but it should be done with caution (R. v. Mah, 2002 NSCA 99 ¶¶ 70-75).

e) Special consideration must be given to the testimony of witnesses who are parties to proceedings; it is important to consider the motive that witnesses may have to fabricate evidence. R. v. J.H. [2005] O.J. No.39 (OCA) ¶¶ 51-56).

[37] There is no principle of law that requires a trier of fact to believe or disbelieve a witness's testimony in its entirety. On the contrary, a trier may believe none, part or all of a witness's evidence, and may attach different weight to different parts of a witness's evidence. (See R. v. D.R. [1966] 2 S.C.R. 291 at ¶ 93 and R. v. J.H. supra).

[576] Many documents, mostly e-mails and trading records, from the period 2000 to 2001, were produced. They were the focus of the oral evidence.

[577] In my assessment of the evidence of Wadden and Ms. Wadden, it became apparent that Wadden often failed to answer questions in a direct and responsive manner; in addition, he often answered questions as an advocate. This detracted from his reliability and credibility. Ms. Wadden's memory became particular vague when she was asked pointed questions about documents not helpful to the Wadden's claims. This affected the reliability and credibility of her evidence.

[578] Actions or conduct, reflected in this case in documents made contemporaneous with events, spoke louder than testimony that many years later attempt to explain away or rationalize them.

[579] My analysis of the actions and conduct of Clarke (in respect of the claims of Dunham, the Weirs and the Barthe estate), as reflected in his responses to the documentary evidence put before him, led me to find that most of his explanations were incredible. The same analysis applies to the often incredible and unreliable explanations by Wadden of the historic documentary evidence.

[580] In contrast, the evidence of MacLellan, hired by Wadden on July 17, 2000, and terminated without explanation about August 24, 2000, was straightforward, apparently unbiased, and in harmony with the apparent meaning of the notes, records and communications made by him at the time of the events. His testimony was reliable and credible, and helpful. I relied on it.

[581] Wadden attended, but did not graduate from, university. He worked for about ten years in the banking industry, beginning as a credit officer. In 1994, he joined his long time friend and computer whiz, Ray Courtney, to create Micronet, a business that installed and distributed computer hardware and software, primarily to educational institutions. By 1999, it had grown significantly.

[582] Wadden was aware of Potter through his successful development of ITI Education. He learned from colleagues about Potter's new efforts in KHI.

[583] Potter is a brilliant and persuasive entrepreneur. He was trained as a lawyer but saw himself a new economy guru. Wadden clearly was impressed by Potter and his reputation for success.

[584] In a very short span in mid-1999, Potter convinced Wadden and Courtney to sell Microsoft to KHI at the exact time that Micronet (with its partners) was awarded a very substantial and long-term contract to install and maintain a computer network (hardware and software) in the Nova Scotia school system.

[585] In exchange for Micronet, Wadden and Courtney received no money but each received 1.1 million KHI shares (and warrants) as well as executive jobs.

[586] Wadden and Courtney each became owners of more than 10% of KHI's stock; only Potter and his family were larger shareholders.

[587] Up to this point, Wadden had no substantial income or net worth, and did not have a high standard of living. With the acquisition of these shares, Wadden naively believed he had become a multimillionaire. Immediately, on the sale of Micronet to KHI, he and his wife (who retired), purchased and started extensive renovations to a historic South End Halifax residence, and began building a substantial summer residence in Cape Breton.

[588] Wadden believed in the KHI dream. He purchased more KHI shares.

[589] The shares were highly speculative. KHI did not have a track record or plan that would, at that point, support the market share price. KHI was a thinly traded, small public technology company. Wadden did not appear to appreciate that ownership of shares in KHI was not money in the bank.

[590] In December 1999, Snow, who had, like Wadden, sold his Cape Breton e-commerce business to KHI for shares months before Wadden and Courtney, decided to cash in his KHI shares. Keating, a successful, self-made entrepreneur who acquired wealth in the cable television industry, was persuaded to buy one million shares for about $5,920,000.00 in January 2000. Keating did not buy all of Snow's shares. Wadden and Courtney agreed to each buy 100,000 shares at $6.00 per share.

[591] When Wadden and Potter sold Micronet, the shares they acquired were placed in escrow to be released to them in equal portions over five years.

[592] In exchange for Wadden and Courtney agreeing to buy 200,000 KHI shares from Snow, Potter agreed that all of their shares would be immediately released from escrow, and Potter promised that he would find buyers, or buy himself, from each of Wadden and Courtney, 250,000 KHI shares by June 2000. Wadden described this as a gentleman's agreement.

[593] At this time, Wadden believed that KHI's share price would double from January 2000 to June (as it had in a few months in 1999). He thought it was a good investment.

[594] Wadden had investment accounts in the CIBC, and with his longest and best friend as well as a former co-worker, Richards, who was a broker at FCG. Wadden used the KHI shares, which constituted almost all of his net worth, as security for borrowing on margin accounts. The borrowing was used to make other investments, to finance the renovation / constructions of his two residences, and to live on.

[595] I conclude that in addition to being naive, Wadden did not paid attention to details or take much time to analyse his situation objectively. He appeared to have been very trusting of Potter and his dream.

[596] This is reflected by an important event in early March 2000. The event is described in part by Wadden in his testimony.

[597] In his examination-in-chief, Mr. Wadden testified that the circumstances which led to the deposit of his 220,000 shares in the 540 account were as follows:

> A. Okay. Throughout the winter, Knowledge House was in the process of doing some large deals - several large deals, including a national partnership with IBM, a big deal with Bell Aliant. They were going to buy a - their technology division Wave. There were several large deals under way.
>
> And prior to us heading up to do the - the investor stuff, what do you call it the - going to Bay Street to talk to institutional investors, there was a lot on the go and a lot of activity.
>
> The stock had progressed from I think \$6.00 to probably \$7.00 and at the time, prior to me leaving for Florida, I was in the offices at Spring Garden Road and Mr. Potter approached me about Knowledge House's orderly market account (p. 3759 - 60)

[598] Wadden testified that he had a discussion with Potter some time around lunch time and Potter told him that KHI's orderly market account was offside and he was going to ask all of the founders that were partners in the business to each pledge security. He was asking everyone for 100,000 shares, since all of the founder shares were released from escrow.

[599] Wadden went upstairs to Richards' office and asked him for a share certificate. Richards gave Wadden the only one that he had available which was for 220,000 shares. Wadden took the Certificate downstairs and gave it to Potter and Potter said - "sign the back of it and give it to Ruth Cunningham".

[600] Wadden then endorsed the certificate and gave it to Ruth Cunningham.

[601] On his cross-examination, Wadden testified that when he delivered the endorsed Certificate to Ruth Cunningham, he said to her - "Dan said to send this down to National Bank, to Bruce Clarke."

[602] At that time, Wadden understood Clarke was a stock broker at NBFL, used by Potter and KHI. I find that at that time he did not know about Clarke's numbered company and 540 account. What Wadden understood Potter to be talking about on that March noon was that KHI had an orderly market brokerage account at NBFL (of which Clarke was the broker), which was used to buy and sell KHI shares. Wadden believed that the account that he was lending shares to was to be used to buy and sell KHI shares.

[603] I find that at that time, Wadden did not know how that account was used, and that, in fact, that it was used to buy KHI's shares, and to occasionally sell shares in deals that Potter arranged with new investors.

[604] Wadden was careless in respect of Potter's request in early March 2000, and agreed to it without any further inquiry, either of Potter or otherwise, as to what it involved. At that time, he did not know whether KHI was permitted to hold an account for the purpose of trading in its own shares. There is no evidence that he was then aware that the only appropriate and legal orderly market accounts were those operated by "market makers" designated as such by the stock exchange on which the publicly traded shares were traded.

[605] In March 2000, Richards advised Wadden that he had reached the limit of his margin borrowing at FCG on the security of the KHI shares.

[606] At the time that Potter asked Wadden to participate in the orderly market account, Wadden opened a margin account at NBFL with Clarke, transferred 220,000 KHI shares held by him at CIBC (with a margin debt of $300,000) to Clarke at NBFL, and arranged to get access to more margin. This was in response to Richards' advice that he had reached the limit of margin borrowing at FCG. This move helped Wadden to access more margin, in part because the market price of KHI shares continued to rise (or apparently so). The market price reached a peak on March 29, 2000, of $8.95.

[607] Also in the spring of 2000, Richards decided to move from FCG, which did not have full brokerage standing, to a full standing brokerage firm. He made a deal with BMO and moved. He believed that he could move with his two biggest clients, Wadden and Courtney, with their large accounts and margin debts secured by KHI shares; Richards was wrong. When BMO head office reviewed the accounts, after Richards had moved, they expressed concern about the margin debts secured by KHI shares and, despite lobbying by the Halifax branch, BMO head office would only agree to accept the Wadden accounts on the basis that the KHI shares would be liquidated by a deadline. The first deadline was June 1; this was extended to June 30, 2000.

[608] I find that Wadden was kept informed by Richards about the position of BMO head office and the lobbying by the Halifax branch on his behalf. Wadden was confident that Potter would find him a sale for 250,000 KHI shares by the end of June as promised in December 1999. While he

knew of the BMO's position, this did not stop him from transferring his accounts to BMO under their conditions.

[609] At the end of June 2000, Potter did not come through with a buyer for Wadden's 250,000 KHI shares. This was now a big problem for Wadden.

[610] Shortly after, in early July, Wadden learned that Courtney, who was in a similar financial circumstance as him, had been advanced a $400,000.00 loan by KHI. Wadden felt betrayed by Potter by this secret loan, which he had not been offered. He was under the same financial pressure to reduce his margin debts.

[611] In March 2000, Wadden had realized he was not a good fit as an executive at a public company, so he had resigned his position as an officer and director of KHI, and in June he was in the process of leaving KHI to become a self-employed real estate developer. His finances were not helped by the absence of an income.

[612] On learning of the Courtney-KHI loan, Wadden lost his cool. He got into heated exchanges with Potter and, on one occasion, Potter's prime facilitator, Colpitts. He refused to have any direct dealings with them. He decided to sell his KHI shares on the market and advised Potter. Potter, unlike Wadden, fully knew that, if Wadden started placing significant amounts of KHI shares on the market, the market could not absorb them and the share price would decline significantly. KHI would be adversely affected. Potter's attempts to appease Wadden were not successful.

[613] KHI, through Colpitts, made threats to Wadden that he was a still an insider and that he could not sell KHI shares, except with the consent of KHI, and in particular, not during "closed" periods. Colpitts advised that his resignation as a director had not yet been accepted by the KHI Board.

[614] Wadden became more frustrated, and, on July 17, hired and first met with Brian MacLellan Q.C., a corporate lawyer.

[615] Shortly before this time, in response to pressure from Wadden, Potter had caused 120,000 shares, held by one his numbered companies, to be transferred to Wadden's NBFL account to replace some of the 220,000 KHI shares that Wadden had placed in what he thought was KHI's orderly market account. He was trying to take the financial pressure off Wadden by giving him or shares against which to borrow on in Wadden's margin account.

[616] On July 17, MacLellan sent an e-mail to Wadden outlining his understanding of his retainer. It included three things: (1) arranging a sale of 250,000 KHI shares to Potter; (2) obtaining the return of the remaining 100,000 KHI shares that Wadden thought was in KHI's orderly market account at NBFL; and, (3) arranging to free up the KHI shares he had transferred from FCG to BMO, and which BMO was not prepared to let him sell without paying off his margin debt.

[617] MacLellan worked in respect of these three objectives for about one month without success. Without explanation, his services were terminated by Wadden on or about August 24.

[618] On the early morning of August 24, Wadden, who up to that point had refused to speak to Potter, met with Potter for breakfast and later that morning attended KHI's Board of Directors meeting.

[619] I conclude that on or about August 23, Wadden had an epiphany. He realized that there was no market for large quantities of KHI shares. He realized that it was not that Potter did not want to find a buyer for Wadden's shares; Potter could not find a buyer for his shares. He seems, by this about-face, to have realized that there was little liquidity in KHI shares and his KHI shares were not money in the bank.

[620] His only hope was to assist Potter to find substantial investors. This included helping to maintain the market price of KHI shares, until KHI had new investors.

[621] The actions of Wadden from August 24, 2000, until the end of August 2001, when KHI collapsed, clearly demonstrate his efforts, with those of others, including Potter, Colpitts and Clarke, to manipulate the share price of KHI shares while looking for new financing and investors.

[622] This conclusion is based mostly on the documentary evidence generated in 2000 and 2001.

[623] In early March 2000, Potter asked Wadden to lend KHI's orderly market account 100,000 KHI shares. Wadden understood Potter was asking for the same from the other major shareholders. The purpose was to support the buying and selling of KHI shares in KHI's orderly market account, which was offside. While a more savvy person might, at this point, have asked more questions or investigated the operation of the orderly market account, Wadden did neither. He immediately retrieved his only available share certificate and endorsed it in accordance with the request of Potter, then provided it Potter's assistant to deliver to NBFL.

[624] I am not satisfied, on a balance of probabilities, that at that time, Wadden was aware that the account was not an account in the name of KHI and that it was not being operated in accordance with the applicable securities regulations and stock exchange rules. I am satisfied that he understood it simply to be a mechanism to smooth out the buying and selling of KHI shares.

[625] Because the only share certificate available to Wadden at that time was one in the amount of 220,000 KHI shares (he received five certificates of 220,000 KHI shares in exchange for his interest in Micronet), he simply, as requested by Potter, endorsed it and gave it to Potter's assistant to deliver to Clarke at NBFL. He did not ask for return of the remaining 120,000 KHI shares in a new certificate. He did not pay attention.

[626] Wadden later asked for the return of his 120,000 shares when he realized that the other founding share holders were resisting Potter's entreaty to contribute. I find that Wadden did not know how the orderly market account was operated or that it was operated in a manner that was in violation of securities regulations and stock exchange bylaw.

[627] NBFL submits that the McInnis e-mail of February 3, 2000, to Clarke, copied to Wadden, is evidence that Wadden knew of the 540 account, or a similar account in the name of KHI, and that the account was being used in contravention of securities laws. I do not read that e-mail as supporting that submission. The reference in that e-mail is to the 40,000 KHI shares of Dunham and Wilsack, required to be sold by them, to pay KHI the $281,000.00 they owed KHI as calculated in February 2000 audit respecting the sale of Innovative to KHI. In fact, Clarke sold these shares for Dunham and Wilsack, not for KHI, or through the 540 account.

[628] For the purposes of NBFL's submission, I note that the e-mail does not refer to the 540 account or a KHI orderly market account. The last sentence in the e-mail refers to the use of the shares to support the market or fill pending orders.

[629] I do not draw the inference from the e-mail that Wadden was aware at that time of what I find Clarke was doing to support the market illegally.

[630] On June 9, 2000, after Potter had arranged for 120,000 KHI shares held in one of his numbered companies to be transferred to Wadden to replace 120,000 of the 220,000 KHI shares of Wadden in the 540 account, Clarke faxed Wadden a letter setting out that the 220,000 KHI shares were in Clarke's private 540 account; that 120,000 had been returned to Wadden's personal account, leaving him with 100,000 KHI shares in the 540 account; and that Potter had place 120,000 KHI shares and $100,000 in cash in the 540 account. Clarke asked Wadden to sign and return a copy of the letter; Wadden's evidence is that he did not do so.

[631] I was not satisfied with Wadden's evidence respecting the fax sent to him by Clarke on June 9, 2000. His evidence was simply that he did not have an arrangement with Clarke. The fact that he did not sign a copy of the letter acknowledging its contents, does not answer his claim that he was unaware that his shares had been put into the trading account of Clarke's numbered company. There was no evidence before the Court, oral or otherwise, that when Wadden received the June 9 letter he took issue with its contents. In fact, he appears to have been satisfied with the fact that he was contributing 100,000 KHI shares to the KHI cause.

[632] I conclude that Wadden knew, by mid-June 2000, that the account into which his KHI shares had been placed was the 540 account of Clarke's private company.

[633] MacLellan's July 17 memorandum, summarizing his retainer after his initial meeting with Wadden, Greenwood and Richards, identifies the return of the 100,000 KHI shares belonging to Wadden and held in an NBFL account as an issue. In MacLellan's oral evidence, upon review of his notes, he confirmed that Wadden was aware and had advised him that the shares were in Clarke's numbered company account. It appears to have been MacLellan who was unclear of the basis on which Wadden's shares were deposited with NBFL.

[634] MacLellan's July 20 letter to Clarke is premised on this understanding. His follow-up letter to Clarke's manager Hicks on August 2 maintains that understanding. Clarke's August 4 reply to MacLellan, drafted by Colpitts after a meeting on August 3 with Clarke and his manager Hicks at

the NBFL office, simply repeats what the June 9, 2000, letter from Clarke to Wadden previously set out.

[635] Late on August 3, 2000, MacLellan left a voice message for Colpitts, in which he refers to Colpitts' phone call to him from NBFL's office that afternoon. The message is clear that MacLellan then understood that Wadden's shares had not gone to NBFL but to Clarke's numbered company account. MacLellan tells Colpitts in the message that he could stop writing about the shares if Colpitts' people had the ability to give NBFL 100,000 KHI shares so that Wadden could receive his 100,000 shares back.

[636] It was against NBFL policy for Clarke to be doing business with a client without approval from NBFL's head office. It was negligent for NBFL not to have been supervising Clarke's 540 account and therefore not know about the issue raised by MacLellan with Clarke. This does not change the fact that at least from the time Wadden received the June 9, 2000, fax from Clarke, he knew where his shares were, even if he did not know precisely how they were being used.

[637] After Wadden's epiphany on August 23, and meeting with Potter early August 24, several communications evidenced participation in the scheme to support the KHI market price. Neither Clarke nor anyone at NBFL was the registered market maker with the TSX for the KHI shares. That was a Mr. Watson with BMO.

[638] Whether or not Clarke was satisfied with Watson's performance of his job, it does not change the fact that the scheme by which Clarke assisted KHI insiders to artificially support the KHI share price was a breach by Clarke and NBFL of their respective contractual obligations as stock broker and stock brokerage company.

[639] The fact that MacLeod deposited 100,000 KHI shares into Wadden's account on August 29 to free Wadden from any financial support of the 540 account does not diminish the evidence of Wadden's involvement in the scheme. He was still the second largest share holder in KHI and his financial well-being was dependent upon KHI's increasingly precarious and fragile financial situation. I reject the submission that Wadden made peace with Potter and went along with the scheme under duress only because Potter and Colpitts would prevent him from selling any shares if he did not go along. Rather he realized that his only hope was for Potter to find wealthy individuals or institutions to buy, and keep the KHI market price up in the meantime.

[640] Immediately after Wadden made peace with Potter, he was asked and agreed to take on the responsibility of investor relations for KHI, effective September 1, 2000.

[641] When Ristow and Barthe agreed to subscribe by private placement to purchase 600,000 KHI shares for $3,250,000.00 in four equal instalments, payable on November 15, 2000 and January 15, May 15 and August 15, 2001, Wadden was part of the team of KHI insiders attempting to maintain the share price.

[642] Ristow was in the process of opening an NBFL account during the week of Monday, November 13, 2000. At the same time, Colpitts' law firm was preparing the agreements and documents for submission to the TSX for their approval of the private placement, which approval was conditionally received on November 21, 2000.

[643] In that context, Potter e-mailed Wadden, with a copy to Colpitts, on November 19, 2000, advising Wadden that ". . . we don't have a liquidity solution at the moment, but we meet with the shareholders tomorrow." He goes on:

> As you know, we are closing on a $3,250,000 treasury issue to our German friends - we are hoping to get this completed (closed) on Monday or Tuesday (November 20 or 21). The price of this issue is $6.50 per share. If the market is driven down in advance of this issue, it is quite likely that the investors will not close. This would be most harmful for the company and all of its shareholders, including Steve. Hopefully he will be convinced to proceed with care, prudence and caution.

[644] At a board of director meeting on August 24, 2000, attended by Wadden, the Board authorized the exercise of the call option on the KHLP units. On December 21, 2000, KHI gave notice of the exercise of the option to redeem the units for KHI shares before January 1, 2001.

[645] On January 1, 2001, Potter e-mailed Wadden:

> This is just a note to let you know that there _______ significant selling pressure on KHI on December 29th - about 40,000 shares offered which did not get bought by the end of the day - 20,000 out of Montreal, 15,000 from former CDE employees etc. I assume they will be back on Tuesday, January 2nd. If you can be of any assistance in helping to find some buyers, that would be great. We have been and will continue to be working on this in the coming days, but I am concerned that the selling may exceed any support bids we can engender in the next few days.

[646] On or about January 4, (transcribed January 5, 2001), Wadden left a voice message for Blois Colpitts:

> Hello Blois, is Calvin calling. Just talking to Dan and he had give me an idea with the LP being converted back - there were shares available and he expedited those over to Bruce to allow some support from his account and just . . . and I'm going to ask Bruce to do the same for mine if you can - this is an authorization, I guess, if that's okay with you, to send them over and if you see maybe a pick up, well maybe 20,000 shares in the market with that use in the leverage - I guess as long as National approves it, I'm going to give them a call right now and see if that's okay on his side and maybe you can give him a call when you get a second.

[647] At 10:50 a.m. on Thursday, January 4, Wadden e-mailed Colpitts: "Please forward my share certificate for the converted LP to Bruce as soon as possible. I will be depositing to my margin account and will be able to give to help Bruce take 20,000 shares of KHI out of the market if we can do this today. Thanks."

[648] The same day Clarke's sale assistant acknowledged receipt of Wadden's share certificate for 28,125 shares. Immediately following the transfer, Wadden used the new margin available in his NBFL account to buy 20,000 KHI shares. At 11:57 a.m. on January 4, Potter e-mailed Wadden, in part: "Thanks for the participation in purchasing shares."

[649] Wadden's motive for wanting to support the market price of KHI shares is reflected in his January 17 e-mail to Potter:

> I am sure this is no surprise Dan and is not a plea for assistance, but I am personally extended to the limit and not able to come up with a solution for this new wrinkle. If you have any ideas you would like to put forward, I would like to hear from you. I had a margin call today from Yorktown on my personal account for $60,000 due to the close of KHI at $5.60. I am sure this is the last thing you need to hear, but $5.90 to $6.00 is where my account is not under pressure. Also Bruce has my account at National margined and becomes an issue and under pressure at under $5.90. . . .

[650] On January 22, 2001, Clarke advised Wadden that his margin account at NBFL, with outstanding debt of $1,140,000.00, was under margin by $69,000.00. He set out some scenarios that would get it on-side.

[651] On January 31, Wadden replied to Clarke that he would like to cross 60,000 shares of ITI and replace the value with KHI shares and cash. He added:

> I have noted the KHI price today is $5.40 but I am using $5.10 for my calculations. This should cover any margin requirements and provide a cushion if the stock continues in the $5.15 to $5.40 range. Please let me know as soon as possible as I'm heading to Toronto Thursday morning and would like to have this completed by then.

[652] The same day, Wadden e-mailed Potter, in part, as follows:

> I haven't heard from you since last week so I thought I would drop you an e-mail. From the look of the market, it seems that we have had success in stabilizing the market and I hope we can look forward to better days ahead. I'm glad to see Donnie [Snow] working as part of the team, as well as Ray and I communicating again.

[653] On February 1, Potter replied to Wadden, in part:

> Regarding the market, while we have had a few easier day, our support buying capacity is currently nil. We badly need a few interested buyers over the next few days. Important sales at KHI are going well and we now have 1.1 million committed in the private placement - it's a challenge but we're making progress.

[654] On February 8, Wadden again e-mailed Potter under the heading "market support":

> I have been speaking with Ray, Blois and Ken throughout the day and they have been in supporting the market. Ray and I would really like to get stock to $5.45 and try to solicit more support from the group going forward. If we can get to $5.45 to $5.50, I would like to see each of us put 5,000 shares into the support side and try to inch up toward $6.00 to $6.50 until we get some positive news on the street. If we could come up with a formula to provide support, say 5,000 shares each, at each 15 to 20 cent gain forward, we could be building some reserve and give each of us some breathing room until we attract substantial buyers. . . . Ray and Ken each purchased 4,000 shares today and have agreed to pick up an additional 1,000 shares each by the close. Blois and I bought as well. Aside from all the bad feelings, it was good to see the team work this afternoon. ...

[655] The next day, Potter e-mailed the other five insiders (Schelew, Wadden, MacLeod, Courtney and Colpitts) under the subject heading "Coordination - Investor Relations, etc. by Calvin", in part, as follows:

> This memo confirms my telephone conversations with each of you regarding formalizing an arrangement with Calvin, whereby he will take on an active role of investor relations consulting on behalf of KHI on a month-to-month basis for $5,000 per month. This role will include overall coordination of all day-to-day retail market support as well as specific initiatives, including, but not limited to: acting as the "administrator" under the "managed selling agreement" (Blois, we need to get this written up ASAP . . . acting as the coordinator of the major shareholder group (the six of us who sign the managed selling agreement) for all purposes, including meetings and other discussions and actions regarding market support . . . acting as main day-to-day coordinator with some market makers in KHI shares, including Bruce Clarke and any others that are brought in from time to time . . .

[656] Wadden explained at trial that this e-mail followed a meeting at Colpitts' office of those receiving the e-mail, during which Potter stated a belief that these shareholders were selling shares on the market. Potter was not prepared to continue supporting sales on the market if, as he believed, he was supporting sales by the founding shareholders. Either "we" were to help support the market or he was moving to Vancouver and we were all going bankrupt. Wadden acknowledged KHI was fragile at that point. He stated that Potter did not believe that these shareholders were not out selling shares and wanted us to all show our investment account records each month.

[657] The Court notes that the trading records in the week leading up to this February 9 e-mail, the Waddens sold in 17 transactions about 12,000 KHI shares (with settlement dates on February 8 and 9). Beginning the next week (settlement date February 15), Wadden made 35 purchases of KHI shares between the price of $5.70 and $4.99.

[658] On February 13, Wadden responded to a Steve Wilsack e-mail, in part, as follows:

> I had a meeting with Ken, Dan, Ray, Bernard at breakfast . . . I made a point to tell the whole table you are not selling into them, you are actually buying (big impact and helped me convince Ray and Bernard to support and help put the stock in the $6.00 plus range) . . . Dan and crew (Bernard, Blois, Ray and Ken) voted to put me on retainer 5,000 a month. Nice to feel wanted again but the answer was no! I am in this for my own benefit and they know it. My position is if we work as a team for our mutual benefit we all win big time. . . . Give me a call and keep an eye on the market! I can honestly say I is the reason the damn stock ain't at $4.00. I am working for the shareholders!

[659] In an e-mail exchange the next day (February 14) Wadden wrote to Schelew, in part:

> I spoke with Bruce Clarke just minutes ago and he has Dan's stock and Ken is also buying. Thanks for the team support! I am confirming Ray's stock today. Bruce has mine and should be in good shape this week. I was also speaking with Donnie Snow last night and I asked him to pledge stock in an account with us for support if need be. At first he said definitely no but I wore him down to a maybe. He will be part of the solution, I'm sure!

[660] On February 19, Potter e-mailed the five insiders to the effect that Calvin and he had just spoken today by telephone and are asking that we all meet tomorrow ". . . to discuss further market support including by us directly, through an investment account to which we all contribute some shares and by working with third parties such as Doug Rudolph."

[661] On February 21, Schelew gave Wadden a summary of his investment in KHI. He reported he had not sold any KHI shares, but after reviewing his financial situation "... I'm afraid I can't participate in any more rounds of buying."

[662] In a March 1 e-mail from MacLeod to Potter, Wadden, Courtney and Schelew, it is clear that the news from the market was all bad and that "... on the staying alive side, there's still a lot of if's ..." He comments on "Calvin's latest brain wave" of a sale of a bulk of their shares at a discounted price to Keating as a way that "... the company has a much better chance of surviving in the short term."

[663] Even Potter's e-mail to MacLeod, Schelew, Wadden, Courtney and Colpitts early the next morning was pessimistic. He noted Wadden's willingness to offer to Keating or Fountain to sell 1.4 million shares at a $1.83 (the amount of his margin debt on the shares), in order to get a substantial investor on board. Potter added a strong recommendation that the five major shareholders, as a team, immediately commit to buy 5,000 more shares while they work on the options.

[664] On Friday, March 2, Wadden e-mailed MacLeod, Potter, Schelew, Courtney and Colpitts following a meeting to discuss market support. He wrote, in part:

> As of yesterday, the only additional support for KHI was Dan and I'm sure there is a limit to that. If everyone does not have the ability or desire to purchase shares again today, I am once again saying that I will not participate without everyone in the group involved. This is a difficult time for everyone, but it was evident to me that without market support "the five of us" all buying at the same time, we were faced with a tough decision. I am still putting my hand up and will be prepared to sell my stock to clear my outstanding margin and leave something at the end.

[665] Wadden testified that he pulled his offer to sell to Keating his shares for the amount of his margin debt because of tax advice he received.

[666] On March 6, Colpitts e-mailed Wadden, Potter, Schelew and MacLeod to state that he had spoken to Schelew about Wadden's withdrawal of his offer and Schelew was prepared to do a deal as long as Courtney, MacLeod, Wadden and Potter agreed to provide proportionately 100,000 of market support "conditional on the managed selling agreement previously discussed", a draft copy of which had been prepared and circulated by Colpitts.

[667] In a March 19 e-mail to Schelew, Wadden, MacLeod and Courtney, Potter asked for a get-together the next day, to discuss "the private placement, managed selling agreement, market support matters" and that it was critically important that all attend. He stated that Wadden would call them to follow up.

[668] On July 8, Wadden e-mailed Potter from outside of Canada thanking for him updates and adding:

> I noticed we are under pressure in the market again. I wonder if Bernard had any more thoughts on lending or selling his stock to use for support. My own financial issues aside, I think we all could do a little more on the positive front to change the direction of the pressure. I think we should have a talk

> with everyone again. Seems to me that some of the team are running for cover and by doing so putting a negative cloud over our efforts. I understand Ray is continuing to move assets around and is working with his lawyer and Eric on the details. I also know Blois is frustrated and may sell his stock to just cover his margin (plus $1.80). Blois mentioned that me one day and I'm not sure if he was serious or just frustrated as we all are.

[669] These are only some of the communications involving Wadden and the stock manipulation scheme. The stock transactions by Wadden and his family coincide with the communications.

[670] I conclude that Wadden was actively involved with Potter, Colpitts, Clarke and others in artificially manipulating the stock price of KHI shares, not for the purpose of facilitating an orderly market, but rather for the purpose of maintaining the price to protect their margin debts and the value of their shares, until such time as they could put together a business plan sufficient to attract wealthy investors.

E. Causation

[671] NBFL argues that even if Clarke is found to have breached the applicable standard of care, liability is not established because Clarke's actions did not cause the losses experienced by the Dunlop Clients. NBFL submits that with the exception of Blackwood, none of the Dunlop Clients sought or relied on any advice of Clarke regarding the acquisition of KHI shares. NBFL notes that a number of the Dunlop Clients acquired their KHI shares as payment for purchases of their businesses or through the conversion of KHI Limited Partnership units.

[672] The Dunlop Clients do not make a common submission on causation. Dunham argues that but for Clarke's failure to disclose the existence of the 540 account, Clarke's relationship with insiders, and Clarke's conflict of interest, he would never have deposited his KHI shares with NBFL. The Barthe Estate argues that but for this non-disclosure, Barthe would never have invested in KHI. Wadden does not argue non-disclosure (at least in the post-trial brief) and instead argues that NBFL wrongly converted his shares, at least temporarily, and thus exposed him to risk of a future decline in share value. Weir and Blackwood argue that but for Clarke's failure to execute their sell orders, they would not have been holding KHI shares when the stock collapsed.

[673] In their rebuttal brief (May 31, 2012), the Dunlop Clients alter their submissions on causation and submit that Clarke's fraudulent misrepresentation both vitiates their respective margin debts owed to NBFL and grounds the secondary liability they claim for the collapse of KHI. Dunham, Weir, and Blackwood contend that this concealment induced them to invest on margin. Wadden argues that the concealment prevented him selling his shares in a timely manner, which forced him to acquire the margin debt. The rebuttal brief is silent on the claim of the Barthe Estate.

[674] From a pleadings perspective, it is important that any purported claim or defence be included in the pleadings (*Rowe v New Cap Inc.* (1994), 134 NSR (2d) 52, 1994 CarswellNS 186 at para 15 (SC)). There may be some leniency for giving pleadings a broad and generous interpretation where litigants are self-represented (*Sullivan v Victoria (City)*, 2010 BCSC 218 at para 2), but even self-represented litigants are expected to comply with the requirements of pleadings (*Sokol v*

Photonics Research Ontario, 2009 CarswellOnt 521 at para 21(Ont Sup Ct J); *Benson v United Steel Workers Inter-Alia Brotherhood of Maintenance of Way Employees*, 2008 MBQB 94 at para 14). Lawyers are expected to do a better job.

[675] In my view, the allegation that Clarke committed a fraud, in manipulating the market in KHI, has always been part of this case from the pleadings stage onward. The Dunlop Clients' claim has always been that Clarke actively concealed his manipulation, not that he was careless in his actions. Counsel for the Dunlop Clients advanced a claim for careless omission of material information and then proceeding as though the case were advanced as a deliberate omission of material information. The tests for negligence and breach of contract, and fraud, are different. The Dunlop Clients' post-trial submissions do not clearly delineate the specific cause of action and test that applies. Nonetheless, I am satisfied that the Dunlop Clients have adequately pleaded fraud as a defence to the margin debt claims of NBFL.

[676] Therefore, for the purposes of this decision, there are two tests that are relevant: 1) the test for fraudulent misrepresentation as a defence to the NBFL debt claims, and 2) the test for negligence or breach of contract for the Dunlop Clients' claims against NBFL.

[677] To establish fraudulent misrepresentation as a basis for rescission of a contract, the plaintiff must prove, on a balance of probabilities, that the defendant: (1) made a false representation; (2) deliberately or recklessly; (3) with the intention of inducing the plaintiff to contract, and (4) that the plaintiff was induced to contract to his/her detriment (*United Shoe Machinery Co. v Brunet*, [1909] AC 330 (PC); *Royal Bank v Druhan* (1997), 163 NSR (2d) 174, 1997 CarswellNS 438 (CA)). Whether the claim is in tort or in contract, a plaintiff must establish that the defendant's actions or omissions were at least a proximate cause of the damages suffered.

[678] Active concealment by silence or non-disclosure of a material fact can constitute a false representation *(Bank of British Columbia v Wren Development Ltd* (1973), 38 DLR (3d) 759 (BC SC); *Wallace v Gummerson* (1915), 8 OWN 35, *Ruthenian Farmers Elevator Co. v Hrycak*, [1924] 3 DLR 402 (Sask CA); *Leeson v Darlow* (1926), 59 OLR 421 (Ont CA)). However, the Dunlop Clients face two difficulties in establishing fraudulent representation as a defence to their debt obligations. Firstly, active concealment of market manipulation must be held to be a misrepresentation. Secondly, this misrepresentation must have induced the Dunlop Clients to contract.

[679] Market manipulation is a form of representation. The very purpose of market manipulation is creating an artificial stock price or trading volume that induces investors to buy or sell the stock in question. It follows that failure to disclose market manipulation can constitute active concealment or non-disclosure of a material fact for the purposes of meeting the fraudulent misrepresentation test.

[680] I am satisfied that Clarke actively concealed his market manipulation scheme from his clients. The problem, however, is that the Dunlop Clients were not universally induced to open margin accounts with NBFL as a result of this misrepresentation. Wadden's margin debt was assumed by NBFL when his account was transferred. Weir did not start his margin account for the

purposes of purchasing KHI shares. Dunham was advised by Clarke to open a margin account, but not for the purpose of purchasing KHI. In short, none of the Dunlop Clients were induced by Clarke's market manipulation to open margin accounts. This is fatal to any claim for rescission as a result of fraudulent misrepresentation linked to the market manipulation.

[681] With that said, Clarke's actions constitute fraudulent misrepresentation with respect to the Weirs. Weir testified that he opened his margin account initially for cash flow purposes because a KHI share certificate had yet to arrive in his account and he wanted to buy a car for his wife and meet an RRSP contribution deadline. Weir further testified that Clarke advised, as of February 28, 2001, that the share certificate had not arrived. The documentary evidence shows that the share certificate did in fact arrive on February 28, 2001.

[682] I infer that Clarke's misrepresentation was for the purposes of getting Weir to open a margin account and not sell their KHI shares. In this circumstance, rescission is a remedy available to the Weirs.

[683] Rescission is obviously available to Dunham for breach of fiduciary duties.

[684] Full rescission may not be available where it has been established that the Dunlop Clients received an enduring benefit from the margin debt accrued, such as the Weirs' purchase of an automobile. It would not be equitable to absolve the Weirs of this component of their debt obligation to NBFL. Moreover, inducement is extinguished once the misrepresentation is disclosed (*Burrows v Burke* (1984), 49 OR (2d) 76 (CA), leave to appeal to SCC denied (1985), 10 OAC 354 (SCC)). Once the Weirs learned that the share certificate was in their account, any inducement to maintain the margin account was extinguished.

[685] Causation in the context of secondary liability securities litigation is an evolving area of the law. Where there is a fiduciary relationship and the fiduciary breaches that relationship by failing to disclose a material fact, there is no need to establish what the plaintiff would have done with the information. Liability is established and proving causation is unnecessary *(London Loan & Savings Co v Brickenden*, [1934] 2 WWR 545 (Ontario PC); *Canson Enterprises Ltd. v. Boughton & Co.* (1989), 39 BCLR (2d) 177 (BC CA); affirmed [1991] 3 SCR 534; *Reidy Motors Ltd. v. Grimm* (1996), 38 Alta LR (3d) 131 (QB)); reversed in part on other grounds (1997), 52 Alta LR (3d) 343 (CA); leave to appeal to SCC refused (1997), 226 NR 315.

[686] Where there is no fiduciary relationship, the approach in Canada has tended to differ from that of United States. It is generally easier to establish liability in the United States. In *Chasins v Smith, Barney & Co*, 438 F.2d 1167 (2nd Cir. 1970), the United States Court of Appeals for the Second Circuit held that a stock brokerage firm's failure to disclose its legitimate market-making status, in a security that it recommended to a client, was a material non-disclosure sufficient to result in civil liability under the *Securities Exchange Act*.

[687] When the defendant's actions rise to the level of manipulation, the plaintiff must establish that "but for" the defendant's unlawful means, the loss would not have occurred *(Bastian v Petren*

Resources Corp., 892 F.2d 680, 685 (7th Cir. 1990), but there is a rebuttable presumption that a plaintiff has relied on a material non-disclosure or misstatement (See *Affiliated Ute Citizens v United States*, 406 US 128 (1972) and *Shapiro v Merrill Lynch, Pierce, Fenner & Smith, Inc*, 495 F.2d 228 (2d Circ. 1974) for examples of material non-disclosures; See *Blackie v Barrack* , 524 F.2d 891, 907 (9th Cir.1975) [Blackie] and *Basic Inc v Levinson*, 485 US 224 (1988) for examples of material misstatements). The reason for this rebuttable presumption of reliance is the "fraud on the market" theory, which the 9th Circuit explained in Blackie as follows:

> A purchaser on the stock exchanges…relies generally on the supposition that the market price is validly set and that no unsuspected manipulation has artificially inflated the price, and thus indirectly on the truth of the representations underlying the stock price-whether he is aware of it or not, the price he pays reflects material misrepresentations.

[688] The Supreme Court of the United States reaffirmed the "fraud on the market" theory in *Dura Pharmaceuticals, Inc v Broudo*, 125 S Ct 1627 (2005). There, the Court held that there is a rebuttable presumption of reliance, but that the plaintiff must establish that the defendant's manipulation was a proximate cause of the economic loss suffered. In proving such causation, the Court rejected the argument that there must be a direct link between disclosure of the alleged misstatement and the price drop/economic loss.

[689] In *Carom v Bre-X Minerals Ltd* (1998), 41 OR (3d) 780, 1998 CarswellOnt 4285 (Ct J (Gen Div.), Winkler J (as he then was) rejected the application of the "fraud on the market" theory in Canada:

> 35 This is a pleadings motion and the amendments sought must be granted unless, to use the language of the Supreme Court of Canada in Hunt, supra, it is plain and obvious that the assertion is certain to fail because of a radical defect. In my view, there are several radical defects in the proposition that it would be open to an Ontario court to find that the presumption created by the fraud on the market theory is applicable to the torts of fraudulent or negligent misrepresentation.
>
> 36 In the United States the fraud on the market theory has one application: it is asserted in a cause of action founded on a breach of a statutory duty. Here, the plaintiff's seek to apply the fraud on the market theory and the resulting presumption to common law causes of action. They also seek to apply the theory in these actions without the limitations which circumscribe its application in the United States. However, the nexus, between the plaintiffs' claims and the theory, is absent without the necessary statutory framework from which it emanated. Moreover, attempts to advance the theory in common law actions in the United States have been almost unanimously rejected, and no appellate court there has approved of the theory in the context of such actions. The theory was developed in support of a legislative objective directed at securities fraud and the cause of action is accordingly circumscribed by two important limitations of the statute, as judicially interpreted, specifically the unavailability of punitive damages and a shortened limitation period. In contrast, punitive damages are available under the common law torts, are claimed in the instant proceedings and the limitations periods here are significantly longer than under the U.S. statute.
>
> 37 Furthermore, the s. 10(b) and Rule 10b-5 legislative objectives have been interpreted as providing a cause of action based on fraudulent behaviour. See Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A., 511 U.S. 164 (U.S. Colo. 1994) In the instant case, the plaintiffs

allege as against all the defendants, inter alia, fraudulent misrepresentation, negligent misrepresentation and a breach of the Competition Act with the exception that fraudulent misrepresentation is not alleged against the SNC-Lavalin Group. The plaintiffs seek to obtain the benefit of an application of the theory and the resulting presumption to all of the pertinent causes of action as alleged, even though fraud is not an element of all such causes of action.

38 Finally, as noted, central to the development of the theory's presumption of reliance aspect in the United States is the requirement of a predominance of common issues for class action certification under Rule 23 of the U.S. Federal Rules of Civil Procedure. The presumption of reliance was adopted in part as a means to counter attempts by defendants to defeat the certification of Rule 10b-5 actions as class actions on the basis that individual issues of reliance predominated. In comparison, the predominance of common issues requirement has not been incorporated into the CPA in Ontario. As Moldaver J. stated in Abdool at 471:

> ...Likewise, I must respectfully disagree with [the] statement that the Act was not intended to be used in circumstances where the individual issues to be determined could be said to predominate the common issues. As will be seen, while I am of the view that individual issues ought not to be completely ignored when considering whether a "class proceeding would be the preferable procedure for the resolution of the common issues" as required under s. 5(1)(d) of the Act, I cannot accept that the legislature intended to incorporate the predominate issue test into the Act.

39 The adoption of the fraud on the market theory by an Ontario court cannot be justified where neither the statutory duty, the cause of action founded upon its breach, nor the predominance test as a procedural barrier to class proceedings exist. More so, the plaintiffs seek to apply the theory to common law causes of action, to which it would not be applicable in the United States, and in a wholesale fashion, without the restrictions which circumscribe it there. Simply put, the proposition advanced is ill-conceived.

40 The torts of fraudulent and negligent misrepresentation are neither novel nor undeveloped in Canada. Both have been canvassed by the Supreme Court of Canada and the pronouncements of that court on the elements of each must be considered to be settled law. In my view, the presumption of reliance created by the fraud on the market theory can have no application as a substitute for the requirement of actual reliance in either tort. In the context of the torts of fraudulent and negligent misrepresentation a presumption of the nature advocated for by the plaintiffs does not exist in Canadian common law. Indeed, to import such a presumption would amount to a redefinition of the torts themselves.

[690] This approach was followed in *CC&L Dedicated Enterprise Fund (Trustee of) v Fisherman*, 2001 CarswellOnt 4206 (OSCJ) at paras 59 to 62.

[691] In *Kripps v Touche Ross & Co* (1997), 33 BCLR (3d) 254, 1997 CarswellBC 925 at para 98, leave to appeal to the SCC refused 225 NR 236, the British Columbia Court of Appeal held that establishing actual reliance was necessary, but

> that liability may be found where the plaintiff's reliance on a fraudulent misrepresentation is only one of several factors inducing her to act. And it held, relying on Parallels Restaurant, supra, that where a defendant has made a material misrepresentation calculated to induce the plaintiff to act as she did, and where the loss is consistent with the plaintiff having acted on the misrepresentation alleged, the burden of proof shifts to the defendant to prove that the plaintiff did not rely at all on that misrepresentation.

[692] The Court then proceeded to extend these principles in the context of negligent misrepresentation.

[693] The underlying principles behind the "fraud on the market" theory are not limited to the American statutory context. Price and volume are proximate factors on which any purchaser of a security relies, at least to some extent.

[694] It is not necessary to apply the “fraud on the market” theory to the circumstances of any of the Dunlop Clients. Clarke was an agent of each and in breach of his duty of honesty and good faith. He participated in a deliberate scheme. It would be contrary to common sense to suggest that Barthe would have not considered and relied on price and volume of KHI transactions in agreeing to invest in KHI at $6.50 per share, or that Dunham or the Weirs would not have insisted on sale of their shares but for the apparent price and volume of trades. This is clearly reflected in Dunham’s reaction to Clarke offering to sell KHI shares at the time Barthe was buying; Dunham noticed the activity in the stock and Clarke had to convince him to sell.

[695] Since the Dunlop Clients have not advanced a claim for fraudulent or negligent misrepresentation, reliance is not an explicit element of the applicable test, and the only question is whether general negligence or breach of contract causation is established.

[696] Recently, in *Clements (Litigation Guardian) v Clements*, 2012 SCC 32, the Supreme Court of Canada reviewed the law on causation in Canada, in the context of a negligence claim resulting from a motor vehicle accident.

[697] The Court reaffirmed that the "but for" test is the normal test to apply, and held that the "material contribution to risk" test is only to be applied in situations where there are multiple tortfeasors collectively responsible for the loss and it is impossible for the plaintiff (through no fault of their own) to identify which specific tortfeasor caused the loss on a "but for" basis. The Court also made some helpful comments on how to apply the "but for" test:

> The "but for" causation test must be applied in a robust common sense fashion. There is no need for scientific evidence of the precise contribution the defendant's negligence made to the injury.

[698] A common sense inference of "but for" causation from proof of negligence usually flows without difficulty. Evidence connecting the breach of duty to the injury suffered may permit the judge, depending on the circumstances, to infer that the defendant's negligence probably caused the loss.

[699] Where "but for" causation is established by inference only, it is open to the defendant to argue or call evidence that the accident would have happened without the defendant's negligence, i.e., that the negligence was not a necessary cause of the injury, which was, in any event, inevitable [citations omitted] (*Clements* at paras 9 to 11).

[700] Case law applying the "but for" test in the securities context is consistent with the common sense approach to the "but for" test advocated by the Supreme Court of Canada. This is important

because investors will often be faced with arguments that they would have acted in a particular manner despite the defendant's breach; such arguments may be hard to dispel if the plaintiff is required to establish, with scientific exactitude and ignoring the benefits of hindsight, what he/she would have done.

[701] In *Northey-Taylor v Casey*, 2007 ABQB 113 at para 62, additional reasons at 2007 ABQB 306, aff'd 2008 ABCA 149, the Court rejected the defendant stock broker's submission that the plaintiffs would have proceeded with the purchase even if they were adequately advised of the risk and held "that the focus should not be on the allure of the transaction but the fact that the Plaintiffs were denied the chance to make an informed decision." In *Chasins v Smith, Barney & Co*, 438 F.2d 1167 (2nd Cir. 1970), the United States Court of Appeals for the Second Circuit held that a stock brokerage firm's failure to disclose its market-making status, in a security that it recommended to a client, was a material non-disclosure sufficient to result in civil liability under the *Securities Exchange Act*. The Court reasoned that the focus was not on whether the firm sold the security at a fair price, but whether it deprived the plaintiff of information that would have influenced his decision to purchase the security.

[702] In this case, the only Dunlop Client who was aware of Clarke's activities was Wadden, and he only learned of the 540 account at a later stage. It is true that Clarke did not generally advise the Dunlop Clients to purchase KHI, but the evidence establishes that Dunham, at the very least, would have diversified his holdings "but for" the actions of Clarke, and the Weirs would have insisted on their January 19, 2001, e-mail instruction to sell “but for” the actions of Clarke. These actions included deliberate refusals to execute sell orders and the creation of an artificial price and volume in the KHI shares. The evidence suggests that Weir, in particular, relied on this price and volume information in his decisions to not insist on selling at $5.00 at particular points.

[703] There is substantial evidence linking Clarke's market manipulation to the collapse of KHI. The manipulation may not have been the only reason for KHI's collapse, but it was a fundamental factor, and at the very least, prolonged the time before there was an ultimate reckoning in the price of KHI. This prolongation allowed Barthe to be brought in and defrauded by the conspiracy between Clarke, Potter and Colpitts. The market manipulation deprived Dunham and Weir of the information they needed to make informed decisions with respect to their portfolios.

[704] From the evidence of Clarke's market manipulation, which was a serious breach of the standard of care, even at the most basic level of an order taker, and the linkage between this manipulation and the losses suffered by the Dunlop Clients when KHI collapsed, it can be inferred that Clarke's wrongdoing probably did cause the losses suffered by Dunham, Weir and Barthe. I find that "but for" Clarke's failure to disclose his market manipulation and ongoing conspiracy, Dunham and Weir would have liquidated their entire position in KHI, and Barthe would not have purchased any stock in KHI. Subject to my finding respecting Barthe’s last two installments in the private placement, I find that Clarke caused the losses experienced by these Plaintiffs.

[705] The same cannot be said about Wadden. Wadden discovered the market manipulation and conspiracy. He was faced with a choice of losing everything and then suing to recover his losses or

participating in the scheme with the hope that Potter would be able to find a buyer to allow him to sell his shares and exit the conspiracy. He chose the latter.

[706] Wadden was certainly faced with a difficult choice, but it can hardly be said that "but for" the actions of Clarke, Wadden would not have suffered the losses he experienced. Wadden’s losses occurred after he assumed the risk and responsibility of holding the second largest stake in the equity of KHI.

[707] Wadden knew about the box account and that KHI was being manipulated by Clarke and others. He took a chance; it did not pay off. It was Clarke that pushed Wadden to the precipice, but it was Wadden who chose to remain there, and it is Wadden that must bear the responsibility for any damages that resulted from him falling off.

F. The Defence of Ratification

[708] NBFL pleads the defence of ratification. It argues that the Dunlop Clients' failure to complain about the transactions in their respective accounts means that they acquiesced, and therefore ratified, those actions of which they now complain. The Dunlop Clients argue that they could not ratify that of which they were unaware.

[709] In *Connolly v Walwyn Stodgell Cochran Murray Ltd* (1993), 121 NSR (2d) 278, 1993 CarswellNS 436 [*Walwyn*], the Court of Appeal held that a failure by the plaintiff investor to repudiate unauthorized trading on the part of his stockbroker meant that the plaintiff had acquiesced to the trading, and as a result of this ratification, could not claim against the brokerage firm for failure to supervise. The Court stated that when the plaintiff "first discovered the unauthorized trading, his only option so far as [the brokerage firm] was concerned was to terminate the contract" (*Walwy*n at para 18). See also *Grenkow v Merrill Lynch Royal Securities Ltd, MacFadden and Smith* (1983), 23 Man R (2d) 54, 1983 CarswellMan 278 (QB) [Grenkow] for the proposition that silence can amount to ratification.

[710] In *Forrest v Gairdner & Co* (1962), 33 DLR (2d) 575, 1962 CarswellBC 81 (BC CA), the British Columbia Court of Appeal held that the time period in which an investor was required to repudiate a transaction began to run when the investor knew or ought to have known of the transaction.

[711] There are two general situations where silence or apparent consent will not amount to ratification.

[712] The first is where the investor lacks knowledge of the transactions or the legal significance of these transactions (*Ryder v Osler, Wills, Bickle Ltd* (1985), 16 DLR (4th) 80, 1985 CarswellOnt 1423 at para 43; *Dixon v Deacon Morgan McEwen Easson*, 1990 CarswellBC 1726 at para 17). As the author of Bowstead & Reynolds on Agency, 17th ed (London: Sweet & Maxwell, 2001) explains:

> In order that a person may be held to have ratified an act done without his authority, it is necessary that, at the time of the ratification, he should have full knowledge of all the material circumstances in which the act was done, unless he intended to ratify the act and take the risk whatever the circumstances may have been. But knowledge of the legal effect of the act may be imputed to him, and it is not necessary that he should have notice of collateral circumstances affecting the nature of the act. [footnotes omitted]

[713] The second is where there is a fiduciary relationship between the broker and the investor, and the broker's actions breach that relationship to the extent that "it corrodes the very nature of the relationship itself" (*Williamson v Williams* (1997), 160 NSR (2d) 106, 1997 CarswellNS 283 at para 78 [Williamson]; See also (1996), *Penner v Yorkton Continental Securities Inc.*, 183 AR 5 (QB)). In *Williamson*, the Court of Appeal held that even though the plaintiff's acquiescence might have amounted to ratification in contract, the broker's breach of the fiduciary obligations of trust and loyalty owed to the plaintiff meant that ratification did not operate as a full defence.

[714] In a recent decision, *Hayward v Hampton Securities Ltd* (2002), 46 BLR (3d) 43, 2002 CarswellOnt 5919 (Ont Sup Ct J), the Ontario Superior Court of Justice reviewed this case law on ratification in the context of an investment advisor/client relationship that was covered by a deemed ratification clause. The Court noted that *Walwyn* and *Grenkow* "both involved sophisticated investors who, after acquiring knowledge of unauthorized acts, participated in schemes to conceal unauthorized transactions from the defendant brokerage firms" (*Hayward* at para 201).

[715] The Court concluded that even if ratification was available in a breach of fiduciary duty case, the plaintiff had not ratified the investment advisor's "exploitation of her trust and confidence." The Court held, at para 206:

> In my opinion she need not know the full legal effect of [her investment advisor's] actions but she did need to know the material circumstances surrounding his actions so that she could make an informed decision. This included knowledge that the rules of the firm and the industry did not permit discretionary trades in these circumstances. It also included knowledge of the change in the stated objectives for her account and awareness of the lack of suitability of the investments. Again like [in Williamson], the advice [the plaintiff] received from [her investment advisor] was that she need not worry, he was looking after her. She was not placed in a position to make an informed decision and in those circumstances her actions or inaction may not be treated as constituting ratification. Lastly, I accept her evidence that she repeatedly complained to [her investment advisor] about not trading without her authority to no avail. She felt powerless in the circumstances. It was clear that she did not intend to ratify his discretionary actions. In my view, he abused the trust she placed in him. He cannot now shelter under her inability to deter him.

[716] The relationship between Clarke and the individual Dunlop Clients varied, ranging from a mere order taker to a full fiduciary agent. These distinctions are irrelevant to the defence of ratification in the circumstances of this case.

[717] With the exception of Wadden, none of the Dunlop Clients were aware of Clarke's market manipulation scheme in KHI and his fraudulent behaviour. Even though the Dunlop Clients did not advance a case for fraudulent misrepresentation, deceit, or conspiracy, I am satisfied that they did plead fraud.

[718] "A contract induced by fraud is voidable" by the defrauded party (**GHL Fridman**, *The Law of Contract in Canada*, 5th Ed (Toronto: Thomson Carswell, 2006) at 293; *Farah v. Barki*, [1955] SCR 107; *TWT Enterprises Ltd v Westgreen Devs (North) Ltd* (1991), 78 Alta LR (2d) 62 at 78 (QB)). To the extent that the Dunlop Clients' apparent ratification is an independent contract, I am satisfied that it was induced by Clarke's fraud.

[719] More important, I am of the view that Clarke's market manipulation was a material circumstance that the Dunlop Clients must be found to have been aware of in order to find that acquiescence amounts to ratification. The various Dunlop Clients could not ascertain the suitability of Clarke's investment advice, his management of their accounts holding KHI, or his buy/sell decisions or omissions, without understanding that he was simultaneously manipulating the market in KHI.

[720] Dunham and the Weirs were not aware of Clarke's market manipulation activities. This defeats NBFL's ratification argument with respect to their claims.

[721] The situation is difference with regards to the Barthe and Wadden Claims.

[722] Barthe first became aware that Potter and others were supporting the stock in the January 19, 2001 fax. The contents of their communications with Potter thereafter clearly show a change in their attitude. As noted before, I conclude that Barthe (and Ristow) had their eyes opened with regards to KHI's market support program. There was no evidence at trial to suggest that Barthe (or Ristow) knew the time frame for that market support activity; that is, how long before January 19, 2001, it had begun. Further, there was no evidence before the Court as to the extent of the disclosure to Barthe and Ristow of that market support before January 19, 2001.

[723] I have also already determined that Barthe did not participate in the stock manipulation scheme. He politely made excuses not to participate, but he was in a quandary of what he should, at that point, do.

[724] Barthe now knew that KHI insiders were manipulating the public stock price.

[725] He could either refuse to advance the remaining two instalments of $1,625,000.00 that he was legally obligated to pay under the Subscription Agreement for the private placement and risk litigation, both for the payment of that sum and possibly for any consequences to KHI flowing from a refusal to pay the remaining subscription instalments, or, alternatively, lose the $3,325,000.00 that he and Ristow had already invested in KHI by paying his remaining obligation and hope that KHI survived. Clarke (and NBFL) was not in a fiduciary relationship with Barthe.

[726] While there is no evidence that Barthe should have known how long the manipulation had gone on, or even, at that point, Clarke's role in it, Barthe advanced to KHI the last $1,625,000 with knowledge of the stock manipulation scheme by KHI insiders. For the purposes of the last $1,625,000.00 payment, Barthe acquiesced to what he knew. He ratified payment with knowledge of a stock manipulation scheme affecting the public share price of KHI shares.

[727] He did not ratify Clarke's fraud in respect of the 259,000 shares he had purchased in August 2000. It is not reasonable to expect that in the circumstances as described by Potter after January 19, 2001, that he could have sold those shares on the market and recovered any of the $1,700,000.00 purchase price.

[728] Wadden knew, or should have known, of the stock manipulation efforts of Potter and Clarke after he received Clarke's June 8, 2000, letter outlining the deposit of his share certificate for 220,000 KHI shares into Clarke's 540 account.

[729] By August 24, 2000, he had become a member of the stock manipulation scheme and, as of September 1, was KHI's "Investor Relations" coordinator. There is no evidence that Wadden was refused by NBFL (or BMO) the opportunity to sell any KHI shares after August 24, 2000. The evidence is that Wadden not only kept the shares he had, but purchased many more.

[730] Wadden's claim against NBFL appears to be primarily that:

a) he never agreed to lend 220,000 KHI shares to Clarke's 540 account and when he tried to recover those shares, he was given back 120,000 KHI shares, but not his 120,000 KHI shares, and was unable to obtain the remaining 100,000 KHI shares until September 25, 2000, after he had made peace with Potter on August 24; and

b) NBFL refused illegally to permit him to sell KHI shares between early July and August 24, 2000.

[731] After August 24, 2000, Wadden was part of the stock manipulation scheme. It is not alleged that he was prevented by NBFL from selling KHI's share after August 24. Therefore, ratification is not a live and real issue in the disputes between Wadden and NBFL.

[732] I agree with NBFL's post-trial submission (paras 105 to 122) to the effect that there was only one instance when NBFL refused to follow Wadden's instruction to sell KHI shares. On August 11, 2000, Wadden phoned Clarke to sell 3,000 KHI shares at $6.50. Clarke called Colpitts and, in the advice of Colpitts, refused Wadden's instructions. The Court does not accept Wadden's evidence that in mid-July, and in particular, on July 19, that he instructed NBFL to sell his KHI shares. For that, the Court prefers the evidence of MacLellan and the analysis of NBFL in their brief. The issue of ratification is not relevant to the Wadden claim.

G. NBFL's Claims against Barthe and Wadden

Against Barthe

[733] NBFL third-partied Barthe for any liability found against it.

[734] The actual basis of the claim is NBFL's allegation that Barthe was treated as a director at the time he was advised that the share price was being supported. Barthe took no steps to caused the manipulation to be disclosed.

[735] It cites *United Services Funds v Lazzell*, 1998 CarswellBC 245 (BCSC) at paras 307 to 310. In that case, two directors became liable in a stock manipulation scheme, where they became aware of it and did not disclose it. The relevant paragraphs in the decision are 307, 308 and 310, they read as follows:

> 307 But not only was silence concerning these statutory breaches an act of assistance but so also was silence when the price of the shares of the companies of which they were directors shot up not for a rational reason but from trading which was patently a breach of s. 340(b) and (c) of the *Criminal Code*. Although there was no evidence form any of the officers of the fund as to what they would have done had they been apprised, in December 1984, of these goings on of illegal trading and breach of the *Securities Act*, I am satisfied from the action which the fund took in May 1985 that, if so apprised, it would have taken then the same action that it took in May 1985.
>
> 308 In my opinion, they had as directors a duty to the fund as a principle shareholder to apprise it of the relevant facts as to control and illegal trading whether or not they had, as directors, a duty to inform the fund of the scheme of bribery itself.
>
> . . .
>
> 310 Thus, it follows that in my opinion they are liable to the plaintiffs, subject to which I have to say about the application of the moneys recovered so far, for losses suffered on the purchase of shares of the companies in which each of them was a director made on or after the respective dates which I have determined were the dates of their knowledge.

[736] NBFL's argument is novel.

[737] Barthe was never a director of KHI and was never offered the position of director. His friend Ristow was promised a directorship in October 2000, when he and Barthe agreed to invest $3,250,000.00 in the private placement, but even then KHI deferred appointing Ristow a director until eight months later, on June 27, 2001. Ristow never attended a directors or shareholders meeting.

[738] At the original meeting at the airport in October 2000 that lead to the Subscription Agreement, KHI offered Barthe the opportunity to attend in Ristow's place any directors meetings that he may miss. Barthe never attended any directors or shareholders meeting.

[739] Ristow, and likely therefore Barthe, did receive some information from Potter/KHI beginning in January 2001 about the affairs of KHI. Some of that information was not generally available. In that sense, it was confidential. From October 22, 2000, Barthe and Ristow had asked Potter and KHI for a copy of its five-year plan. They had been promised it but were repeatedly put off and never did receive it.

[740] NBFL did not advance, and the Court is not aware of any principle of law or relevant legislation or case law, that would support the proposition that a shareholder in a company, who has been provided with some of the memoranda to the directors, has an obligation to a third party like NBFL to blow the whistle when he or she or it becomes aware of a stock manipulation scheme in a company in which he is a shareholder.

[741] Even if the principle in *Lazzell* applied to a shareholder like Barthe, this liability would only relate to losses suffered on the purchase of shares in the company made on or after the date of their knowledge (para 310).

[742] Three facts are relevant to any possible liability of Barthe, if *Lazzell* might impose liability on him to NBFL.

[743] First, there is no evidence of purchases made by Dunham or the Weirs after Barthe became aware that a stock manipulation scheme existed.

[744] Second, there was no evidence before the Court as to depth of Barthe's knowledge of what the stock manipulation scheme consisted of, other than the contents of Potter's fax of January 19, 2001. There is no evidence if he ever became aware of the 540 account or the length of period of time during which the manipulation had gone on. I would be surprised if he was aware that it had been going on long before his first purchase of shares on the market using NBFL and Clarke as his broker.

[745] Thirdly, NBFL had earlier access to more information and therefore more reason to be suspicious of the activities of the stock manipulators, especially Clarke, than Barthe. Roby, Senior Vice President Compliance at NBFL, had directed Clarke (and Hicks) to reduce NBFL's position (those of their clients and of Clarke personally) in KHI shares and to refrain from buying more KHI shares in both July and September 2000. The account and trading records available to NBFL, and upon which the decision by Roby to direct a reduction in exposure to KHI in 2000, should have painted a clearer picture to NBFL than what Barthe saw after January 19, 2001.

[746] Barthe should not be liable to NBFL for a stock manipulation scheme that NBFL should, but for its failure to supervise the 540 account and Clarke generally, have known about since shortly after March 2000 and especially after the meeting held between Hicks, Colpitts and Clarke in Hicks' office on August 3, 2000.

Against Wadden

[747] NBFL claims against Wadden as a manipulator, as the only remaining defendant in the Main Action, and as third party in the Debt Action and the Barthe action.

[748] Wadden joined as well as knowingly and intentionally participated in the stock manipulation scheme after August 24, 2000.

[749] Clarke knowingly and intentionally participated in the stock manipulation scheme, from not later than the first of March, 2000.

[750] Dunham's claim against NBFL is based upon Clarke's breach of his fiduciary duty and failure to diversify his account. While Clarke was a participant in the scheme from March 2000, he is separately liable to Dunham by reason of his failure to full his fiduciary obligation and to diversify

Dunham's account. Said differently, Wadden's participation in the scheme after August 24, 2000, was not the cause of Dunham's loss.

[751] In addition, NBFL's liability to Dunham is, in part, based on the manner it treated Dunham during this litigation.

[752] The Weirs/Blackwood claims are based on Clarke's failure to sell their KHI shares when instructed on January 19, 2001 (if the price fell below $5.00). Instead, he actively dissuading them from selling without disclosing his conflict of interest and the stock manipulation scheme.

[753] The reason Clarke did not sell the KHI shares held by the Weirs and Blackwood was because of his participation in the stock manipulation scheme. Clarke and his cohorts were running out of money to support the public market price of KHI; additionally, they were at the limit of their margin debt and in danger of facing margin calls if the KHI price dipped.

[754] Wadden was an active participant in the scheme at this time. Wadden is liable jointly and severally with NBFL for the loss to the Weirs and Blackwood in the value of their KHI shares.

[755] NBFL's liability to the Weirs and Blackwood is based in part on the manner in which NBFL treated them in this litigation. Wadden is not liable to NBFL for that aspect of NBFL's liability to the Weirs and Blackwood.

[756] Barthe's claim against NBFL is based solely on Clarke's participation in the stock manipulation scheme and the fraud perpetrated Barthe by reason of it.

[757] NBFL's liability is limited to the original August 2000 purchase of 259,000 KHI shares by Clarke for Barthe on the market, mostly from KHI insiders as directed by Potter. His liability does not extend to the last two instalment payments on the Subscription Agreement, made by Barthe, after January 2001, when he became aware of a stock manipulation scheme.

[758] The original deal between Barthe on the one hand and Potter / Sullivan / KHI on the other was made on August 3, 2000 (signed all parties by August 14). On August 23, Clarke communicated with Barthe with regards to setting up an account at NBFL and act as his agent to purchase the shares. Barthe's account at NBFL was open and in receipt of Barthe's money by Monday, August 28, 2000. Clarke immediately commenced purchasing shares. On August 29, he did the trade from himself to Colpitts for 43,300 KHI shares and of Colpitts to Barthe for 73,300 shares. At the same time, he arranged for the sale by Wadden and Courtney of 50,000 KHI shares each.

[759] Wadden was aware, at the time that the purchases were being made by Clarke for Barthe, of the stock manipulation scheme and he participated in the sale and benefited by it. He is liable to NBFL jointly and severally for the liability of NBFL to Barthe respecting the purchase of the 259,000 KHI shares.

H. Waddens' Claims against BMO Nesbitt Burns

[760] Calvin Wadden, Andrea Wadden, and Wadden's numbered company 3019620 Nova Scotia Limited, claim against BMO for breach of contract and negligence. Both before and during trial, counsel for the Waddens and BMO expressly represented to the Court that, despite the plaintiffs' pleadings, they were not advancing the pleading that BMO participated in the stock manipulation scheme. BMO Nesbitt Burns was not required to evidence with respect to any other claim except breach of contract and negligence.

[761] In post-trial submissions, counsel for the Waddens particularized BMO's conduct underlying their claim as:

a) failure of BMO Nesbitt Burns to advise the Waddens in advance of transferring their accounts of the restrictions that would be placed on their accounts if they were moved to BMO.

b) improper "freezing" of their account from July 10, 2000, to August 24, 2000.

[762] The only evidence called by BMO was Robert Lowe ("Lowe"), a chartered accountant and business valuator. He gave opinion evidence with respect to trading in KHI shares. Lowe's evidence was to assist the Court in calculating losses claimed to be suffered by the Waddens from the alleged freezing of their accounts between July 10 and August 24, 2000. BMO called no witnesses respecting liability itself.

[763] The Waddens submit that the failure of BMO to call evidence should lead the Court to exercise the discretion to draw an adverse inference against BMO with regards to any of the evidence given by the Waddens and not contradicted by evidence of witnesses under the control of BMO. Counsel cites the text by **Allan W. Bryant, Sidney Lederman** and **Michelle Fuerst**, *The Law of Evidence in Canada*, 3rd Ed., *CR Faulkenham Backhoe Services v Nova Scotia*, 2008 NSCA 38 and *Northern Wood Preservers v Hull Corporation Shipping (1969) Limited*, [1973], 42 DLR (3d) 679.

[764] Counsel argues that the issue of credibility should be resolved on the basis of the only evidence given orally at trial: Wadden, Ms. Wadden, Banks and MacLellan.

[765] Counsel submits that BMO failed to call Richards, Shirley Locke, Michael Meredith or Carol Cushing, and no other evidence, expert or otherwise, that would show it was legally entitled to freeze the Wadden accounts, which, Wadden alleges, was done wrongfully at the request of Colpitts.

[766] Effectively, Wadden asks the Court to find that on August 24, 2000, Wadden gave up in his efforts to fight Colpitts and Potter because of their seeming ability to have his accounts frozen wherever they were held. After that date, Wadden began cooperating with Colpitts and Potter, making no further efforts to sell large amounts of shares, because he knew that the moment he stepped out of line, conditions, like those imposed by BMO, would be reimposed. Based on that scenario, BMO was the key player in putting the "screws" to the Waddens who, under duress, agreed to terms with Potter and Colpitts and did not thereafter attempt to sell their shares. Their direct losses from foregone share sales after July 10, 2000, are claimed in the amount of $2,261,939.00.

[767] The Waddens also claim consequential losses flowing from the freezing of their accounts and their inability, between July 10 and August 24, 2000, and thereafter, to sell their shares. They point to *Athey v Leonati*, [1996] 2 SCR 458, for the proposition that they need not prove that BMO was the sole cause of the consequential damages, only a cause.

[768] The consequential damages they claim are: interest paid on margin debt, losses on trades in non-KHI shares, mortgage interest paid on real estate, certain life insurance fees, legal fees, the losses arising from the forced sale of their Halifax South End residence and Baddeck summer property, and Calvin Wadden's loss of income for three years. The total is $3,374,592.20.

[769] In its post-trial submission, BMO denies that it breached its contract or acted negligently in relation to the transfer of the Wadden accounts from FCG. With respect to the second claim (refusing to execute orders to sell KHI shares from July 10 to August 24, 2000), its defence is that it was reasonable to treat Wadden as an insider and in a special relationship with KHI during that period of time.

[770] BMO disputes many of the Waddens post-trial factual submissions, as referring to facts not in evidence.

[771] Regarding the Waddens submissions about drawing adverse inferences by its failure to call Richards, Locke, Meredith or Cushing, BMO says that at the end of Wadden's case there was no need to call evidence. These witnesses were no longer employees of BMO and not in their exclusive control. These witnesses had been discovered by the Waddens. The Waddens had been free to call them as witnesses themselves. BMO at no time undertook to call them as witnesses. Counsel cites, *St. Elizabeth Home Society v Hamilton*, 2010 ONCA 280; *Lambert v Quinn (1994),* 110 DLR (4th) 284; *Levesque v Comeau*, [1970] SCR 1010; *Canada Trustco Mortgage Co v Co-operators General Insurance (1997)*, 1 CCLI (3d) 22 (NSCA) and *Doiron v Hache*, 2005 NBCA 75.

[772] BMO says credibility (and I infer reliability) of the Wadden witnesses is an important issue. It argues that the Wadden's evidence is not credible or reliable. The Waddens' evidence was coloured by the numerous discussions they had over the years; the absence of any contemporaneous notes by Wadden, and the fact that the notes of Ms. Wadden (her diary), do not corroborate Wadden's version of events. BMO submits that Ms.Wadden was strongly motivated to support her husband, and even testified that "the ends justify the means".

[773] BMO submits that Greenwood's evidence should be viewed from the perspective that he was a close friend and employee of the Waddens and, at one point, sent a letter on their behalf that contained untrue statements. Banks' memory of events is suspect by reason of his failure to make contemporaneous notes and his admission that a little of his memory of events was faulty.

[774] Finally, BMO submits that, where there is a difference in the testimony of the Waddens and their lawyer MacLellan, the evidence of MacLellan, who had no vested interest in this litigation and who made extensive contemporaneous notes, should be found credible and reliable.

[775] For reasons, many of which are expressed earlier in this decision, I found Wadden's evidence to be not credible or reliable. BMO submits that Wadden's tendency was to look for reasons to blame others for his own actions and not take any responsibility for his own decisions; I agree.

[776] The effective cross-examination of Ms. Wadden left the Court placing no reliance or credit on her evidence.

[777] The Court found the evidence of MacLellan to be both credible and reliable.

[778] Contrary to the submissions of BMO, the Court found the evidence of Banks to be straightforward. He admitted to the limitations of his memory with regards to the particulars of dates and times of conversations between him and Locke, but he was firm in his memory of the discussions. He had no agenda. He has remained a client of BMO throughout, and of Locke - the latter until the commencement of the litigation when, at her request, he ceased being her client. His evidence was credible and reliable. I accept his evidence.

[779] To establish that BMO was negligent, the Waddens had to prove that BMO owed them a duty of care; that BMO breached the duty and standard of care; that the Waddens suffered a loss or damage; that the breach of the duty and standard of care by BMO was the proximate cause of the Waddens' loss, and that no defence or bar to recovery negated or mitigated their loss.

[780] Prior sections of this decision deal with the duty and standard of care of a stock broker to its client and to the issue of causation. Those statements of law apply to the Waddens claim against BMO.

[781] The starting obligation of a broker, as an agent, is to act scrupulously, fairly, openly and honestly with its principal.

[782] The particulars of the agent's duties and standard of care depend upon the particular relationship. The circumstances differ in each case.

[783] The two particular breaches of the standard of care alleged by the Waddens against BMO are:

a) not advising of restrictions that would be placed on their margin accounts on moving from FCG to BMO; and,

b) improperly freezing their accounts between July 10 and August 24, 2000.

[784] The standard of care is informed by the provisions of the Account Agreements (*Austral Imports Inc. v Bank of Montreal*, [2006] ABQB 428). The duty and standard of care are the same in contract and in negligence. The standard of care is also informed by any evidence tendered of the applicable statutes, regulations, stock exchange rules and industry practice.

[785] In this litigation, the Waddens have not directed the Court to any statutes, regulations, stock exchange rules or industry practices that relate to either of the two particular alleged breaches.

[786] The Account Agreement between the Waddens and BMO Nesbitt Burns provide basically as follows:

a) it permitted BMO to determine in its discretion whether or not any order was "acceptable" and whether to execute said order;

b) it gave BMO a broad and sole discretion whether to grant a margin facility to the Waddens, to reduce or cancel any margin facility once granted, and to refuse to grant any additional margin; and,

c) it gave BMO authority to cancel any outstanding orders if the Waddens failed to pay any indebtedness when due, without prior notice or demand.

[787] In *Venture USA Inc. v Yorkton*, [2005] OJ No. 1885 at paras 25 to 34, the Court determined that a more narrowly worded "refusal clause" should be interpreted in a manner that affords a broker like BMO "burdened with the gatekeeper function" latitude "to refuse suspect transactions *despite a lack of clear proof of illegality*".

[788] An investment dealer's ability to execute a client's order is subject to its overarching regulatory obligations as "gatekeeper".

[789] The "gatekeeper" function refers to the obligation of a securities registrant like BMO to "detect and forestall" activities that should contravene securities law.

[790] BMO's decision to refuse to execute trades in KHI shares for the Wadden accounts on or about July 13 was consistent with its obligations as "gatekeeper" and reasonable in the circumstances. (See: *RE: Wentzel [2005]*, ASCD No 153 (Alberta Securities Commission)).

[791] I find that Locke had a very close and special relationship with Colpitts. It is evident in her conduct and was the subject of oral evidence the Court found credible. It is evident in her aggressive peddling to Banks (whose evidence I accept completely) of various investment proposals in KHI. The evidence generated enough concern respecting her possible knowledge of the scheme by KHI insiders to inhibit sales of KHI shares while finding new investors that it merited closer scrutiny.

[792] In the end, I am not persuaded, on a balance of probabilities, that she, and therefore BMO, knew or ought to have known of the stock manipulation scheme by KHI insiders, including Colpitts, so as to infuse BMO with that knowledge.

[793] I conclude that BMO did not act dishonestly or in bad faith in its assessment of the credit worthiness of KHI shares and its assessment of Colpitts' representation to BMO that BMO could be subject to litigation if it permitted Wadden, an insider, to sell KHI shares.

[794] BMO submits that the approach by MacLellan in July and August 2000 in his dealings with Colpitts, is a useful guide in assessing the reasonableness of BMO's response to the information

conveyed by Colpitts to Meredith, BMO's legal counsel. MacLellan, despite some indicia that Wadden was not a director, proceeded on the assumption that he was. MacLellan assumed Colpitts was in a better position to determine that and whether Wadden had insider information. MacLellan was not prepared to assume that Colpitts, as an officer of the Court, would be motivated to lie.

[795] While the Halifax branch of BMO was interested in hiring Richards, at least in part, because two of his clients, Wadden and Courtney, who had substantial accounts, BMO's head office was never satisfied that KHI was worthy of the kind of margin debt that existed on these accounts when they were transferred to BMO. BMO's assessment of the credit worthiness of KHI for the purposes of margin debt was reasonable and made in good faith.

[796] Because of the resistance to head office views by the Halifax branch, BMO agreed to accept the Wadden accounts, but only on the condition that the margin debt be reduced immediately.

[797] Both Wadden and the Halifax branch believed that this would happen. At that point, Wadden and his broker Richards, believed that Potter would be purchasing or arranging for the purchase of 250,000 KHI shares by the end of June, 2000.

[798] BMO submits that on the facts of this case, it was not negligent in failing to advise the Waddens of the account conditions before the opening of their accounts; I agree. There is no evidence that anyone at BMO represented to the Waddens that their margin debts would be accepted by it unconditionally when the Waddens applied to open accounts.

[799] BMO accepted the transfer of the Wadden accounts from FCG on May 23 and paid out approximately 1.3 million dollars in margin debt owed to FCG. If Wadden wanted to transfer the accounts out of BMO before the end of June, he still could have done so. He did not because he trusted that Potter would find a purchaser for 250,000 KHI shares by June 30 and because of his close relationship with his best friend Richards.

[800] When the Waddens initiated the transfer to BMO, the Wadden's margin debt at FCG totalled approximately 1.3 million dollars. The KHI shares constituted almost the entirety of their accounts. In effect, BMO was being asked to lend 1.3 million dollars to the Wadden accounts on the security of KHI shares. At that time, there was no assurance of BMO accepting their applications to open margin accounts.

[801] I agree with BMO that Ms. Wadden testified that she appreciated that a brokerage firm did not have to offer margin to a particular client if it was not satisfied with the client's credit worthiness or the securities that it would be getting the loan. On May 23, 2000, BMO transferred funds to FCG to discharge the Waddens' margin debt and to accepted transfer of the shares.

[802] I agree with BMO's submission that the Wadden's evidence that they were not informed at any time prior to mid-July that their accounts were accepted on the condition that the margin debts be paid down by the end of June is simply not credible.

[803] It was not of concern to Wadden because he believed, at that time, that Potter was arranging a sale for 250,000 KHI shares by the end of the June and the proceeds would be used, at least in part, to pay down their margin debt. Wadden agreed that having a June 30 deadline to pay down his margin debt would not have been a big issue for him.

[804] The relationship between Richards and the Waddens was of long duration and very close. Richards was Wadden's best friend. They socialized frequently. It makes no sense that Richards would have risked his friendship and business relationship with Wadden by attempting to conceal information about the condition respecting the account transfers when Richards learned of them. There was no reason Richards would not have told Wadden of the conditions respecting the transfer of the accounts to BMO.

[805] In Wadden's trial evidence, there were many examples of advice given by Richards to Wadden that was clearly in the best interests of Wadden. For example, when Wadden was contemplating purchasing the 100,000 KHI shares in January 2000 from Snow; Richards advised against it. Further, when Richards learned that FCG would no longer advance further margin to the Waddens, he disclosed it and provided them with the opportunity to open margin accounts elsewhere. Both of these would have been adverse to Richards' own economic interests. Hiding information about BMO's transfer conditions would have been entirely out of character.

[806] I find that Wadden was advised by Richards and was aware of the transfer conditions when he knew and prior to June 30.

[807] The Wadden's second claim against BMO is its refusal to accept orders to sell KHI shares between July 10 and August 24, 2000.

[808] On July 10, 2000, Wadden had an angry telephone call with Potter, in which he expressed concern about, among other things, the fact that Potter had not arranged a buyer for his shares as promised, and had made a $400,000.00 loan to Courtney that had not been disclosed to him. Contrary to his previous undertakings not to sell shares of KHI, Wadden communicated his clear intention to begin selling KHI shares into the market.

[809] Immediately after that phone call, and the first time since opening accounts at BMO, Wadden instructed Richards to start selling shares of KHI from his margin account.

[810] BMO makes the point that as of July 10, 2000, there had been no public disclosure of the fact that KHI had made a $400,000.00 loan to Courtney, an insider, an action that Wadden considered to be have been illegal and a misuse of corporate funds. At the same time, Wadden was aware of the existence of the 540 account and, after the June 8 letter, knew that 220,000 of his shares had been used in connection with that account. He was in a dispute with NBFL about what he believed to be an improper use of his shares and his inability to get them back. There had been no public disclosure by KHI of this fact.

[811] Pursuant to Wadden's instructions, Richards succeeded in selling 6,155 KHI shares on July 10 (settled on July 13).

[812] The next day, Wadden instructed Richards to sell KHI shares held by his father, due to Wadden's concerns about the fact that KHI was making inappropriate loans to insiders, a fact not publicly known. It was this concern that Wadden acknowledged was one of the factors that caused him to place an order to sell his own shares.

[813] On July 12, Wadden instructed Richards to sell an additional 5,000 KHI shares from his margin account.

[814] Wadden acknowledges that it was not a secret that he had accounts at BMO. He acknowledged that Colpitts subscribed to a service that allowed him to view trading in shares of KHI on the TSX in real time, and that would have permitted Colpitts to see which brokerage firms were selling shares of KHI. He acknowledged that the trades being executed through BMO would have been visible to Colpitts. He acknowledged that it would not have taken a rocket scientist to figure out that the shares were being sold through BMO beginning on July 10, and that the shares were probably being sold by him.

[815] At about this time, Wadden informed Colpitts that he was "dumping garbage" and Colpitts told Wadden that he was in breach of his duties as a director.

[816] On or about July 12 or 13, Richards advised Wadden that he could not execute the last order and that Wadden's accounts had been taken out of his control. He disclosed that there had been a threat of legal action by KHI and suggested that Wadden get legal advice. Shortly after, Richards arranged a three-way phone call between Wadden, himself and Meredith, BMO's legal counsel.

[817] Wadden's evidence was that he interpreted what Meredith told him as being to the effect that BMO was taking direction from KHI's legal counsel. I prefer to accept, as reliable, not that Meredith was taking instructions from KHI's legal counsel, but the answer Meredith gave to MacLellan in his phone call and correspondence with Meredith on August 3. MacLellan says that Meredith told him that Colpitts had advised him (Meredith) that Wadden was in breach of his duties as a director and that BMO faced the prospect of legal action if he continued to trade in KHI shares.

[818] I accept BMO's submission that MacLellan's characterization of Meredith's statement is likely a more accurate reflection than Wadden's understanding that BMO was taking directions from Colpitts.

[819] MacLellan testified that, in his discussions with Colpitts, Colpitts took the position that Wadden remained a director and was bound by a fiduciary duty to KHI. He had threatened action against Wadden in connection with that breach. Greenwood testified that he was aware of the threat of legal action by KHI against Wadden and that he took that threat of litigation very seriously. MacLellan said that one of Wadden's objectives was to avoid being sued.

[820] I accept BMO's submission that, in the circumstances, it was reasonable for BMO to take the same view of Colpitts' statement of KHI intentions and to decide not to accept orders by Wadden to sell KHI shares from any account over which he exercised control. The information available to

BMO, as of July 12, raised *bona fide* issues about the acceptability and legality of Wadden's trades and whether he may be in breach of his duties as a director of KHI.

[821] It is significant that, based on MacLellan's interviews with Wadden and his research, MacLellan at no time took steps to caution BMO that Wadden was not a director or insider trading on insider information. It is not disputed that Wadden was a director of KHI from 1999 up until at least June 2000. Wadden says he resigned in June 2000; Colpitts says the resignation was not effective as it had not been accepted by KHI.

[822] It is clear that, at this time, Wadden was in possession of insider information not generally available to the public. He owned more than 10% of the issued shares of KHI.

[823] I find that Wadden was an insider and a "person in a special relationship" with KHI, as defined in the *Ontario Securities Act* and the *Nova Scotia Securities Act*. That status imposed upon him statutory obligations to file public reports disclosing purchases and sales of KHI shares, not to sell KHI shares while in possession of material undisclosed information, and not to tip others to do so.

[824] Even if Wadden ceased being a director upon the tender of his resignation in or about the first of July, he still was prevented from trading for so long as he remained in possession of material, undisclosed information about KHI, obtained while he was an officer, director or 10% shareholder.

[825] It was prudent and reasonable for BMO to treat the threat of litigation from KHI seriously and to have considered that there was potential for a breach of securities law and/or a fiduciary duty by Wadden.

[826] Despite the Court's suspicions about the relationship between Locke and Colpitts, the Court finds it more likely than not that the impetus for BMO's actions on July 13 in refusing to permit Wadden to continue to execute trades in the shares of KHI until the issues discussed above had been sorted out was reasonable. It was consistent with BMO's gatekeeper function, which included an obligation to decline to execute trades in circumstances suggesting potential illegality. It was not negligent.

[827] BMO submits that there is no evidence that it refused to accept orders to sell from Wadden after July 13; therefore, the Court should not infer that the Wadden accounts were "frozen". I disagree.

[828] The nature of the communications between Meredith and MacLellan reinforces the inference that BMO would not permit trading while the unresolved allegations of illegalities were outstanding.

[829] The fact that Wadden was focussed after July 17 upon negotiating a term sheet for the sale of a block of KHI shares at a guaranteed price, and therefore not attempting to sell KHI shares on the market, does not detract from the inference that if he had attempted to sell shares before BMO began selling shares about August 16, on its own account, that he would have been prevented from doing so.

[830] The Wadden's claims against BMO are in contract and negligence.

[831] With respect to the claim in contract, the allegation that BMO failed to advise the Waddens of the conditions of their accounts before the transfer is not alleged to constitute and could not constitute a breach of contract. They preceded the execution of the account opening documents and KYC form, which constitute the contract between the Waddens and BMO.

[832] BMO submits that it had the right, on or about July 13, to refuse to execute Wadden's orders to sell shares under the account agreements.

[833] The account agreement specifically provided: "Upon acceptance of the Application, I agree to the terms and conditions set out on the reverse side of this application form which, together with the completed application form, constitutes this Agreement . . ." The terms and conditions gave BMO the express right to determine the acceptability of any order and to refuse to execute any order.

[834] Condition Number 3, titled "Operation of the Account", para (a) reads: "Nesbitt Burns has the right to determine in its discretion whether or not any order for Transactions in Securities for the Account is acceptable or whether to execute said order."

[835] Like the refusal clause in issue in *Venture Capital* (see paras 25 to 34), para 3 gives BMO the right to refuse to execute trades, "beyond those provided for provided by the common law". Paragraph 35, in part, states:

> . . . is to be interpreted in the context of the complex world of securities regulation. Large volume transactions involving large sums of money proceed at a rapid pace, and the risks are high . . . the agreement between the broker and the client should be interpreted in a manner that affords the broker burdened with the gatekeeper function latitude to refuse suspect transactions despite a lack of clear proof of illegality.

[836] The term "acceptable" in para 3 of the BMO Agreement is broader than the term found in *Venture Capital*. The ordinary meeting of "acceptable" includes "suitable" and "satisfactory".

[837] Of course, BMO cannot justify actions taken in bad faith but, in this case, I find that BMO had sufficient grounds to determine that Wadden's orders to sell KHI shares were not acceptable or suitable. They raised the possibility that the Waddens would be contravening the prohibitions against insider trader and tipping. Additionally, they also raised the possibility that Wadden may be acting in breach of a fiduciary duty to KHI.

[838] BMO also relies upon para 5 of the account agreement, which dealt with margin. Paragraph 5 reads, in part:

> If the Client applies for a margin facility, Nesbitt Burns may, in it sole discretion, grant the facility to the Client provided that Nesbitt Burns may, at any time and from time to time
>
> a) reduce or cancel any margin facility available to the Client or refuse to grant any additional margin facility to the Client; or

b) require the Client to provide margin in additional to the margin requirements of the applicable Regulatory Authorities.

[839] BMO, when it decided to accept the account, had reservations with respect to the suitability of KHI as security for the margin debt that it agreed to take over from FCG. It had provided the Waddens with notice requiring the margin debt to be cleared by June 30, 2000. I have already found that the Waddens were aware of this before June 30. It was not a breach of contract for BMO to refuse to execute trades thereafter until the margin debt was cleared.

[840] Paragraph 8 of the Agreement also authorized BMO to take steps to protect itself. This included cancelling outstanding orders without prior notice.

[841] In summary, any refusal to execute Wadden orders to sell KHI shares on or about July 13, 2000, was made in accordance with the rights of BMO under the Account Agreements entered into with the Waddens, and in good faith.

[842] BMO submits, in the alternative, that the Waddens were at fault for the loss of their investment in KHI, either entirely or by contributory negligence. In its post-trial brief, it itemized ten particulars of the Waddens' failure to act reasonably to protect their own interests. These include:

a) Wadden's failure to undertake proper due diligence prior to selling his interest in Micronet to KHI for shares and not for cash.

b) Ms. Wadden's failure to undertake proper due diligence before investing $250,000.00 in a private placement in the fall of 1999 and borrowing money for that purpose.

c) The Waddens' purchase of another 100,000 KHI shares from Snow in January 2000 for $600,000.00, purchased entirely on margin, even though Richards advised them against the transaction.

d) The Waddens signing their account opening documents without reading them.

e) Wadden quitting his job and arranging no alternative employment, in reliance on the fact that Potter would arrange, by the end of June 2000, for the same of 250,000 KHI shares held by the Waddens (which Ms.Wadden acknowledged in hindsight was "not a wise thing to do".)

f) In addition to borrowing a million dollars to invest in KHI, between March and June 2000, borrowing another million dollars on margin to live on and to spend on other projects, which appear to include over a million dollars on renovations to a home and summer property.

[843] I agree that the Waddens made several significant decisions that show they did not act reasonably in their own best interests with respect to their investments in KHI, separate and apart from the sale of the business for shares and no cash. However, because I find that BMO was not in

breach of its duty and standard of care in contract or in negligence, it is unnecessary to apportion liability between the Waddens and BMO.

[844] BMO also asserts that the Waddens ratified any wrongdoing by it.

[845] Ratification is limited to that which the Waddens knew or ought to have known at the time of ratification. As previously noted, the Waddens and BMO, both before trial and at the commencement trial, put on record their agreement that none of the Wadden claims against BMO rely upon fraud arising from the illegal stock manipulation scheme or an allegation that BMO was a part of it.

[846] Wadden testified that, as of August 2000, he believed the conduct of BMO was wrongful. If the Court is wrong in its finding of no breach of contract or negligence, I agree with BMO's submission that the Waddens accepted and acquiesced after August 24, 2000, that which they now complain to have been the consequence of the alleged misconduct by BMO.

[847] This Court has previously outlined its position with respect to causation and, in particular, proximate cause.

[848] If I am wrong in finding that BMO did not breach either of the two alleged breaches of contract and negligence, I am not satisfied that any of the claimed losses were caused by BMO.

[849] The Court has already found that KHI was a thinly-traded stock. While the Court is satisfied that small quantities of stock may have been salable on the public market, the large quantity held by the Waddens - the second largest share holdings in KHI, were clearly not salable, other than the blockbuster sales arranged by Potter and other KHI insiders. Nothing BMO did was the proximate cause of the failure of Waddens to sell any significant amount of their shares.

[850] More important, after Wadden's epiphany of August 24, 2000, he became an active buyer of shares on the market for the purpose of maintaining the price while he, Potter and other insiders sought new investors. They did this as a group working together. Wadden had an active part of that group.

[851] BMO advanced opinion evidence to quantify the trading in KHI shares, and effectively estimate how many potential shares could have been sold between July 13 and August 31 if Wadden had been permitted to sell 5,000 KHI shares per day.

[852] I am somewhat sceptical of the calculations and conclusions because the report and evidence did not include the fact that most of the volume of shares consisted of three sales arranged by KHI insiders: to Banks, Barthe and Fountain. Without these purchases, arranged by the insiders, there was a very thin market for KHI shares.

[853] In their post-trial brief, the Waddens submit that BMO is responsible for the fact that none of Wadden's shares were purchased by Banks on August 3, 2000. There is no evidence that Banks was prepared to buy shares of KHI at a higher price than what he negotiated following his own

inquiries. Wadden was, throughout, not prepared to sell his shares on the terms that Banks was prepared to buy.

[854] While not directly determinative, I observe that Wadden was always trying to get more for his shares than the market would bear. He declined, at one point, Potter's offer to assign to Wadden the Barthe agreement of July 2000. He repeatedly failed to see where KHI's share price was heading.

[855] BMO claimed that there were no restrictions on Wadden's trading after July 13, and I concluded that there would have been (if Wadden had asked to sell after July 13), so long as Meredith was of the view that BMO was subject to possible litigation by KHI. However, there was nothing to prevent the Waddens from attempting to sell shares after August 31, which they claim they wanted to do on and after July 17. I do not accept Wadden's evidence that he did not attempt to sell after August 31 because he believed that if he did he had been closed down again. If there was a market for KHI shares, the Waddens could have mitigated any freezing of the BMO accounts between July 10 and August 24. They did not do so. Their failure to attempt to sell after August was not caused by anything BMO did.

[856] In an exhibit presented at trial, the Waddens claimed total loss of $6,591,922.41. Of this, $5,292,641.00 was with respect to the loss in the value of KHI shares. The remainder was consequential losses. Because of the finding that BMO did not breach its duty and standard of care in contract and negligence, it is unnecessary to deal with their claim for consequential losses.

I. Assessment of Damages against NBFL

I.1 Dunham's Loss and Damages

[857] The analysis of NBFL's liability for damages to Dunham starts with the following factual findings:

a) Clarke, as the agent for Dunham, breached not only his duty and standard of care in contract but a fiduciary duty. He took advantage of Dunham's vulnerability because of his conflicts of interest, including his own investments in KHI and his participation in the stock manipulation scheme. He did not attempt to diversify Dunham's account. He acted fraudulently in ignoring Dunham's instructions to sell and requests for professional advice;

b) NBFL's breached its duty and standard of care owed to Dunham in contract and in negligence by failing to proper supervise Clarke and his 540 account. It failed to uncover, as it should have uncovered, Clarke's conflicts of interest and fraud in his dealings in KHI shares;

c) As between NBFL and Dunham, NBFL is and should be liable for the loss and damage to Dunham from Clarke's wrongdoing, not only by reason of its negligence and breach of contract, but by reason of its vicarious liability for Clarke's wrongdoing;

d) By reason of its own investigation in 2003, NBFL believed, on the basis of "overwhelming evidence", that Clarke had participated in the stock manipulation scheme that had lead to NBFL's losses (mostly in respect of margin debt). It has always been in the best position to know what Clarke did, and that it was wrongful in every sense.

Lost Value of KHI Shares

[858] It is not possible to determine exactly what would have happened if Clarke had not acted fraudulently and breached his fiduciary duty to Dunham - sold his KHI shares and diversified Dunham's account between June and August 2000. That said, it is not speculative to calculate the loss in the KHI share price, but for Clarke's breach wrongdoings. There was a market price at which KHI shares were traded on the TSX.

[859] KHI was a thinly-traded stock. Except for the arranged block purchases by wealthy investors (Keating, Banks, Barthe and Fountain) and by Clarke, there was no obvious large purchasers. Nevertheless, the number of the shares sought to be sold by Dunham was not substantial.

[860] I conclude that it was likely that, but for Clarke's failure to give prudent investment advice and his dishonesty in diverting Dunham from selling KHI shares and, instead, creating margin debt, Dunham would have sold almost all (and possibly all) of his KHI shares before the end of September 2000. I therefore calculate the loss of KHI share value as being the market value at which KHI shares sold between June 30 and September 30, 2000.

[861] For the most part, KHI shares sold between $6.65 and $6.80. The highest price during that period was $6.95 and the lowest price (on two different days) was $6.40. I estimate that the median price at which KHI shares sold during the period was $6.75.

[862] Excluding the first 30,000 shares, which were sold by Clarke to pay off Dunham's debt to KHI and withdrawn for personal use, I calculate the loss to Dunham from the failure to sell his KHI shares as 120,000 KHI shares at $6.75 or $810,000.00. From this, I deduct the net proceeds from the sale of the 13,000 KHI shares on September 13, November 7, and December 19, 2000.

[863] The law is clear that for a breach of fiduciary duty, one of the remedies is to disgorge the wrongdoer from profits.

[864] Clarke acted fraudulently and in breach of his fiduciary duty. I disallow deduction of any brokerage fees that would normally be incurred on the sale of these shares. For the same reason, in giving credit for the sale of 13,000.00 KHI shares, I give credit for only the net amount received.

[865] Second, NBFL argues that from this should be deducted the margin debt of $353,021.96.

[866] Dunham argues that, by reason of Clarke's fraud and breach of fiduciary duty, for which NBFL was liable, Dunham should not be liable for any of the margin debt.

[867] It appears from the submissions of the parties, that of the margin debt, $34,418.00 was interest charged monthly on the margin debt by NBFL. The remainder of the margin debt appears, for the most part, to be in the form of withdrawals by Dunham for his personal use. The personal use appears primarily to relate to the construction of a residence and the purchase of a vehicle, but may have included monies for investments in other projects pursued by Dunham after he left KHI in April 2000.

[868] The principle that wrongdoers, especially those with a fiduciary duty or who acted fraudulently should be disgorged of any profit, means that it would be inequitable for Dunham to be liable for the portion of the margin debt related to interest charged by NBFL on the debt.

[869] At the same time, the Court fails to see the rationale for deducting from the value of the KHI shares that should have been sold by Clarke the principal amount of margin debt that was withdrawn by Dunham for personal purpose. For that reason, the Court deducts from the $810,000.00 loss in the market value of his KHI shares not the just the net amount recovered from the sale of 13,000 KHI shares, but the principal portion of the margin debt, which I believe is $318,603.96.

[870] Dunham is entitled to prejudgment interest from September 1, 2000. Absent better evidence, the default prejudgment interest rate, set out in the *Civil Procedure Rules* is 5%. NBFL, in its post-trial submission, provides detailed calculations supporting a prejudgment interest of 2.614%. This rate is calculated on the basis of the average of the one-year Treasury Bill and two-year Government of Canada Bond Rate for the relevant period. I adopt that rate, compounded and calculated monthly, not in advance.

Consequential Losses

[871] The claimed consequential losses over 11 years include:

a) Lost income from June 30, 2000 to December 31, 2012, at the rate of the $40,000 per year ($440,000.00).

b) Loss of the value of investments ($80,000.00).

c) Loss of his investment in a business project "Fantasy Stocks", which he claims he was unable to complete because of lack of financing - $113,000.00.

d) Interest paid on credit cards - $51,576.00.

e) Professional fees paid in relation to his filing for personal bankruptcy - $2,200.00.

f) Interest paid on the mortgages he took out on the home that he mortgaged to live on and pursue his projects on - $126,000.00.

[872] The law permits claims for consequential losses. The starting point, however, is causation and the application of the "but for" analysis to the connection between the wrongdoing of the defendant and the loss to the plaintiff.

[873] Dunham did not cease his employment with KHI and was not prevented from pursuing other employment, by reason of the failure of Clarke to diversify his account.

[874] As a result of his withdrawals in his margin account, Dunham's home appears to have been paid in full, until he took a collateral mortgage on July 31, 2001 in the amount of $159,000.00 and remortgaged the property on August 30, 2002 for $337,533.75 (of which some of the proceeds were used to pay off the earlier mortgage). I agree with NBFL that the timing of the mortgage advances negates Dunham's claim that the failure of Dunham's various business projects, including "Fantasy Stocks" was casually connected to the failure of Clarke / NBFL to liquidate his KHI shares.

[875] Dunham has failed to establish that the consequential losses were caused by Clarke's wrongdoing. A determination of what other reason may have led to the failure of those business ventures, and the money borrowed through the two mortgages is not necessary.

Punitive Damages

[876] Dunham claims a substantial award of punitive damages. He cites *Whiten*. He notes, in particular, that NBFL had no defence to Dunham's claim for the loss of the value of his KHI shares, and that NBFL itself had taken the position in 2003 and 2005 that it had overwhelming evidence to believe that Clarke and others had conspired to manipulate the stock price of KHI shares. This view was acted upon with commencement of the Main Action in 2003, and defended in this court in 2005.

[877] In 2005, Justice Scanlan urged NBFL to settle with those who were not implicated in the stock manipulation scheme. Clearly Dunham was not implicated. NBFL never alleged that he was. NBFL continued to fight Dunham's claim with what his counsel described as a "litany of tactics, stratagems and rouses" over twelve years.

[878] His counsel describes the treatment of Dunham (and the Weirs) as similar to that imposed on the Blackburns in *Blackburn* (upheld by the Ontario Court of Appeal, 2005 CarswellOnt 671). In that case, punitive damages were not awarded but costs were awarded at three times the normal rate. Counsel argues that the ten factors considered at para 24 in the Court of Appeal decision in *Blackburn* support a claim for punitive damages in this matrix. In *Blackburn*, the Court denied punitive damages because the stockbrokers had been otherwise punished. In this case, no one had been otherwise punished.

[879] Dunham's counsel directs the Court to para 79 in the *Whiten* decision. It distinguishes the failure to honour the contractual duty of good faith, from liability for the actual breach of the contract, in setting up the basis for an award of punitive damages.

[880] NBFL argues that Dunham has not established an independent, actionable wrong on the part of Clarke or NBFL that would put this case in the category of exceptional cases for which punitive damages are awarded. Citing *Honda v Keays*, 2008 SCC 39, NBFL argues that punitive damages are restricted to "advert wrongful acts that are so malicious and outrageous that they are deserving of punishment on their own."

[881] With respect to punitive damages for breach of contract, the Nova Scotia Court of Appeal stated in *Plaza Corp. Retail Properties Ltd. v Mailboxes Etc*, 2009 NSCA 40, that "a very high threshold must be met before an award of punitive damages is merited." And, quoting from *Fidler v Sun Life Assurance Co. of Canada*, [2006] 2 SCR 3, "[b]y their nature, contract breaches will sometimes give rise to censure. But to attract punitive damages, the impugned conduct must depart markedly from ordinary standards of decency . . ."

[882] NBFL notes that in *Blackburn*, no punitive damages were awarded in a case in which the broker had engaged in unauthorized trading on a regular basis and that his employer had been aware of his breaches.

Analysis

[883] Punitive damages is relevant to both the Dunham and Weir claims. This part of the decision deals with general principles, and the application of those principles to the Dunham matrix.

[884] The starting point for assessment of punitive damages in Canada is *Whiten*, as explained in *Fidler* and *Honda v Keays*.

[885] For the purposes of this litigation the first eight of the ten conclusions of Justice Binnie in *Whiten* (para 67) are helpful. I summarize them as follows:

a) The attempt to limit punitive damages by categories does not work. The control mechanism lies not in restricting the category of case but in rationally determining circumstances that warrant the addition of punishment to compensation in a civil action. The nature of the remedy is that punitive damages will largely be restricted to intentional torts or breach of fiduciary duty, but may be available in exceptional cases in contract and in negligent cases.

b) The general objectives of punitive damages are punishment (in the sense of retribution), deterrence of the wrongdoer and others, as well as denunciation.

c) The primary vehicle of punishment is criminal law and regulatory offences; therefore, punitive damages should be resorted to only in exceptional cases and with restraint. The fact and adequacy of any prior penalty imposed in any criminal or other proceedings is a factor to be considered.

d) The incantation of time honours pejoratives such as high-handed, oppressive, vindictively, provides insufficient guidance or discipline to the judge and a more principled, less exhortatory approach is desirable. The Court should relate the facts of the particular case to the underlying purposes of punitive damages and ask how, in particular, an award would further one or other of the objectives of the law and what is the lowest award that would serve the purpose.

e) It is rational to use punitive damages to relieve a wrongdoer of its profit where compensatory damages would amount to nothing more than a license fee.

f) The proper focus is not on the plaintiff's loss, but on the defendants misconduct. A mechanical or formulaic approach does not allow sufficiently for the many variables that ought to be taken into account at arriving a just award.

g) The governing rule for quantum is proportionality. The overall award should be rationally related to the objectives for which the punitive damages are awarded (retribution, deterrence and denunciation).

[886] Beginning at paragraph 111, Justice Binnie wrote that proportionality was the key to the permissible quantum of punitive damages. He identified proportionality in seven contexts: the blameworthiness of the defendant's conduct; the degree of vulnerability of the plaintiff; the harm or potential harm directed specifically at the plaintiff; the need for deterrence; the recognition of any other penalties, civil and criminal, which are or likely to be inflicted on the defendant for the same misconduct; and, the advantage wrongfully gained by the defendant from the misconduct.

[887] Clarke's failure to follow Dunham's request for advice respecting the diversification of his account, and NBFL's failure to properly supervise and uncover his conflict of interest and participation in a stock manipulation scheme is not the independent cause of action that will found a claim for punitive damages.

[888] The motive and intent of Clarke to use his position, *vis-a-vis* Dunham, a position of trust (as a fiduciary) was for the purposes of furthering the scheme of preventing or attempting to prevent the selling of KHI shares on the market, which persisted from June 2000 through to and including August 2001. The vulnerability of Dunham and very precarious position that, to the knowledge of Clarke, his conduct put Dunham in, does raise Clarke's conduct to the level of advertent wrongful acts that are so outrageous as to be deserving of punishment on their own. Clarke's misconduct was more than the simple breach of a contract. It was a very serious breach of a fiduciary duty.

[889] The unfortunate personal circumstances of Dunham that followed, which the Court has determined were not proximately caused by Clarke's failure to sell his KHI shares, was something which Dunham made Clarke aware of but did not affect Clarke's selfish priority of maintaining the value of KHI shares through attempts to prevent sales. It was in his personal best interests and those

with whom he was associated in the manipulation scheme to breach the most fundamental of his duties to Dunham.

[890] The public securities market involves enough risks without the risk that an investor's broker or investment advisor cannot be trusted to act honestly and in good faith, especially in those circumstances where the relationship is more than a simple order-taker and rises to a fiduciary-like relationship. Investment advisors are generally looked on as professionals. They have an obligation to act prudently and to protect their client's interests. Their duty is infused by this obligation. Clarke had been on the receiving end of securities industry discipline before his employment by NBFL. His dishonesty toward Dunham is inexcusable. NBFL's duty is infused by this with an obligation to have systems in place to inspect for, monitor, and enforce statutory, exchange, industry, and their own rules. They should not be forced by civil litigation proceeding to carry out their duty.

[891] The failure by NBFL to properly monitor him was more than a minor glitch or aberration. It appears in this case to have been a major failing.

[892] The aggressive, no-holds-barred, prolonged pursuit of litigation against Dunham, with respect to liability more than quantum, in light of what NBFL knew when it commenced the Main Action about Clarke's misconduct, and which it defended in motions before Justice Scanlan in 2005, is not justifiable. It was, in hindsight, outrageous.

[893] The conduct is exceptional. It merit punitive damages.

[894] The difficult analysis is determining the appropriate quantum of punitive damages. The purpose clearly has to be denunciation and deterrence - to discourage investment advisors and their employing brokers from conducting their affairs with clients in circumstances where conflicts of interest can exist, and go undetected. Deterrence to employers of advisors who may act fraudulently and in circumstances of conflicts of interest, and who fail to protect their clients, is important

[895] This litigation commenced with 54 sets of parties, the overwhelming majority of whom are no longer part of this litigation. Many of those parties were clients of NBFL and investors in KHI. Many were not alleged by NBFL in its Main Action (in which they allege a stock manipulation scheme by many insiders) to have been insiders.

[896] Rousseau swore in 2005 that NBFL had overwhelming evidence that Clarke was part of the stock manipulation scheme. It continued the litigation with Dunham, a clear vulnerable victim of Clarke's wrongdoing for several years thereafter.

[897] Assessment of a quantum for punitive damages is not a precise science. The circumstances in respect of Dunham, based on the harm to him; based on the need for deterrence and to recognize that the defendant should not benefit from the misconduct of its broker, suggests that punitive damages should at least be in the amount of $200,000.00.

I.2 Damage Claim of the Weirs / Blackwood

[898] Counsel for Weir and Blackwood claim for the loss in the value of KHI shares: for Blackwood Holdings, $42,000.00; and for Lowell Weir in his LIRA account, $26,250.00 and in his margin account, $157,500.00; plus prejudgment interest at 5%. They claim punitive damages based on the manner in which NBFL has conducted this litigation. Also, they claim costs on a solicitor - client basis.

[899] NBFL submits first that if the Court finds it liable to Weir and Blackwood, that the amount of the Promissory Note with prejudgment interest should be deducted from the award; otherwise, NBC should have judgment against the Weirs for $100,000.00 plus prejudgment interest. In addition, credit should be given against any claim of Weir for the amount of his margin debt, $60,177.00.

[900] Similarly, if the Court finds NBFL liable to Blackwood for failure to sell its 7,000 KHI shares, NBFL should have credit for its outstanding margin debt of $10,404.00.

[901] NBFL argues that it is not liable for the consequential damage caused by the liquidation of the 325,500 Enervision shares held by Blackwood on the basis that it had sole discretion respecting the margin called per the margin agreement and had no duty to Blackwood regarding how it liquidated the Enervision shares. It cites *Paciorka v TD Waterhouse [2007],* OJ No. 289 (OSC) at paras 76 and 80.

Analysis

[902] I found that Clarke / NBFL are liable to Weir and Blackwood for failing to sell their KHI shares when they dipped below $5.00 after Weir's communication to Clarke on January 19, 2001.

[903] As I noted in the analysis of Dunham's claim, KHI was a thinly-traded stock, but not so thin that, if Clarke had followed instructions, the small quantum of shares held by Weir and Blackwood would most likely have sold on the market. The Court notes that the sale of 1,000 KHI shares on March 24 brought more than $5.00.

[904] Because the failure to follow instructions was intentional and based on Clarke's conflict of interest and fraud, NBFL should not be entitled to profit from broker fees or commissions respecting the sale of the shares. The principle of disgorgement applies.

[905] The loss to Weir in his LIRA account is $25,000.00, calculated as 5,000 KHI shares at $5.00. The loss to Blackwood in its margin account is $35,000.000, calculated as 7,000 KHI shares at $5.00. The loss to Weir in his margin account is $140,625.00, calculated as 28,125 KHI shares at $5.00.

[906] Respecting the latter shares, I found that the standing instructions to sell of January 19, 2001, apply to the shares placed into Weir's margin account on February 28 (unbeknownst to him). NBFL argues that those shares were restricted from being sold until June 27, 2001. I disagreed in my analysis. Even if I was wrong, they should have been put on the market on June 27, 2001. I am satisfied that it is likely that they would have been sold if that had been done.

[907] Consistent with my analysis respecting Dunham's claim for damages, the principal portion of the margin debt owed by Weir and Blackwood to NBFL is deductible from the award for loss in the value of the KHI shares.

[908] The interest portion (all interest charged and/or paid at any time) is not deductible from the claim for the loss in value of the KHI shares on the same principle that Clarke / NBFL should not profit, or should be disgorged of any profit from Clarke's intentional wrongdoing.

[909] I agree with Weir and Blackwood that the manner in which NBFL dumped Blackwood 325,000 Enervision shares on the market on September 19, 2001, for a nominal price (about two cents per share) was unreasonable, and not done in good faith. Just because NBFL had a sole discretion under the margin account agreement to deter how to handle margin debt and had no duty to maximize the price, its conduct in this case clearly was not intended to benefit NBFL so much as to cause damage to Weir, who at that time was accusing (with the benefit of hindsight rightly) NBFL of wrongdoing.

[910] Blackwood has produced no evidence as to what the market value of the Enervision shares would have been, " but for" NBFL dumping them on the market on September 19. Weir has testified with respect to the loss of his business reputation and its consequences upon Enervision. That loss has not been quantified.

[911] The Court found that because Enervision had just entered into a major contract in Norway that Weir was not able to mitigate the damage caused by NBFL's dumping of the shares, by purchasing them himself.

[912] Absent evidence of the quantum of the loss to Blackwood respecting the manner in which NBFL dumped those shares; I decline to award damages. However, that is not the end of the matter. My interpretation of the evidence of Weir, and the communications and documents associated with the advance of the $100,000.00 by NBC in March 2003, is that the $100,000.00 advance by NBC to the Weirs related primarily to the settlement of Weir's (and Blackwood's) complaint against NBFL related to the damage to Enervision and Blackwood's investment in Enervision. Consequently, I find that NBC is not entitled to repayment of the $100,000.00 advanced towards a settlement of the Enervision aspect of the Weir / Blackwood claim against NBFL's liability to Weir and Blackwood with respect to its loss of the KHI shares, nor to a set-off against the other damages awarded to Weir and Blackwood.

[913] Weir and Blackwood claim punitive damages. I adopt my review of the law respecting punitive damages in the preceding section of this decision. The Weir / Blackwood claim has a different foundation than Dunham's claim. Dunham's claim was founded in breach of contract and the advertent abuse by Clarke of a fiduciary duty.

[914] Clarke was not a fiduciary to Weir or Blackwood. He breached his contract with each, and NBFL breached its duty in two other ways: in its failure to properly supervise Clarke and in the manner in which it dumped the Enervision shares of Blackwood.

[915] NBFL's conduct of its litigation against Weir and Blackwood has been outrageous. It promised to settle, then reneged, and waged an aggressive, no-holds-barred, defence of their claim, especially respecting liability.

[916] The punitive damage claim of Weir and Blackwood must be proportional. It must act as a deterrent to similar conduct in future. It must be more than a slap-on-the-wrist. The conduct proven at trial gives the investment industry a black eye, but more important it will create mistrust of an important institution.

[917] The quantum of this punitive judgment award is based upon the abusive and disingenuous treatment of Weir and Blackwood after the margin calls. The bullying and threats, followed by the litigation, followed by the acknowledgment of wrongdoing in March 2003 and advance of settlement, followed by nine years of contesting vigorously the Weir / Blackwood claim is abusive conduct of an exceptional nature.

[918] NBFL acknowledged in 2003 in affidavits, filed in respect of motions contesting its pleadings, that it had independently investigated the conduct of Clarke and others, such that they had overwhelming evidence of a stock manipulation scheme in which Clarke played an important part. NBFL had the best access to the records that proved Clarke's involvement in the scheme, and its effects on NBFL's clients It made an advance to Weir on an eventual settlement with him at the same time that it commenced the Main Action.

[919] It represented that it would settle when it had recovered a contribution from the others, whom, it represented to Weir, should share in the wrongful conduct against Weir. There was no justification for it to have contest Weir's claim, at least with respect to liability, for the next nine years.

[920] At trial, NBFL presented no evidence to rebut any of the oral testimony of Weir or McLaughlin-Weir. In its post-trial brief, it acknowledged that it had failed to supervise Clarke's conduct in respect of his 540 account, while maintaining that the Dunlop Clients had failed to prove that Clarke's market making was illegal.

[921] NBFL's actions speak louder than its submissions. There was no justification, on the evidence before the Court, for NBFL to contest Weir's claim after 2003, except as to quantum.

[922] The question is not whether punitive damages should be awarded, but rather the quantum. As pointed by Justice Binnie in *Whiten*, beginning at para 111, the quantum has to be in the context of the purpose of punitive damages (retribution, deterrence, denunciation).

[923] NBFL's conduct in contesting the Weir / Blackwood claim after March 2003, when it acknowledged its liability to him, was intentional. It persisted in an outrageous manner over a lengthy period of time (9 years).

[924] The vulnerability of the Plaintiffs and consequential abuse of power by the Defendant reflected a substantial power imbalance. Many other "outside" investors dropped out of the litigation

between 2001 and the commencement of trial 11 years later. NBFL has benefited from the fact that many could not stay in the arena with it.

[925] The quantum of the damage award has to be proportionate with to the need for deterrence. The Defendant is a substantial national institution. An important portion of its business involves investments by its clients in the Canadian securities market. It is a factor, even if of limited importance, that the quantum of the punitive damage claim recognize that a smaller award would have less deterrence on it than a less substantial corporation.

[926] Applying these factors to the purpose of punitive damages, I award Weir and Blackwood jointly punitive damages in the amount of $200,000.00.

I.3 Barthe

[927] Counsel for the Barthe estate submits that the calculation of damages in this claim is the easiest. Based on the Court's assessment of the evidence respecting liability, I agree.

[928] Barthe made two investments in KHI after Clarke became involved in the stock manipulation scheme. However, as the Court found, the evidence appears to show that Barthe paid the last two installments on the private placement after he became aware of the stock manipulation scheme and he knew or should have known, that Clarke was a party to that scheme.

[929] Barthe advanced to Clarke 1.7-million dollars in August 2000 to purchase shares. Clarke purchased 259,000 KHI shares.

[930] The loss to Barthe in the value of the KHI shares was 1.7 million dollars, less the amount recovered by his sale of those shares after the collapse of NBFL. The Court awards 1.7-million dollars less the amount recovered from the sale of the 259,000 KHI shares after the collapse of KHI plus interest at the prejudgment interest rate referred to earlier in this decision of 2.615% per year, compounded monthly, not in advance, from September 1, 2000 to the date of judgment.

[931] With respect to NBFL's argument regarding mitigation, unlike the circumstances of Dunham and Weir / Blackwood, the quantity of KHI shares held by Barthe was so significant, and the public market so thin, that it is not reasonable to expect that if Barthe had attempted to sell into the market after January 19, 2001 that he would have recovered anything for the shares. It is more likely that placing those shares into the market would have caused an earlier collapse in the public price of the KHI shares.

I.4. Calvin Wadden's Third Party Liability to NBFL

[932] Wadden is not liable to NBFL for any of its liability to Dunham.

[933] Wadden was an active participant in the stock manipulation scheme in January 2001, when Clarke did everything he could to prevent the Weirs / Blackwood from following through on their instructions to him to sell the KHI shares if they dropped below $5.00. He is jointly liable to Clarke

for the actual net loss to Weir and Blackwood in the value of their KHI shares. He is not liable for the punitive damages claim, which is based on NBFL's conduct of litigation, nor the $100,000.00 promissory note (the advance by NBFL respecting the manner in which NBFL conducted its margin call for the Enervision shares).

[934] I have already determined that at the time Clarke was purchasing shares for Barthe, which included shares of Wadden, Wadden was an active participant in the stock manipulation scheme. He is jointly liable to NBFL for its liability to the Barthe Estate respecting this Court's award to the Barthe Estate.

1.5 Costs

[935] Counsel disagree on whether the Court should hear further from them before awarding costs. Counsel for Dunham and Weir/Blackwood seek solicitor-client costs.

[936] While the Court recognizes that its finding respecting the conduct of NBFL towards the Weir family and Dunham, on its face, could support a substantial costs award, the Court declines to award costs without further submissions. These submissions would include, in the Dunham and Weir matters, factual information with respect to actual solicitor - client costs.

[937] In any event, costs in respect of the Barthe and Wadden claims, NBFL's third party claims, and the Wadden claim against BMO, require submissions.

[938] The Court will received submissions on how those submissions should be received, by conference call or by a motion in chambers, or otherwise.

J.