



Court File No.:

**ONTARIO  
SUPERIOR COURT OF JUSTICE**

Electronically issued : 27-Mar-2020  
Délivré par voie électronique  
Toronto

**DENIS FRAYCE and MAXWELL WALLACE**

Plaintiffs

**- and -**

**BMO INVESTORLINE INC., CIBC INVESTOR SERVICES INC.,  
CREDENTIAL QTRADE SECURITIES INC., DESJARDINS SECURITIES INC.,  
HSBC SECURITIES (CANADA) INC., NATIONAL BANK FINANCIAL INC.,  
QUESTRADE INC., RBC DIRECT INVESTING INC., SCOTIA CAPITAL INC.,  
TD WATERHOUSE CANADA INC., LAURENTIAN BANK SECURITIES INC.,  
and BBS SECURITIES INC.**

Defendants

**STATEMENT OF CLAIM**

Proceeding Under the *Class Proceedings Act, 1992*

TO THE DEFENDANTS:

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

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

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

Instead of serving and filing a statement of defence, you may serve and file a notice of intent to defend in Form 18B prescribed by the *Rules of Civil Procedure*. This will entitle you to ten more days within which to serve and file your statement of defence.

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

IF YOU PAY THE PLAINTIFF'S CLAIM, and \$» for costs, within the time for serving and filing your statement of defence, you may move to have this proceeding dismissed by the court. If you believe the amount claimed for costs is excessive, you may pay the plaintiff's claim and \$400.00 for costs and have the costs assessed by the court.

TAKE NOTICE: THIS ACTION WILL AUTOMATICALLY BE DISMISSED if it has not been set down for trial or terminated by any means within five years after the action was commenced unless otherwise ordered by the court.

Date: March 27, 2020

Issued by \_\_\_\_\_  
Local registrar

Address of court office 393 University Ave  
Toronto, ON M5G 1E6

**TO: BMO INVESTORLINE INC.**  
100 King Street West, 21<sup>st</sup> Floor  
Toronto, ON M5X 1A1

**AND TO: CIBC INVESTOR SERVICES INC. C/O CIBC CORPORATE  
SECRETARY'S DIVISION**  
199 Bay Street  
Commerce Court West, 44<sup>th</sup> Floor  
Toronto, ON M5L 1A2

**AND TO: CREDENTIAL QTRADE SECURITIES INC.**  
800-1111 West Georgia Street  
Vancouver BC V6E 4T6

**AND TO: DESJARDINS SECURITIES INC.**  
1000-25 York St.  
Toronto, ON M5J 2V5

**AND TO: HSBC SECURITIES (CANADA) INC.**  
70 York Street  
Toronto, ON M5J 1S9

**AND TO: NATIONAL BANK FINANCIAL INC.**

1155 Metcalfe Street, 5<sup>th</sup> Floor  
Montreal, QC H3B 4S9

**AND TO: QUESTRADE INC.**  
5650 Yonge Street, Suite 1700  
Toronto, ON M2M 4G3

**AND TO: RBC DIRECT INVESTING INC, C/O SUBSIDIARY GOVERNANCE  
OFFICE**  
200 Bay Street,  
Royal Bank Plaza  
South Tower, 12<sup>th</sup> Floor  
Toronto, ON M5J 2J5

**AND TO: SCOTIA CAPITAL INC.**  
Corporate Secretary's, 8<sup>th</sup> Floor  
40 King Street West  
66<sup>th</sup> Floor, Scotia Plaza  
Toronto, ON M5W 2X6

**AND TO: TD WATERHOUSE CANADA INC.**  
66 Wellington St W  
TD Tower, 15<sup>th</sup> Floor  
Toronto, ON M5K 1A2

**AND TO: LAURENTIAN BANK SECURITIES INC.**  
1360 Rene-Levesque West Blvd, Suite 620  
Montreal, QC H3G 0E8

**AND TO: BBS SECURITIES INC.**  
199 Bay Street, Suite 2600  
Commerce Court West  
Toronto, ON M5L 1E2

## CLAIM

1. The Plaintiffs claim on their own behalves and on behalf of the other Class Members:

- (a) an order certifying this action as a class proceeding pursuant to the *Class Proceedings Act, 1992*, S.O. 1992, c. 6 ("*CPA*"), and appointing the Plaintiffs as the representative plaintiffs for the Class;
- (b) a declaration that the Defendants were negligent in their conduct with respect to the administration and operation of the Discount Brokerages, particularized below;
- (c) a declaration that the Defendants are liable to the Plaintiffs and the other Class Members for breach of contract;
- (d) a declaration that the Defendants were unjustly enriched by the acts and omissions pleaded herein;
- (e) a declaration that the Defendants are liable for knowing receipt and knowing assistance of breach of trust;
- (f) an order requiring the Defendants to account to the Plaintiffs and the other Class Members for their profits realized through Trailing Commissions, and to disgorge such profits to the Class;
- (g) damages and/or equitable compensation in a sum this Court finds appropriate at the trial of the common issues or at a reference or references to restore the Plaintiffs and the other Class Members to the position they would have been in had the Defendants not paid and/or received the Trailing Commissions;
- (h) punitive damages in an amount that this Court finds appropriate at the trial of the common issues or at a reference or references;

- (i) an order directing a reference or giving such other directions as may be necessary to determine issues not determined at the trial of the common issues;
- (j) an equitable rate of interest on all sums found due and owing to the Plaintiffs and the other Class Members to compensate them for the diminution in the value of their investments resulting from the Defendants' payment and/or receipt of the Improper Management Fees;
- (k) prejudgment and post judgment interest pursuant to the *CJA*;
- (l) costs of this action on a substantial indemnity basis or in an amount that provides full indemnity;
- (m) pursuant to section 26(9) of the *CPA*, the costs of notice and of administration;
- (n) plan of distribution of the recovery in this action plus applicable taxes; and,
- (o) such further and other relief as this Honourable Court may deem just.

## **OVERVIEW**

2. This class proceeding concerns the payment of illegal and improper trailing commissions to the Defendants ("**Trailing Commissions**"). The Defendants collected massive sums in wrongful payments while providing no benefit or consideration to the Class. In almost all circumstances, the Class had no idea it was paying these Trailing Commissions to the Defendants, or for what purpose.

3. The Defendants operate online investment brokerage platforms. They sell mutual fund products to investors that carry costly commissions commonly referred to as Trailing Commissions. Trailing Commissions are paid to the Defendants by the companies that manage and operate mutual funds ("**Mutual Fund Managers**") on an ongoing basis when the Defendants' clients invest in mutual funds. Unbeknownst to

ordinary investors, Trailing Commissions are paid out of the value of their investments on an ongoing basis, thereby steadily depleting their value.

4. The Defendants' online brokerages are often referred to as "**Discount Brokerages**", or "order execution only" brokerages. Class Members create accounts with the Defendants and make investment choices through online investment platforms. The Defendants execute securities trades for Class Members without needing to employ the assistance of a "live" broker. The Class Members are sometimes referred to as "DIY" investors.

5. Trailing Commissions are designed to pay the selling broker a fee on a reoccurring and continuous basis. The Trailing Commission "trails" the investment choice made by the investor. Trailing Commissions are designed to compensate the broker for the "advice and services" the broker has provided to the investor client. Trailing Commissions are paid out of the value of the client's holdings in the mutual fund. Trailing Commissions are paid directly by the Mutual Fund Manager to the broker.

6. Trailing Commissions for "advice and services" are improper in the context of Discount Brokerage investing and should never have been paid by, collected from or charged back to the Class Members. Discount Brokerages cannot and do not provide "advice and services" to their investor clients. As a result, the Trailing Commissions paid to the Defendants were improper and constitute an unlawful loss suffered by the Class.

7. Discount Brokerages are regulated by the Investment Industry Regulatory Organization of Canada ("**IIROC**"), the Canadian Securities Administrators ("**CSA**"), and the provincial securities administrators. Under the IIROC Rules, Discount Brokers are prohibited from providing investment advice to investors. Discount Brokerages are designed to allow "DIY" investors to make trades themselves, without relying on the input of a traditional investment broker. In theory, these brokerages come at a 'discount' because they do not provide investment advice. In practice, such illegal fees for advice are commonly charged, particularly in the case of Trailing Commissions.

8. Trailing Commissions create conflicts of interest. The existence of a Trailing Commission incentivizes a "live" broker to advise their client to choose a mutual fund

over an equivalent investment option, because the broker receives a "kick-back" from the Mutual Fund Manager in such circumstances. In the circumstance of a Discount Brokerage, where there is no "live" broker and advice to investors is prohibited, such Trailing Commissions serve no purpose.

9. Discount Brokerages face a conflict of interest when they:
  - (a) decide what investment products to make available;
  - (b) choose to present various investment products to an investor; and,
  - (c) are faced with the option to inform the investor that an equivalent investment is available which does not carry a Trailing Commission.

10. The Discount Brokerages' conflict of interest manifests itself when they prioritize investment options which carry Trailing Commissions. In all circumstances, such products should never have been sold through Discount Brokerages because it violates their regulatory obligation to avoid conflicts of interest. Equivalent or superior investments were available and Discount Brokerages are not entitled to Trailing Commissions for "advice and services". In the alternative, the Trailing Commissions collected by the Defendants should have been returned to the Class Members, because the Defendants had no right to collect such fees.

11. Every Trailing Commission that was collected by the Defendants through the sale of mutual funds is rightly the property of the Class Members. These illegal fees are worth hundreds of millions of dollars. The savings of ordinary Canadians have been improperly and irrevocably depleted while the Defendants have reaped massive illegal profits.

#### **THE PLAINTIFFS AND THE CLASS**

12. The Plaintiff, Denis Frayce, is an individual who resides in the City of Montreal, in the Province of Quebec. Mr. Frayce has used the discount brokerage services of several Defendants since the late 1980s.

13. In 1987, Mr. Frayce purchased 357 units of the Trimark Fund via his Disnat account, which he continues to hold along with additional units he purchased via Disnat in subsequent years. In 2015, he transferred these mutual fund holdings to an account with TD Direct Investing. Trailing fees were inappropriately paid by the Mutual Fund Managers to the Desjardins and TD Defendants (as defined below), to the detriment of Mr. Frayce. At no point did Mr. Frayce receive any advice from the Desjardins or TD Defendants, nor was any available to Mr. Frayce.

14. In 1988, Mr. Frayce purchased 37 units of the Cundill Value Fund A (renamed Mackenzie Cundill Value-A around 1998) via his Disnat account, which he continues to hold along with additional units he purchased via Disnat in subsequent years. In 2015, he transferred these mutual fund holdings to an account with TD Direct Investing. Trailing fees were inappropriately paid by the Mutual Fund Managers to the Desjardins and TD Defendants (as defined below), to the detriment of Mr. Frayce. At no point did Mr. Frayce receive any advice from the Desjardins or TD Defendants, nor was any advice available to Mr. Frayce.

15. In 2016, Mr. Frayce purchased 5,416 units of the TD Investment Savings Account (TD8150) via TD Direct Investing. Trailing fees were inappropriately paid to the TD Defendants (as defined below), to the detriment of Mr. Frayce. At no point did Mr. Frayce receive any advice from the TD Defendants, nor was any advice available to Mr. Frayce.

16. The Plaintiff, Maxwell Wallace, is an individual who resides in the City of Toronto, in the Province of Ontario. Mr. Wallace has used the discount brokerage services of several Defendants since the early 2010s.

17. In or around 2012, Mr. Wallace purchased 1,198 units of the BMO Growth & Income Fund (Advisor series) and 758 units of the CI Signature Enhanced Yield Fund via BMO Investorline. He held these units in an account with BMO Investorline until 2013. Mr. Wallace purchased other mutual funds via BMO Investorline, among them 7,976 units of the RBC O'Shaughnessy U.S. Value Fund (A series) in 2013, which he sold in 2015. Trailing fees were inappropriately paid by the Mutual Fund Managers to the BMO Defendants (as defined below), to the detriment of Mr. Wallace. At no point



did Mr. Wallace receive any advice from the BMO Defendants, nor was any advice available to Mr. Wallace.

18. Since 2017, Mr. Wallace has held mutual fund units in accounts with Questrade. Questrade has received trailing fees from these mutual funds, to the detriment of Mr. Wallace. In some cases, Questrade has charged monthly fees in order to rebate the trailing fees it received back to Mr. Wallace. In other cases, Questrade has not rebated the trailing fees back to Mr. Wallace at all.

19. In 2017, Mr. Wallace transferred 3,017 units of the Sentry U.S. Growth and Income (A series) mutual fund from a full service financial advisor, Assante Wealth Management, to a non-registered account with Questrade. He purchased an additional 752 units of this mutual fund through Questrade in 2018. Questrade charged Mr. Wallace fees of \$29.95 per month in order to provide quarterly rebates of the trailing fees it received out of the value of Mr. Wallace's investment in this mutual fund, back into Mr. Wallace's non-registered account. In 2018, Mr. Wallace purchased 755 units of CI Global Health Sciences Corporate Class and 1,531 units of the Fidelity Global Innovators Class mutual funds via Questrade and held them in a registered account. He sold these units in 2019 and 2020, respectively. Questrade received trailing fees from these mutual funds and did not give the money back to Mr. Wallace, to the detriment of Mr. Wallace. The value of the trailing fees did not exceed the cost of the \$29.95 monthly fee Questrade would have charged for quarterly rebates. At no point did Mr. Wallace receive any advice from the Questrade Defendants, nor was any advice available to Mr. Wallace.

20. The Plaintiffs are seeking certification of the following class (collectively referred to as the "Class" or "Class Members"):

All persons, wherever they may reside or be domiciled, who purchased a mutual fund through a Defendant Discount Broker.

Excluded Persons means the Defendants, the past and present parents, subsidiaries, affiliates, officers, directors, senior employees, legal representatives, heirs, predecessors, and the successors and assigns of the Defendants.

## **THE DEFENDANTS**

### *BMO InvestorLine Inc. ("BMO Defendants")*

21. BMO InvestorLine Inc. is a corporation duly incorporated pursuant to the laws of Canada and is a wholly owned subsidiary of Bank of Montreal, with its head office in Toronto, Ontario. BMO InvestorLine Inc. is an investment dealer in all provinces and territories.

22. BMO InvestorLine Inc. offers two online client services: "adviceDirect" and "Self-Directed." The former is a full service brokerage service that offers advisory accounts for clients and provides suitability recommendations through its online platform with the involvement of registered representatives. The latter is a self-directed investing platform that operates as a Discount Broker pursuant to applicable IIROC Rules.

### *CIBC Investor Services Inc. ("CIBC Defendants")*

23. CIBC Investor Services Inc. is a corporation duly incorporated pursuant to the laws of Canada and is a subsidiary of Canadian Imperial Bank of Commerce, with its head office in Toronto, Ontario. CIBC Investor Services Inc. is a licensed investment dealer in all provinces and territories, and provides online discount brokerage services through CIBC Investor's Edge, a division of CIBC Investor Services Inc.

### *Credential Qtrade Securities Inc. ("Qtrade Defendants")*

24. Credential Qtrade Securities Inc. is a corporation duly incorporated pursuant to the laws of Canada, with its head office in Vancouver, British Columbia.

25. Credential Qtrade Securities Inc. is a registered broker in each Canadian province and territory in which it accepts accounts. Qtrade Investor is the online brokerage division of Credential Qtrade Securities.

26. Credential Qtrade Securities Inc. is a wholly owned subsidiary of Aviso Wealth Inc., a corporation duly incorporated pursuant to the laws of Canada. Aviso Wealth Inc. is a wholly-owned subsidiary of Aviso Wealth LP, which in turn is owned 50% by

Desjardins Financial Holding Inc. and 50% by a limited partnership owned by five Provincial Credit Union Centrals and The CUMIS Group Limited. Aviso Wealth LP is an Ontario Limited Partnership.

*Desjardins Securities Inc. ("Desjardins Defendants")*

27. Desjardins Securities Inc. is a corporation duly incorporated pursuant to the laws of Canada, with its head office in Montreal, Quebec.

28. Desjardins Securities Inc. is a wholly owned subsidiary of Desjardins Financial Holding Inc., with its head office in Montreal, Quebec. Desjardins Financial Holding Inc. is an indirectly wholly owned subsidiary of the Fédération des caisses Desjardins du Québec. Desjardins Financial Holding Inc. is a corporation duly incorporated pursuant to the laws of Quebec, with its head office in Montreal, Quebec. Desjardins Financial Holding Inc. indirectly holds a significant interest in Credentials Qtrade Securities Inc.

29. Desjardins Securities Inc. is an investment dealer registered in the provinces of Alberta, British Columbia, Manitoba, New Brunswick, Newfoundland and Labrador, Nova Scotia, Ontario, Prince Edward Island, Quebec and Saskatchewan.

30. Desjardins Securities Inc. provides online discount brokerage services through the trade name "Desjardins Online Brokerage." Further, Desjardins' discount brokerage products and services are consolidated under the trademark "Disnat".

*HSBC Securities (Canada) Inc. ("HSBC Defendants")*

31. HSBC Securities (Canada) Inc. is a corporation duly incorporated pursuant to the laws of Ontario and is a wholly owned subsidiary of HSBC Bank Canada, with its head office in Toronto, Ontario.

32. HSBC Bank Canada is a subsidiary of HSBC Holdings plc, with its head office in Vancouver, British Columbia.

33. HSBC Holdings plc is a Public Limited Company, with its head office in London, UK.

34. HSBC Securities (Canada) Inc. is a brokerage firm offering online brokerage services through its division, HSBC InvestDirect.

National Bank Financial Inc. ("National Bank Defendants")

35. National Bank Financial Inc. is a corporation duly incorporated pursuant to the laws of Canada, with its head office in Montreal, Quebec. National Bank Financial Inc. is a wholly owned subsidiary of National Bank of Canada.

36. National Bank Direct Brokerage is a division of National Bank Financial Inc., which provides online discount brokerage services.

Questrade Inc. ("Questrade Defendants")

37. Questrade Inc. is a corporation duly incorporated pursuant to the laws of Ontario, with its head office in Toronto, Ontario. Questrade Inc. is a wholly owned subsidiary of Questrade Financial Group Inc. Questrade Financial Group Inc. is a corporation duly incorporated pursuant to the laws of Ontario, with its head office in Toronto, Ontario.

38. Questrade Inc. is a registered investment dealer. Questrade Inc., through the trademark name of Questrade, provides online discount brokerage services.

RBC Direct Investing Inc. ("RBC Defendants")

39. RBC Direct Investing Inc. is a corporation duly incorporated pursuant to the laws of Canada, with its head office in Toronto, Ontario. RBC Direct Investing Inc. is a wholly owned subsidiary of Royal Bank of Canada. RBC Direct Investing Inc. provides online discount brokerage services through the business name of RBC Direct Investing.

Scotia Capital Inc. ("Scotia Defendants")

40. Scotia Capital Inc. is a corporation duly incorporated pursuant to the laws of Ontario, with its head office in Toronto, Ontario. Scotia Capital Inc. is a registered broker in all provinces and territories of Canada. Scotia Capital Inc. is a wholly owned subsidiary of The Bank of Nova Scotia.

41. Scotia iTRADE is a division of Scotia Capital Inc., and is an online discount brokerage service.

TD Waterhouse Canada Inc. ("TD Defendants")

42. TD Waterhouse Canada Inc. is a corporation duly incorporated pursuant to the laws of Ontario, with its head office in Toronto, Ontario.

43. TD Waterhouse Canada Inc. is a subsidiary of Toronto-Dominion Bank.

44. TD Direct Investing is the online discount brokerage division of TD Waterhouse Canada Inc.

BBS Securities Inc. ("BBS Defendants")

45. BBS Securities Inc. is a corporation duly incorporated pursuant to the laws of Ontario, with its head office in Toronto, Ontario. BBS Securities Inc. is registered in all provinces and territories of Canada as an investment dealer.

46. BBS Securities Inc. is a wholly owned subsidiary of CI Financial Corp. CI Financial Corp. is a corporation duly incorporated pursuant to the laws of Ontario, with its head office in Toronto, Ontario.

47. Virtual Brokers is the online discount brokerage division of BBS Securities Inc.

Laurentian Bank Securities Inc. ("Laurentian Defendants")

48. Laurentian Bank Securities Inc. is a corporation duly incorporated pursuant to the laws of Canada, with its head office in Montreal, Quebec. Laurentian Bank Securities Inc. is a wholly-owned subsidiary of Laurentian Bank of Canada.

49. Laurentian Bank Discount Brokerage is the discount brokerage division of Laurentian Bank Securities Inc.

**MUTUAL FUNDS**

50. Mutual funds provide investors with economies of scale, allow for diversification and are generally purported to be managed by knowledgeable and professional investors.

Investors in mutual funds pay fees to the Mutual Fund Managers in exchange for the 'active management' of the underlying securities. Mutual fund investing is massively popular in Canada, the combined assets of Canada's mutual fund industry totaled over \$1.5 trillion dollars in September 2018. Canadians pay the highest mutual fund fees in the world.

51. Units in mutual funds are distributed, marketed and sold to investors by investment brokers.

52. Mutual fund investors in Canada primarily incur two kinds of fees, sales charges and ongoing fund fees. Sales charges are transaction-based that investors pay directly to their broker. Fund fees are ongoing charges paid to their brokers from fund assets, which means that investors pay these fees indirectly to their investment brokers. A significant portion of fund fees are Trailing Commissions.

53. The purpose of Trailing Commissions is to subsidize the advice that investment brokers provide to investors. This purpose is clearly outlined in NI-31-103, Registration Requirements, Exemptions, and Ongoing Registrant Obligations, which requires a Discount Brokerage to report annually to each client on the dollar amount of Trailing Commissions received "for the services and advice we provide you."

54. In the context of Discount Brokerage, Trailing Commissions are improper and create a conflict of interest, which is further particularized below.

55. Mutual fund units that carry Trailing Commissions payable to the broker are often defined as Class "A" mutual funds. They are often called "advisor Class" or "A Class" because they incorporate the fee for advice. This commission structure has existed since the popularity of mutual funds took off in the latter half of the 20<sup>th</sup> century.

56. As Discount Brokerages gained in popularity in the 2000s and 2010s, Mutual Fund Managers responded by creating units of mutual funds that carried low or no Trailing Commissions. Mutual Fund Managers recognized that Discount Brokerages cannot provide advice, and provided investors with the option of investing in the mutual fund without having to pay for advice they cannot receive. These investment options are often called "D" Class, or "discount Class" units of the same fund. These are designed to

be marketed and sold on discount brokerage platforms. "D" Class units are largely the same as "A" Class, but yield a higher return to the individual investor because the advice portion of the fee has been stripped away.

## **DISCOUNT BROKERAGES**

57. Hundreds of thousands of Canadians make or hold investments through Discount Brokerages, such as those operated by the Defendants, at any given time. Discount Brokerages are online web platforms that allow investors to make a multitude of investments without having to place an order through a traditional "broker". One main difference between a traditional broker, who will ordinarily provide advice and other services, and an online discount brokerage, is that the investor can receive no advice from the online platform, or otherwise. As a result, the Discount Brokerage should be less expensive to the investor, as it charges lower, or no commissions, for the trades they execute.

58. Discount Brokerages allow investors and consumers to buy and sell securities online while offering little or no services or support. IIROC's regulatory requirements are intended to ensure that Discount Brokerage clients make their own investment decisions, without receiving any recommendations or suitability assessments from the Discount Brokerages. As such, Discount Brokerages are forbidden from giving "advice" under IIROC's Rules, and are exempt from the suitability requirements so long as they do not provide any recommendations to clients.

59. Canadians employ the services of Discount Brokerages to avoid paying large fees such as Trailing Commissions to "live" or "full-service" brokers for the advice such brokers provide. Accordingly, each Class Member reasonably believed that they would not pay fees related to "advice and services."

### **Discount Brokerage Wrongdoing**

60. Discount Brokerages should not provide mutual funds with Trailing Commissions for purchase by their clients. Discount Brokerages act improperly and unlawfully every time they sell a mutual fund with a Trailing Commission, which are inappropriate for sale via Discount Brokerage. In the alternative, each time a Discount

Brokerage sells a mutual fund and it collects a Trailing Commission, it is obliged to return the fee to its client. Discount Brokerages have no right to retain the Trailing Commission they collect for advice they cannot provide.

61. By offering and selling mutual fund units that are not designed to be sold through Discount Brokerages, the Defendants acted unlawfully and placed themselves in a conflict of interest. In the circumstances, the Defendants should only have offered investment products that did not carry illegal Trailing Commissions.

62. The Defendants have organized their online platforms and software in a manner which causes investors to invest in mutual fund units that carry unnecessarily high fees. In some cases, the Defendants have recognized the unlawful harms they have inflicted on Class Members, but have only taken minor measures to mitigate such harms.

63. For example, starting in June 2017, Scotia iTrade claimed to offer Series A mutual funds only when the equivalent Series D funds were not made available by the Mutual Fund Manager. Before that date, Scotia iTrade prioritized the sale of Series A mutual funds, to the detriment of the Class. Furthermore, Scotia iTrade continues to collect and retain Trailing Commissions for "advice and services" on Series A Mutual Funds when it unilaterally determines that there are no equivalents series, even though such "advice and services" cannot be provided to the Class Members. Such practices are common across the industry and are unlawful in all circumstances.

64. The Defendants have abused the authority entrusted to them by the Class Members and as a result have systematically deprived the Class of higher returns on their portfolios, while correspondingly increasing their own profits at the direct expense of their own clients.

### **Trailing Commissions Constitute a Conflict of Interest**

65. A mutual fund's management expense ratio, or "MER", is published by the Mutual Fund Manager. The MER advises investors of the costs of operating and distributing a mutual fund. A large portion of the MER charged to investors is the Trailing Commission which is redistributed to the broker. The Trailing Commission is



embedded in the management fee, and is often not disclosed as being a distinct charge or fee.

66. Trailing Commissions, on average, make up about half of the value of the MER. Trailing Commissions are paid by the Mutual Fund Managers to brokers on a regular basis, as long as their clients hold investments in the funds.

67. As a result, DIY investors purchase mutual fund securities through Discount Brokerages and pay for services and advice they never receive and do not want.

68. Discount Brokerages are required to operate in a manner that avoids a conflict of interest. In particular, under Rules 42.1-42.3 of the IIROC Rulebook, Discount Brokers:

- (a) shall take reasonable steps to identify existing and potential material conflicts of interest between the interests of the Dealer Member or Approved Person and the interests of the client;
- (b) must maintain written policies and procedures in determining and dealing with conflicts of interest;
- (c) must consider the implications of any existing or potential material conflicts of interest;
- (d) must address existing or potential material conflicts of interest in a fair, equitable and transparent manner, considering the best interests of their clients; and
- (e) must avoid existing or potential material conflicts of interest that cannot be addressed in a fair, equitable and transparent manner, considering the best interests of their clients.

69. Discount Brokers are also subject to National Instruments ("NI") issued by the CSA. Under NI-31-103, Discount Brokerages are obliged to take reasonable steps to identify and respond to existing and potential material conflicts of interest, and to disclose the nature and extent of the conflict to the client where a reasonable investor

would expect to be informed of same. If the risk of harming a client is too high because of the conflict of interest, the conflict must be avoided.

70. Discount Brokerages breach the above IIROC Rules and NI-31-103 when they make mutual funds that carry Trailing Commissions available for sale, and when they sell them to their clients. In particular, the following acts are manifestations of the conflicts of interest inherent in Discount Brokerages collecting Trailing Commissions;

- (a) Selling Series "A" units or other units that carry trailing fees, which are not meant to be sold through Discount Brokerages, but are designed for brokers who are able to provide advice to investors;
- (b) failing to disclose to investors that equivalent mutual fund investment options are available that do not carry fees for "advice and services", such as Series "D"-type units, are available through the sales platform;
- (c) failing to sell only Series "D"-type units of mutual funds, or other investment vehicles such as ETFs, which are specifically designed to be sold through Discount Brokerages and which do not result in additional advice-based fees to be paid to the Discount Brokerage.

71. Each time a Discount Brokerage sells a client an investment option that carries Trailing Commissions, they act against the best interests of their clients, contrary to NI-81-105CP.

72. The payment of Trailing Commissions to Discount Brokerages is also contrary to NI-81-105, which limits the circumstances in which Trailing Commissions can be paid to those where the obligation to make the payment arises after the time of the trade.

73. As a result, each mutual fund transaction that allows for Trailing Commissions to be paid to Discount Brokerages is improper. The Trailing Commissions represent an equal loss to the Class Members, which should never have been suffered.

### **Defendants' Knowledge of Wrongdoing**

74. The Defendants have long known the unlawfulness of their practice of collecting Trailing Commissions from clients when they provided no "advice or services" in return. However, the Defendants have valued their own profits over the financial wellbeing of their clients to wrongfully maximize profits.

75. For example, the Canadian Securities Administrators in the CSA Discussion Paper and Request for Comment 81-407 dated December 13, 2012 addressed the impropriety of Discount Brokerage mutual fund investors "paying for advice and services they do not receive" through Series "A" mutual fund purchases.

76. In January 2017, the CSA issued CSA Consultation Paper 81-408. In that document, the CSA found that embedded commissions, including Trailing Commissions, raise conflicts of interest, limit investor awareness and do not align with the services provided to investors. In particular that document states:

- (a) "discount brokers who provide execution-only services often distribute fund series that pay them the same trailing commission that would be paid to a full service dealer"
- (b) "the majority of fund series sold are the full trailing commission fund series despite the increased availability of Discount/DIY fund series (typically denoted "D" series) in the market. Consequently, many DIY mutual fund investors in the online/discount brokerage channel indirectly pay for services they do not receive"
- (c) "the bulk (roughly 84%) of mutual fund assets held in the online/discount brokerage channel remain invested in the regular retail fund series paying full unreduced trailing commissions to the discount broker"
- (d) "not all investment fund managers offer a discount/DIY series (eg Series D with reduced trailing commission of .25% or less) on their funds, nor do all discount brokers opt to put these series on their shelf when available. These series are available for purchase through certain discount brokerages only. Those investment fund managers that do not offer a discount/DIY series typically make their regular retail series available for

purchase through the discount channel. These series pay full unreduced trailing commissions of 1% to the discount brokerage for execution-only services".

77. The inherent conflict of interest associated with the sale of mutual funds carrying Trailing Commissions through Discount Brokerages was identified by IIROC in Notice 18-0075, which was published on April 9, 2018. IIROC stated that "OEO firms [i.e. discount brokerages] offering funds that pay a trailing commission for ongoing advice (e.g., Series A funds) is an example of a conflict of interest."

78. On June 21, 2018, the CSA published a notice setting out an intended policy change with respect to mutual fund commissions – CSA Staff Notice 81-330. In this document, the CSA proposed a full prohibition on discount brokers who do not make a suitability determination on connection with the distribution of mutual fund securities, stating:

- (a) "despite the limited services provided by discount brokerages, with few exceptions, they typically receive the same trailing commission that is provided to full-service dealers. This results in DIY investors who hold mutual fund securities through discount brokerages paying for investment advice that is not received or desired."
- (b) "we note that dealers may not make a series D option available to clients even in cases where the investment fund manager offers a series D purchase option....this suggest that 83% of mutual fund assets in the discount channel remain in full trailing commission-paying series."
- (c) "in our view, the fees paid by a vast majority of DIY investors in this channel do not appear to align with the execution-only nature of the services they receive. We also observe no justifiable rationale for the practice of paying discount brokerage dealers an ongoing trailing commission for the sale of a mutual fund. For example, other securities, including most ETFs are commonly purchased and sold by way of an upfront transaction fee."

- (d) "to address potential conflicts in the discount brokerage channel and other instances where dealers do not make investment recommendations, as well as to better align the fees investors pay with the services they receive, we propose to prohibit investment fund managers from paying, and dealers from soliciting and accepting, trailing commissions (whether for advise or any other service) where the dealer does not make a suitability determination in connection with the distribution of prospectus qualified mutual fund securities.

79. On September 13, 2018, the CSA released a "Notice of Request for Comments" on their proposed amendments to NI 81-105. These proposed changes include a ban described above. The CSA Stated:

- (a) "For DIY mutual fund investors, we anticipate that the proposed amendment will lead to fees, paid directly, that better align with the more limited services provided by registrants that are not providing suitability determinations. Likewise, we anticipate that the management fees of those fund series that are distributed in the online/discount brokerage channel are likely to fall by the total amount of trailing commissions embedded today".
- (b) online/discount brokerages will need to adjust their business models to bring mutual fund sales in-line with their commission practices for every other security currently offered on their platforms.

80. On December 19, 2019, the CSA published Staff Notice 81-332, outlining that all provincial and territorial members of the CSA will publish for adoption final amendments later in 2020 to ban payments of trailing commissions to dealers who do not make a suitability determination, such as Discount Brokerages.

81. The Defendants had full knowledge of the above-noted publications and regulatory guidance.

82. The Defendants' actions were improper, negligent and illegal long before the regulatory action to make such Trailing Commissions illegal. Throughout the Class

Period, the Defendants had knowledge that they were collecting money for advice and services that were never provided to Class Members. The Defendants purposely limited its offerings to Class Members to the Mutual Fund Securities that carried the highest Trailing Commissions. Even when the Defendants made Series D-type Mutual Fund units available on their trading platforms, they continued to allow Class Members to purchase the equivalent Series A Mutual Fund units, or units that do not carry a trailing fee, rather than alerting them to the equivalent alternative. In any circumstance, offering Series A Mutual Funds via Discount Brokerages, was improper and tortious.

83. Alternatively, the Defendants should have refunded the Trailing Commissions they collected to the Class Members in full and without charging excessive administrative fees, rather than retaining such unlawful fees.

## **SOURCES OF THE DEFENDANTS' OBLIGATIONS TO CLASS MEMBERS**

### ***(i) Regulatory***

84. The Defendants operate in a regulated environment and a regulatory regime for investment counsel portfolio managers.

85. The Defendants are subject to the minimum standards set out in the "IIROC Dealer Member Rules" and the "*Canadian Securities Institute Conduct and Practices Handbook*" (the "***Handbook***").

86. The overriding objective for any investor is to maximize their returns, or at the very least, avoid monetary loss through the payment of unnecessary fees, such as the Improper Management Fees.

87. In addition to the IIROC Dealer Member Rules and the *Handbook*, the Defendant's industry and the applicable duties and standards therein are also informed by the: Ontario Securities Commission regulations, the Ontario *Securities Act*, R.S.O. 1990, c. S.5 itself, Canadian Securities Institute policies; CSA policies; and, various National Instruments.

### ***(ii) Contractual***

88. The relationship between each Class Member and the Defendants are defined in part by contracts whereby the Defendants agree to provide online brokerage services, and in exchange, the Class Members agree to pay for these services.

89. Class Members' contracts are informed by the regulatory context in which the Defendants operate, which sets out certain standards that the Defendants must meet with respect to avoidance of conflicts of interest, and due diligence for its clients, which include the Class Members.

90. It is an express or implied term of Class Members' contracts with the Defendants that the Class Members' financial interests would be placed ahead of illegal or improper fees charged by the Defendants for no juristic purpose.

91. It is also an express or implied term of Class Members' contracts that the Defendants would seek to maximize any returns for the Class Members, including by avoiding charging unnecessary, illegal, improper or avoidable fees.

92. Furthermore, it is an express or implied term of Class Members' contracts that the Defendants would observe a duty of good faith and fair dealing with them, characterized by candour, reasonableness, honesty, and forthrightness. Put another way, it is an express or implied term of Class Members' contracts that the Defendants would not act in bad faith by being, for example, untruthful, misleading or unduly insensitive.

***(iii) Duty of Care***

93. The relationship between the Defendants and Class Members is a relationship of proximity, such that it would be reasonably foreseeable that any lack of care on the part of the Defendants relating to the financial services to the Class would be likely to cause harm to the members of the Class.

94. In these circumstances, the Defendants owe a duty of care to the Class Members. At a minimum this duty of care requires that the Defendants take reasonable steps to ensure that they would not make mutual funds available for sale without refunding in full Trailing Commissions collected for "advice and services".

95. The content of this duty of care to the Class is informed by the Defendant's obligations under the regulatory scheme and in particular the IIROC Regulations and the *Handbook*.

## CAUSES OF ACTION

### *Breach of Contract*

96. Contrary to the express or implied terms of the Class Members' contracts, the Defendants breached Class Members' contracts by, *inter alia*:

- (a) collecting fees for advice and services which were impossible in the circumstances;
- (b) failing to protect Class Members' from unnecessary or easily avoidable fees that could adversely impact their investments;
- (c) failing to act in good faith by placing their own financial interests ahead of those of Class Members or by charging unlawful fees;
- (d) failing to provide investment options that allow Class Members to avoid paying unlawful and inappropriate Trailing Commissions;
- (e) failing to make Class Members aware of comparable but cheaper investment vehicles;
- (f) failing to return the improper Trailing Commissions to Class Members in full; and,
- (g) upon learning of comparable but cheaper alternatives, failing to update the Class Members on an ongoing basis.

97. The Defendants breached the aforementioned contracts. As a result of these the Plaintiffs and Class Members have suffered losses and damages.

98. Further particulars of the Defendant's conduct are within the Defendant's knowledge and will be provided before the trial of the common issues.



### *Negligence*

99. Given the relationship of proximity that exists in the customer relationship between the Defendants and Class Members, the Defendants owe the Class Members a duty of care. This duty of care is informed by the Defendant's obligations set forth, *inter alia*, in the IIROC Rules and CSA policy requirements.

100. This duty requires that the Defendants take reasonable steps to ensure that they provide financial services in a manner that advanced and was consistent with the Class Members' interests and provide timely, effective, and informed customer service to the Class.

101. The Defendants have breached the standard of care. Particulars of that breach include, but are not limited to:

- (a) offering for sale and selling investment options that are inappropriate for the Discount Brokerage channel;
- (b) failing to provide equivalent Series "D"-type investment options, or similar options, that carry low or no fees instead of an equivalent Series "A" or other unit that carries a Trailing Fee;
- (c) failing to inform clients when equivalent Series "D"-type investment options are available, and allowing the sale of Series "A" or units that carry trailing commissions to take place instead;
- (d) failing to refund in full Trailing Commissions obtained through the sale of Series "A" or other units that carry trailing fees;
- (e) failing to adhere to the applicable regulations and professional requirements;
- (f) failing to implement a system that would inform current and future clients of similar investment products that carried a lower or no Trailing Commission

- (g) putting its own interests, and those of its employees, agents and other persons under its supervision, ahead of the interests of clients;
- (h) permitting improper practices to be perpetrated against clients; and
- (i) permitting an atmosphere that allowed the Defendants to usurp client's financial interests with their own financial interests.

102. The Defendants knew or ought to have known that a breach of its duty of care would cause loss and damages to the Class Members.

103. As a result of the Defendant's acts and omissions, the plaintiffs and Class Members have suffered reasonably foreseeable damages and losses, for which they are liable to pay damages.

***Knowing Receipt/Knowing Assistance***

104. The Mutual Fund Managers and the Class Members are in a trust relationship. Each Mutual Fund Manager holds the Class Members' investment property in trust, both at common law and pursuant to contract. The Defendants receive Trailing Commissions, which are taken from funds which the Mutual Fund Companies are holding in trust for the Class. The Trailing Commissions unlawfully reduce the value of the trust assets held by the Mutual Fund Managers. The Defendants had knowledge that the Trailing Commissions, which were paid out of the trust funds held by the Mutual Fund Companies, were being paid improperly and for no good, reasonable or legal purpose. The Defendants knowingly received such trust properties for no lawful or proper purpose.

105. In addition, or in the alternative, the Defendants knowingly assisted the Mutual Fund Managers in breaching their relationship of trust with Class Members by making Class "A" Mutual Funds or other units that carry Trailing Commissions available for sale through the Discount Brokerages. Due to the existence of the conflicts of interest, and the other impropriety of Trailing Commissions pleaded herein, the Defendants knowingly assisted in the breach of the trust relationship between the Mutual Fund Managers and the Class.

106. As a result of the Defendant's acts and omissions, Class Members suffered damages and losses, for which it is liable.

***Unjust Enrichment***

107. The Defendants have been unjustly enriched by the receipt of the Trailing Commissions out of the assets of the Class.

108. The Class Members have suffered a corresponding deprivation by the reduction in the value of their investments arising from the payment of the Trailing Commissions out of their investments. The Defendants were unjustly enriched in an equivalent amount, which is the value of each Trailing Commission paid on mutual funds.

109. There is no juristic reason for the enrichment of the Defendants. The Trailing Commissions were received by the Defendants as a result of their own wrongful acts and omissions. Further, any contracts upon which the Defendants purport to rely to justify the receipt of the Trailing Commissions do not require the receipt the Trailing Commissions, fail for lack of consideration, or are void for lack of reasonable notice, unconscionability, or being contrary to public policy.

***Waiver of Tort***

110. In the alternative to damages, the Plaintiffs plead an entitlement to waive the torts and claim an accounting, or other such restitutionary remedy, for disgorgement of all revenues generated by the Defendants from their unlawful conduct.

111. It would be unconscionable for the Defendants to retain the revenues generated by the conduct set out herein.

**DAMAGES**

112. The Plaintiffs and the other Class Members have suffered loss and damage as a result of the Defendants' acts and omissions particularized herein.

113. As a result of the payment of the Trailing Commissions out of the assets of the Class, the value of the assets of the Class have been significantly reduced.

114. The Plaintiffs and the other Class Members have also suffered loss and damages as a result of the loss of opportunity to earn a reasonable return on investment if the Trailing Fees had not been paid out by the asserts of the Class.

115. The Defendants knew or ought to have known that as a result of their acts and omissions particularized herein the Class Members would suffer loss and damage.

### **PUNITIVE DAMAGES**

116. The Defendants were, at all times, aware that their actions would have a significant adverse impact on the Class Members. The Defendants' conduct was high-handed, reckless, without care, deliberate, and in disregard of the Class Members' rights. Accordingly, the Plaintiffs request substantial punitive damages.

### **REAL AND SUBSTANTIAL CONNECTION WITH ONTARIO**

117. The Plaintiffs plead that this action has a real and substantial connection with Ontario because, among other things:

- (a) the Plaintiff Maxwell Wallace resides in Ontario;
- (b) the transactions between the Plaintiffs and Defendants occurred in Ontario;
- (c) many Defendants are domiciled in Ontario;
- (d) the Defendants carry on business in Ontario;
- (e) a substantial portion of the Class Members reside in Ontario; and
- (f) a substantial portion of the damages sustained by the Class were sustained by persons and entities domiciled in Ontario.

### **RELEVANT LEGISLATION**

118. The Plaintiffs plead and rely on the *CPA*, the *Courts of Justice Act*, R.S.O. 1990, c. C.43, and the *OSA*.

**PLACE OF TRIAL**

119. The Plaintiffs propose that this action be tried in the City of Toronto, in the Province of Ontario, as a proceeding under the *CPA*.

March 27, 2020

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Court File No.:

**ONTARIO  
SUPERIOR COURT OF JUSTICE**

Proceeding commenced at Toronto

Proceeding under the *Class Proceedings Act, 1992*

**STATEMENT OF CLAIM**

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