Ontario
Securities
Commission

Commission des
valeurs mobilières
de l'Ontario

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IN THE MATTER OF THE *SECURITIES ACT*,
R.S.O. 1990, c. S.5, AS AMENDED

- AND -

IN THE MATTER OF DAVID CHARLES PHILLIPS AND JOHN RUSSELL WILSON

REASONS AND DECISION

Hearing:	June 5, 6, 7, 10, 11, 12, 17, 19, 20, 24 September 9 and 25, 2013	
Decision:	January 14, 2015	
Panel:	Edward P. Kerwin	- Commissioner and Chair of the Panel
	C. Wesley M. Scott	- Commissioner
Counsel:	Alistair Crawley Bruce O'Toole	- For the Respondents
	Yvonne Chisholm Brooke Shulman	- For Staff of the Commission

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1. OVERVIEW

A. BACKGROUND

[1] This was a hearing before the Ontario Securities Commission (the "**Commission**"), pursuant to section 127 of the *Securities Act*, R.S.O. 1990, c. S.5, as amended (the "**Act**"), to consider whether David Charles Phillips ("**Phillips**") and John Russell Wilson ("**Wilson**") (together, the "**Respondents**") breached the Act and acted contrary to the public interest.

[2] A Statement of Allegations was filed by Staff of the Commission ("**Staff**") on and dated June 4, 2012, and a Notice of Hearing was issued by the Commission on June 4, 2012. Staff filed an Amended Statement of Allegations on and dated April 25, 2013.

B. HISTORY OF THE PROCEEDING

[3] The first appearance in this matter was held on June 25, 2012. Subsequent to that, two pre-hearing conferences were held on October 12, 2012 and May 30, 2013. On January 25, 2013, the hearing on the merits (the "**Merits Hearing**") was set to commence on June 3, 2013.

[4] The Merits Hearing commenced on June 5, 2013 and concluded on September 25, 2013. Evidence was heard on June 5, 6, 7, 10, 11, 12, 17, 19, 20 and 24, 2013. Throughout the tendering of evidence and the testimony of witnesses, the Commission panel was composed of Commissioners Carnwath (Chair), Kerwin and Scott. On August 1, 2013, after Commissioner Carnwath recused himself from the Panel, an order was issued that the hearing would continue before and be decided by a Commission panel (the "**Panel**") comprised of Commissioners Kerwin and Scott.

[5] The Respondents were represented by counsel throughout the Merits Hearing.

[6] On June 24, 2013, following the completion of the evidence phase of the Merits Hearing, Staff and the Respondents agreed and the Commission ordered that closing arguments would be heard on September 9, 2013. Staff filed and served its written submissions on August 2, 2013. The Respondents' written submissions were to be filed and served by August 21, 2013, and Staff's written reply submissions were to be filed and served by August 29, 2013.

[7] On August 6, 2013, the Respondents filed and served a Notice of Motion, seeking (a) leave to tender new evidence ("**New Evidence**") in the Merits Hearing in the form of, (i) the affidavit of Dr. Douglas Hyatt ("**Hyatt**"), sworn July 30, 2013 (the "**Hyatt Affidavit**") with respect to a meeting of the Independent Committee of the Board of Directors of First Leaside Wealth Management Inc. ("**FLWM**") held on November 13, 2011 (the "**November 13, 2011 Meeting**"), and (ii) the unredacted minutes of that meeting, or (b) in the alternative, leave to recall Hyatt to provide oral evidence in the Merits Hearing, and such further and other relief as to the Commission may seem just (the "**August 6, 2013 Motion**"). The Respondents submitted that there is no suggestion that the admission of the New Evidence required calling or recalling further witnesses to respond to or to contest the New Evidence.

[8] On August 8, 2013, in response to the August 6, 2013 Motion, Staff filed and served a Memorandum of Fact and Law, a Brief of Authorities, the affidavit of Stephanie Collins, sworn August 8, 2013, and the affidavit of Sharon Nicolaides, sworn August 9, 2013. Staff submitted that

the August 6, 2013 Motion should be dismissed. Staff also made alternative submissions that, in the event the August 6, 2013 Motion is allowed, (i) the evidence should be in the form of the Hyatt Affidavit only, (ii) the Respondents should not be permitted to recall Hyatt to give oral evidence, and (iii) the Hyatt Affidavit should be given very little weight.

[9] On August 14, 2013, the Respondents filed and served a Reply Memorandum of Fact and Law, a Brief of Authorities and a Supplemental Motion Record, including the affidavit of Clarke Tedesco, sworn August 14, 2013.

[10] On August 16, 2013, having considered the written materials filed by the Parties, the Commission ordered that it would hear the Parties' oral submissions concerning the August 6, 2013 Motion on September 9, 2013, the date previously set aside for closing argument in the Merits Hearing. By order dated September 9, 2013 (the "**September 9, 2013 Order**"), the August 6, 2013 Motion was allowed, and the Hyatt Affidavit was admitted into evidence in the Merits Hearing. Pursuant to the September 9, 2013 Order, the Commission also set the timing for filing and serving written closing submissions and the date of September 25, 2013 for the hearing of oral closing submissions in the Merits Hearing. Staff was ordered to file and serve written closing submissions by September 16, 2013, and the Respondents were ordered to file and serve written reply submissions by September 20, 2013. Oral closing submissions were heard on September 25, 2013, and Staff, counsel for the Respondents and Wilson were in attendance but Phillips was unwell and did not attend.

[11] On June 19, 2014, the Respondents filed and served a Notice of Motion (the "**Stay Motion**"), seeking an order staying the proceeding against the Respondents, specifically the release of the decision on the merits, until a final determination of the civil action commenced on November 7, 2013 against the Commission and others in Court File CV-13-492385. On July 16, 2014, counsel for Staff filed and served Staff's motion record in respect of the Stay Motion.

[12] On July 28, 2014, the Respondents filed and served a Memorandum of Fact and Law and a Brief of Authorities. In response to the Stay Motion, on August 25, 2014, Staff filed and served a Memorandum of Fact and Law and a Brief of Authorities. Staff submitted that the Stay Motion should be dismissed.

[13] On September 10, 2014, the Panel heard oral submissions from the Respondents and Staff in respect of the Stay Motion. In a separate decision dated January 14, 2015, the Panel determined that there is no reasonable apprehension of bias on the part of the Panel. Therefore, the Stay Motion requesting a stay was dismissed.

C. THE RESPONDENTS

i. Phillips

[14] Phillips was the founder of the First Leaside Group (**"FLG"**) and Chief Executive Officer ("**CEO**"), President and director of FLWM from its incorporation until November 2011. Phillips owned 100% of the common shares of FLWM and was "the driving mind" of FLWM.

[15] Phillips was also the CEO, President, Secretary, a director and ultimate designated person ("**UDP**") of, and employed as a salesperson with, First Leaside Securities Inc. ("**FLSI**")**.** In addition, Phillips was the President, Secretary and a director of First Leaside Finance Inc. ("**FL**

Finance"). As of the date of the Merits Hearing, Phillips remained a director of FLWM. (Exhibit 1 -- Grant Thornton Report, p.15; Testimony of Krieger, June 5, 2013, p. 120 and pp. 155-159; Testimony of Phillips, June 19, 2013, p. 7 and p. 96; Exhibit 2 -- Hearing Brief, Volume 1, Jonathan Krieger, Tab 9; Opening Statement of the Respondents dated June 5, 2012, p. 8)

[16] Phillips was registered with the Commission in various capacities since 1981 and he held many roles as a registrant in respect of FLG entities. Phillips was registered as a trading officer and approved as a director and shareholder from March 1, 2004 to February 24, 2012 in respect of FLSI. During the Sales Period, Phillips was a registrant in respect of FLSI and was registered as UDP of FLSI from January 11, 2010 to February 24, 2012. (Testimony of Phillips, June 19, 2013, p. 7 and pp. 99-100; Exhibit 4 -- Hearing Brief: Corporate and Registration Documents, Tab 9; Exhibit 6 -- Affidavit of Stephanie Collins sworn October 28, 2011, p. 4, para. 10)

[17] Phillips' registrations in respect of FLSI were suspended on February 24, 2012 under subsection 29(2) of the Act when the registration for FLSI as an investment dealer under the Act was suspended by the Commission due to the suspension of FLSI's membership with the Investment Industry Regulatory Organization of Canada ("**IIROC**"). (Exhibit 6 -- Affidavit of Stephanie Collins sworn October 28, 2011, p. 4, para. 10; Exhibit 4 -- Hearing Brief: Corporate and Registrations Documents, Tabs 5 and 6)

[18] Phillips was also registered with the Commission in respect of F.L. Securities Inc. ("**FL Securities**") in various capacities, including salesperson, trading officer, director and shareholder from February 27, 1992 to February 28, 2012. Phillips' registrations in respect of FL Securities were suspended on February 28, 2012 under subsection 29(2) of the Act when the registration of FL Securities as a limited market dealer was suspended by the Commission. (Exhibit 4 -- Hearing Brief: Corporate and Registrations Documents, Tabs 5 and 6)

[19] Phillips was at the top of the reporting structure within FLG and directed all significant aspects of the business and growth of FLG, including capital raising, deal origination, deal negotiation and structuring and internal administration. (Testimony of Krieger, June 5, 2013, p. 108, Testimony of Phillips, June 19, 2013, pp. 102-103, Exhibit 1 -- Grant Thornton Report, p. 23)

[20] Phillips approved all FLG proprietary products, including limited partnerships (individually an "**LP**" and collectively "**LPs**") and fund offerings. He explained new products to the registered representatives at FLSI and signed off on all trades for everyone who was selling in the FLG organization. Phillips also hired, fired and supervised the sales staff until November 2011. (Testimony of Chien, Testimony of Phillips, June 19, 2013, p. 112 and pp. 114-115; Testimony of Chien, June 10, 2013, pp. 65-66 and pp. 76-80)

[21] Phillips' role at FLG also included selling directly to investors. Phillips had between 100 and 500 clients and his book of business by early November 2011 exceeded $100 million in assets under management. (Testimony of Phillips, June 19, 2013, pp. 106-115; Exhibit 19 -- Respondents' Hearing Brief, Tab 27; Testimony of Wilson, June 20, 2013, pp. 84-86)

ii. Wilson

[22] Wilson first heard about FLG as an investor in 1991 when he was a founding investor in Wimberly Apartments Limited Partnership ("**WALP**"), a FLG entity. Wilson has known Phillips since 1991 and described himself and Phillips as good friends who socialized together from time to

time. Wilson joined FL Securities in November 2002, having previously spent 26 years as salesperson of a company in the United States selling industrial machinery. (Testimony of Wilson, May 15, 2012, pp. 86-87; Exhibit 13 -- Phillips and Wilson Transcripts, Tab B, pp. 24-25)

[23] Wilson was registered with the Commission as a trading officer and approved as a director of FL Securities from March 11, 2004 to December 31, 2004. Wilson also was registered with the Commission as a salesperson or dealing representative with FLSI from April 12, 2005 to February 24, 2012, which permitted him to offer wealth management services to clients of FLG. Wilson also was approved as an officer and director of FLSI from March 29, 2011 to February 24, 2012. (Testimony of Wilson, June 20, 2013, pp. 62-63; Exhibit 4 -- Hearing Brief: Corporate Registration Documents, Tab 11)

[24] In early 2011, Wilson was an investment advisor with FLSI and a director of FLSI, FLWM and 960510 Ontario Inc., WALP's general partner. During the Sales Period, Wilson's title was Vice President, Sales of FLSI, but he and Phillips described Wilson's role as that of the Director of Investor Relations since Wilson helped to coordinate communications to investors. (Testimony of Wilson, June 20, 2013, pp. 62-64, 82, 84 and 92-93; Exhibit 4 -- Hearing Brief: Corporate and Registration Documents, Tab 9; Testimony of Krieger, June 5, 2013, p. 108; Testimony of Phillips, June 19, 2013, p. 9; Testimony of Wilson, June 20, 2013, p. 64; Exhibit 1 -- Grant Thornton Report, p. 23)

[25] Wilson was a senior salesperson with FLG who described himself as "an old salesman, an old customer guy" who "very much enjoyed working directly with people". As per his request, Wilson did not have anyone reporting to him and he did not have authority over the other salespeople. Wilson found that in management, "you got further and further away from the customer…." Wilson worked closely with and reported directly to Phillips along with all sales staff at FLG. However, he oversaw a sales team of 6 investment advisors and 19 sales associates. (Testimony of Phillips, June 19, 2013, pp.112-115; Testimony of Wilson, June 20, 2013, pp. 84-87; Exhibit 13 -- Phillips and Wilson Transcripts, Tab B, pp. 24-25; Exhibit 1 -- Grant Thornton Report, p. 23)

[26] As of August 19, 2011, Wilson had raised the most capital within the FL Group. As of early November 2011, Wilson had more than 100 clients and his book of business was in excess of $100 million. (Testimony of Phillips, June 19, 2013, pp. 112-115; Testimony of Wilson, June 20, 2013, pp. 84-86; Exhibit 1 -- Grant Thornton Report, p. 23)

[27] Wilson had invested in excess of $2 million in FLG. His FLG portfolio included approximately $1 million in cash that he put into FLG over time and more than half were units that he received as compensation (including bonuses) in lieu of an amount of cash that he earned while working at FLG since 2002, including certain bonuses. (Testimony of Wilson, June 20, 2013, p. 63)

D. THE ALLEGATIONS

[28] In the Amended Statement of Allegations, Staff alleges that during the period between August 22 and October 28, 2011 (the "**Sales Period**"), Phillips directed and oversaw sales of offerings of equity and debt securities in the First Leaside Group ("**FLG**") which raised about $18.76 million from investors (the "**FLG Sales Investors**"), with Phillips having sold about $3.38

million directly to FLG Sales Investors and Wilson having sold about $8.95 million directly to FLG Sales Investors.

[29] Staff alleges that Phillips and Wilson effected these sales of FLG securities to FLG Sales Investors despite knowing that an independent accounting firm, Grant Thornton Limited ("**Grant Thornton**"), had conducted an extensive six-month review of FLG and had delivered a report to them on and dated August 19, 2011 (the "**Grant Thornton Report**"), which included findings that the future viability of FLG was contingent on its ability to raise new capital and that there was a significant equity deficit.

[30] Staff alleges that the fact that Grant Thornton was reviewing FLG, the existence of the Grant Thornton Report and the contents of Grant Thornton Report were important facts FLG Sales Investors should have known. Staff alleges that, during the Sales Period, Phillips did not disclose these important facts to FLG salespeople, and Phillips and Wilson did not disclose them to FLG Sales Investors to whom they directly sold FLG securities. Staff alleges that by concealing these important facts while selling FLG securities to FLG Sales Investors, and in Phillips' case, supervising the entire sales effort, Phillips and Wilson dishonestly placed FLG Sales Investors' pecuniary interests at risk.

[31] Staff further alleges that, as registrants, each of Phillips and Wilson had an obligation to deal honestly, fairly and in good faith with their clients. In supervising and conducting sales in the circumstances described, Phillips failed to discharge this obligation. In conducting sales in the circumstances described, Wilson failed to discharge this obligation.

[32] Specifically, Staff alleges that each of Phillips and Wilson:

a. directly or indirectly engaged or participated in an act, practice or course of conduct relating to securities which he knew, or reasonably ought to have known, would perpetrate a fraud on FLG Sales Investors, contrary to subsection 126.1(b) of the Act;

b. made statements a reasonable investor would consider relevant in deciding whether to enter into or maintain a trading or advising relationship, which statements were untrue or omitted information necessary to prevent the statements from being false or misleading in the circumstances in which they were made, contrary to subsection 44(2) of the Act;

c. failed to deal fairly, honestly and in good faith with their clients, contrary to section 2.1 of Commission Rule 31-505; and

d. engaged in conduct contrary to the public interest and harmful to the integrity of the capital markets.

E. OVERVIEW OF FIRST LEASIDE GROUP, BUSINESS AND OPERATIONS

i. The First Leaside Group of Companies

[33] FLG was founded in the late 1980's by Phillips. The FLG office was at Phillips' residence address, 430 Durham Road 8 in Uxbridge, Ontario ("**Phillip's Residence**"). (Exhibit 1 -- Grant Thornton Report, p. 15; Testimony of Phillips, June 19, 2013, p. 96; Exhibit 4 -- Hearing Brief:

Corporate and Registration Documents, Tabs 1, 2, 3 and 4)

[34] FLG offered a variety of investment opportunities, including (i) full brokerage and financial planning services administered by Penson Financial Services Canada Inc.; and (ii) higher risk securities with debt and equity offerings invested directly or indirectly within FLG. The type of products offered included limited partnership ("**LP**") units, trust units, mortgages and corporate preferred shares. In addition, FLEX LP (as defined in [40] below) conducted a $5 million offering of subordinated debentures. (Exhibit 1 -- Grant Thornton Report, p. 15)

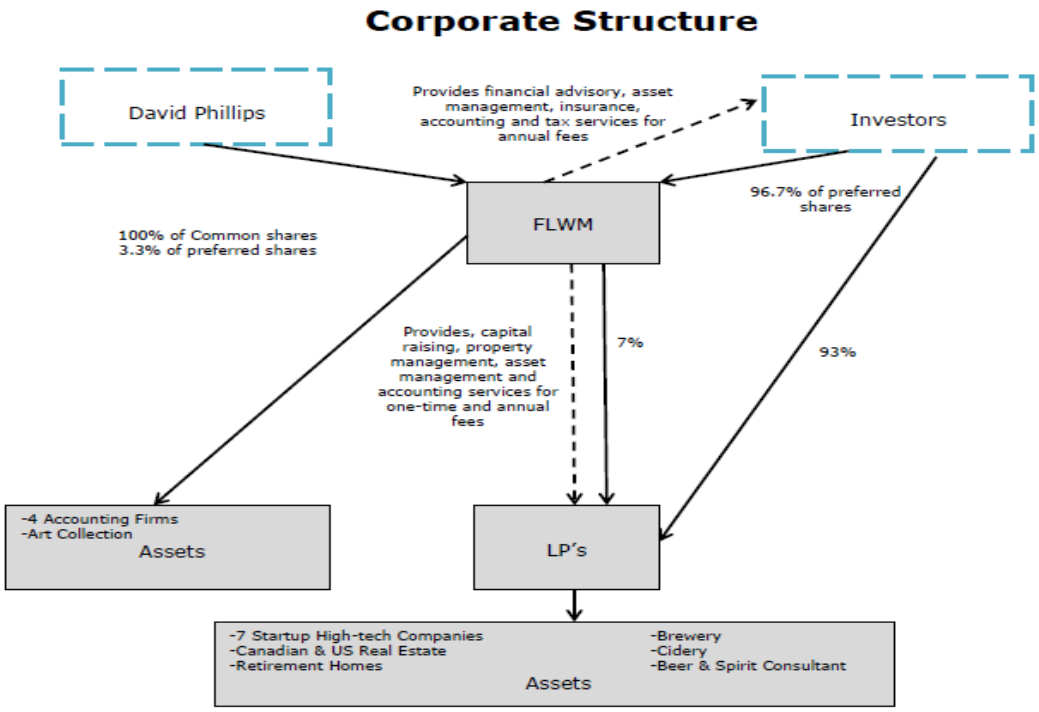
[35] FLG raised debt and equity and pursued investments with the objective of providing its investors with monthly distributions, potential capital appreciation, and in the case of equity investments, potential tax deductions. FLG also offered its investors wealth management, estate planning, insurance, accounting and tax services through a number of different entities. (Exhibit 1 -- Grant Thornton Report, p. 15)

ii. FLG Limited Partnerships and Companies

[36] FLG started raising LP capital and advising investors in 1988. The Grant Thornton Report identified that FLG initially raised $10 million and acquired two Texas properties (Pointe and Crossing), which as of August 2011, still formed part of the WALP portfolio. LP units were initially priced at $1 per unit and the majority of the investments had distribution rates ranging from 4% to 10%, which typically were paid to investors on a monthly basis. (Exhibit 1 -- Grant Thornton Report, p. 15)

[37] Each year, FLG formed a Canadian Limited Partnership ("**Canadian LP**") and a U.S. Limited Partnership ("**US LP**") to acquire and own real estate and to provide tax write-off opportunities. Each LP held different assets. By August 2011, FLG was a complex corporate structure comprised of about 161 LPs and companies. There were significant interrelationships between the entities. (Testimony of Krieger, June 5, 2013, pp. 107-126; Exhibit 6 -- Affidavit of Stephanie Collins sworn October 26, 2011, para. 12)

[38] The following chart depicts the corporate structure of FLG:



(Exhibit 1 -- Grant Thornton Report, p. 23)

[39] By August 2011, FLG managed several of the limited partnerships including FLWM, First Leaside Expansion Limited Partnership ("**FLEX LP**"), WALP, First Leaside Global Limited Partnership ("**Global LP**"), First Leaside Venture Limited Partnership ("**Venture LP**") and First Leaside Realty & Realty II Limited Partnerships ("**Realty I & II LPs**"), First Leaside Acquisitions Limited Partnership ("**Acquisitions LP**"), First Leaside Investors Limited Partnership ("**Investors LP**"), First Leaside Progressive Limited Partnership ("**Progressive LP**"), First Leaside Universal Limited Partnership ("**Universal LP**"), First Leaside Spring Valley Limited Partnership ("**Spring Valley LP**"), FLWM Holding Limited Partnership ("**FLWM Holdings LP**"), First Leaside Select Limited Partnership ("**FL Select LP**"), First Leaside Elite Limited Partnership ("**Elite LP**"), First Leaside Premier Limited Partnership ("**Premier LP**"), First Leaside Ultimate Limited Partnership ("**Ultimate LP**"), First Leaside Visions I & II Limited Partnership ("**Visions I & II LPs**") and First Leaside Mortgage Fund ("**Mortgage Fund**"). (Exhibit 1 -- Grant Thornton Report, pp. 24-28)

[40] LPs and other investment entities within FLG collectively allowed investors to place their capital, directly or indirectly, in certain assets, including, among other things, multi-unit residential properties in Canada and the United States, retirement homes in the provinces of Ontario and British Columbia, raw land with development potential throughout Southern Ontario, four small accounting firms in Western Canada, a cider and brewery in Southern Ontario, a liquor consulting business and high tech companies, which were eligible to receive government grants. (Exhibit 1 -- Grant Thornton Report, p. 15)

[41] Several FLG entities, particularly FLWM, FL Finance, FL Securities and several LPs, along with investors external to FLG, owned units in other FLG LPs and FLG funds.

[42] Certain LPs, particularly WALP, became a drain on the resources in the FLG organization because of recurring operating losses and property rehabilitation costs. (Testimony of Krieger, June 5, 2013, pp. 111-113; Exhibit 1 -- Grant Thornton Report, Organizational Chart at Appendix "B", p. 79 (right side); Exhibit 1 -- Grant Thornton Report, pp. 17 and 29)

[43] By August 2011, FLG had approximately $370 million of assets under management ("**AUM**"), invested in 39 properties and/or investments through 19 LPs. The AUM were divided amongst those associated with real estate (the "**Real Estate Assets**") and non-Real Estate Assets (the "**Admin Assets**"). The majority of FLG Investors had multiple investments within FLG and the average investment was approximately $290,000 per investor in Real Estate Assets and $190,000 per investor in Admin Assets. (Exhibit 1 -- Grant Thornton Report, pp. 17 and 20; Testimony of Krieger, June 5, 2013, pp. 141-146)

FLWM

[44] FLWM is the de facto parent company and the main operating entity of FLG. Phillips owns 100 per cent of the common shares of FLWM. (Exhibit 1 -- Grant Thornton Report, p. 24)

[45] Within FLWM, there are seven operating companies that provided all of the advisory services for FLG. These seven operating companies are: FLSI, FL Securities, First Leaside Fund Management Inc. ("**FL Fund Management**"), First Leaside Accounting and Tax Services Inc. ("**FL Accounting**"), FL Finance, First Leaside Insurance Inc. ("**FL Insurance**") and First Leaside Management Inc. ("**FL Management**"). There were over 50 employees and 399 investors in FLWM.(Testimony of Krieger, June 5, 2013, p. 108; Testimony of Phillips, June 19, 2013, pp. 102-103; Exhibit 1 -- Grant Thornton Report, pp. 23-24 and p. 83)

[46] In 2011, equity was being raised in FLWM through the distribution of three series of preferred shares, paying annual dividends of 10%, 8% and 6% and debt was being raised through the First Leaside Wealth Management Trust Fund ("**FLWM Fund**"), which was paying interest at 7%. FLWM earned its revenue by charging fees of 17.5% on new equity capital raised, property management fees of 2% of net revenues and administration fees for accounting, tax and other services provided within FLG. FLWM debt and equity investments were characterized by FLG Management as having been designed to provide investors with consistent monthly distributions, potential capital appreciation and in the case of equity investments, potential tax deductions. (Testimony of Krieger, June 5, 2013, pp. 126-128 and p. 131; Exhibit 1 -- Grant Thornton Report, p. 15, p. 18 and p. 24)

[47] By August 2011, FLWM owned the following assets:

(i) approximately $13.4 million worth of units in various LPs and other assets within FLG;

(ii) 33.3% of First Leaside Retirement Residences Limited Partnership ("**FL Retirement LP**"), an LP that owns 51 % of a group of 8 retirement properties through Ontario and BC;

(iii) 34.9% of First Leaside Beverages Limited Partnership ("**Beverages LP**"), an entity that owns a cidery in Thornbury, King Brewery in King City and a beer and spirits consulting company called Beer Barons;

(iv) $2 million worth of art and paintings being held for FLG's new office premises in Uxbridge;

(v) $4.1 million in notes receivable from investors who had borrowed funds on a short term basis to acquire units in various LPs within FLG;

(vi) Joanna Hampton Holdings Limited, a company that owned 3 accounting firms in Western Canada;

(vii) Jim Brander Professional Corporation, an accounting firm in Western Canada; and

(viii) $1.6 million in marketable securities. (Exhibit 1 -- Grant Thornton Report, p. 81)

FLSI

[48] FLSI is an Ontario corporation which was incorporated on February 17, 1999. FLSI's registered address is Phillip's Residence. FLSI was registered as an investment dealer under the Act from March 1, 2004 to February 24, 2012. FLSI's registration was suspended on February 24, 2012 due to the suspension of FLSI's membership with IIROC. FLSI charged agency fees, business development fees and acquisition analysis fees. (Exhibit 1 -- Grant Thornton Report, p. 24; Exhibit 4 -- Hearing Brief: Corporate and Registration Documents, Tab 1 and 15; Exhibit 6 -- Affidavit of Stephanie Collins sworn October 28, 2011, p. 6, para. 23)

[49] In 2004, FLSI became registered with the Investment Dealer Association (now IIROC) which allowed the FL Group to become a dealer member. The membership with IIROC allowed FL Group to offer full brokerage services through FLSI, which created a significant revenue source through FLWM and a greater opportunity to attract new investors seeking a more diversified portfolio. With the expansion of its potential investor pool, the FL Group began raising significant capital beginning in 2004. The FL Group's total AUM grew over 500% between 2004 – 2011 from $62M to $370M. (Exhibit 1 -- Grant Thornton Report, p. 62)

FL Securities

[50] FL Securities was incorporated on February 18, 1988 with its registered office address at Phillip's Residence. The President and UDP of FL Securities is Joanna Hampton ("**Hampton**"). (Exhibit 4 -- Hearing Brief: Corporate and Registration Documents Brief, Tab 2; Exhibit 21 -- Email chain with final email from Joanna Hampton to Ellen Bessner dated March 4, 2011; Exhibit 6 -- Affidavit of Stephanie Collins sworn October 28, 2014, pp. 7-8, paras. 26-28)

[51] FL Securities became registered as an exempt market dealer ("**EMD**") with the Commission as of September 28, 2009. Prior to that date, FL Securities was registered as a limited market dealer from March 1, 1991. On September 28, 2009, with the implementation of National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*, the limited market dealer category was changed to the EMD category. The EMD registration of FL Securities was suspended by the Commission on February 28, 2012. FL Securities earns its revenues by charging promotional, acquisition analysis, property management and advisory fees. (Exhibit 1 -- Grant Thornton Report, pp. 15, 24 and p. 86; Exhibit 4 -- Hearing Brief: Corporate and Registration Documents, Tab 6; Exhibit 20 -- Document titled "Welcome to the 2nd Flex Annual General Meeting" dated June 4, 2011; Exhibit 6 -- Affidavit of Stephanie Collins sworn October 28, 2011, p. 7, para. 25)

FL Fund Management

[52] FL Fund Management is described as the investment fund manager within FLG and represented that it was registered with the Commission as an investment fund manager, although no evidence of such registration was provided to the Panel. FL Fund Management provided fund management services to entities of FLG that issued securities to the public and charged fees to all Canadian properties equal to 2% to 4% of net revenues. (Exhibit 1 -- Grant Thornton Report, pp. 24 and 83; Exhibit 17 -- Hearing Brief: HZ and BZ, Tab 4)

FL Accounting

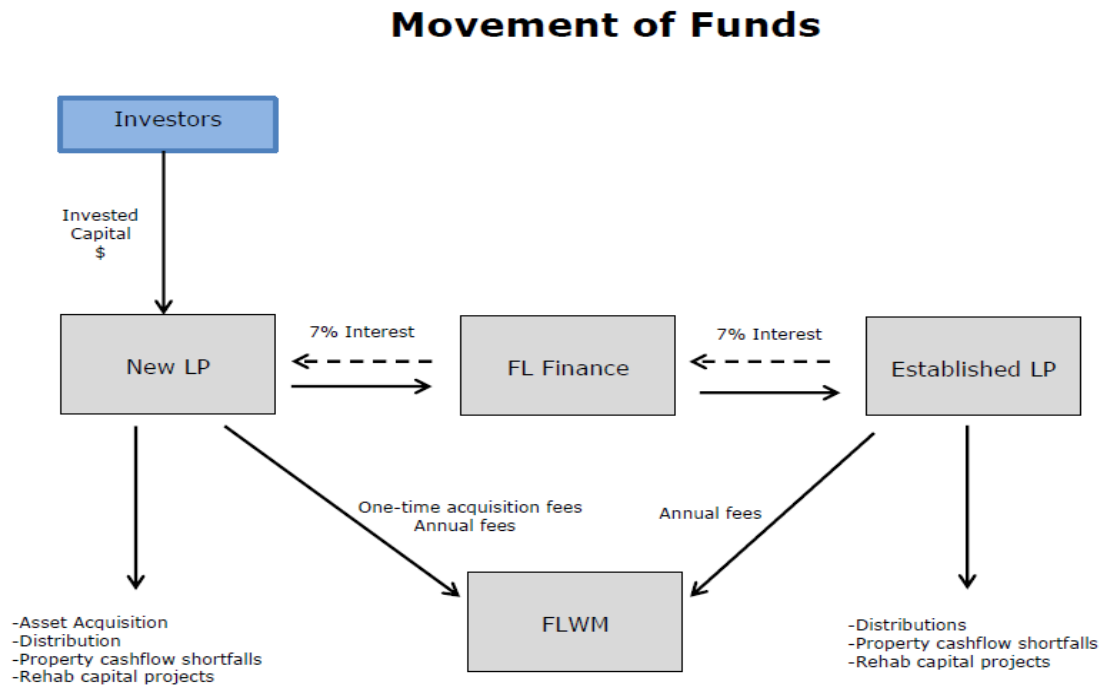
[53] FL Accounting provides accounting and income tax advisory services for Canadian and US personal and corporate needs. Hampton is the President of FL Accounting and oversees a staff of four accountants. (Exhibit 1 -- Grant Thornton Report, pp. 23-24 and p. 66)

FL Finance

[54] FL Finance acts as the central bank within FLG. Most related party transactions are recorded through FL Finance and all purchases of units from investors are financed through this entity. (Exhibit 1 -- Grant Thornton Report, p. 24)

[55] Prior to the review of FLG by Grant Thornton and the release of the Grant Thornton Report, the business of FLG was conducted such that LPs within the FLG organization would often raise more capital than required for a specific project, or raised capital without an identified acquisition or a specific use of proceeds. This resulted in idle cash in the bank account of a respective LP that generated an immaterial amount of interest, while the LP was still obligated to pay the requisite distributions to unit holders. The FLG LP would subsequently lend its idle cash to FL Finance on commercial terms. FL Finance would then lend the cash to another LP in FLG that had an immediate cash flow requirement to fund distributions, property cash flow shortfalls or property rehabilitation costs. Loan agreements were prepared and signed between FL Finance and the lending LP, at an agreed upon interest rate of 7% annually, and subject to a guarantee from FLWM. (Testimony of Krieger, June 5, 2013, pp. 146-151; Testimony of Krieger, June 6, 2013, pp. 60-61; Exhibit 1 -- Grant Thornton Report, p. 31)

[56] The movement of funds between FL Finance and other FLG LPs within the FLG organization is depicted through the following diagram from the Grant Thornton Report:



(Exhibit 1 -- Grant Thornton Report, p. 31)

[57] It was noted in the Grant Thornton Report that significant funds have been loaned between FLG entities through FL Finance on commercial terms, which allowed FLG [and FLWM] to operate perpetually as a going concern, as FLG has generally had access to capital to meet cash flow shortfalls, albeit using new investor money in some cases. (Exhibit 1 -- Grant Thornton Report, p. 9)

[58] By August 2011, the practice of lending funds from one LP to another through FL Finance resulted in a cash flow shortfall within FLG. LPs that had lent money to FL Finance were required to pay interest or distributions to their investors, but the entities that had received the funds from FL Finance, including WALP, which borrowed the majority of the money lent by FL Finance, did not have the cash flow to pay interest to FL Finance. (Testimony of Krieger, June 5, 2013, pp. 151-155; Exhibit 1 -- Grant Thornton Report, pp. 30-32) The balance sheets for each LP and FLWM revealed that the majority of funds lent to FL Finance by certain LPs ("**Lending LPs**") were lent, in turn, by FL Finance to WALP to fund the property rehabilitation costs and operating losses of WALP. However, the funding of losses and property rehabilitation programs would have a negative short term cash flow impact on FLG because FL Finance had to pay 7% interest to the Lending LPs (to cover their interest fund distribution payments) while FL Finance would not receive the 7% interest from the borrowing LP (WALP) if the borrowed money is being used to fund operating losses and property rehabilitation programs that are not yet generating income. Accordingly, the related party balance owing to FL Finance from the borrowing LP would continue to grow with accruing interest on the books of FL Finance.

[59] The FL Finance balance sheet as at December 31, 2010 showed it had borrowed $27.9 million from within FLG, lent $10.2 million to certain LPs, and acquired $11.7 million in LP units

(through investor redemptions at face value of $1.00 per unit for investors who sold their investments back to FLG). By August 2011, FL Finance did not have sufficient liquid assets to pay back the $27.9 million in outstanding loans to the other LPs within FLG from which FL Finance had borrowed the funds. Notwithstanding this fact, as of August 2011, each of FLWM, FLEX LP, WALP, Global LP, Venture LP and First Leaside Mortgage Trust ("**FL Mortgage**") were continuing to raise capital. (Testimony of Krieger, June 5, 2013, pp. 151-155; Exhibit 1 -- Grant Thornton Report, p. 16 and pp. 30-32)

FL Insurance

[60] In August 2010, FL Insurance was incorporated and is a licensed life insurance agency in Ontario. FL Insurance offered services with respect to life, health and accident insurance to investors within FLG. (Exhibit 1 -- Grant Thornton Report, p. 18, p. 24 and p. 83)

iii. The FLG Investment Model and Flow of Funds

[61] The Grant Thornton Report disclosed that FLG Management (as defined in [80] below) targeted a total return on investments ("**ROI**") between 12% to 15% and that FLG Management forecast that investors would begin to realize on their capital appreciation within five years. In order to meet this investment objective, FLG pursued properties that required significant tax deductible expenditures at the initial stage and properties that FLG Management believed would have distinct upside potential in the future (the "**Investment Model**"). (Exhibit 1 -- Grant Thornton Report, p. 18)

[62] The Investment Model required that an LP in the FLG organization raise capital prior to the identification of a property or assets for acquisition by the LP. The strategy was such that the LP would invest in assets in the first or second year of the LP's existence. (Testimony of Chien, June 10, 2013, pp. 66-69)

[63] Certain LPs within the FLG organization were described as blind pools since they did not own any assets at the outset of raising funds, but sought investment opportunities at some point in the future. In certain instances, LPs within the FLG organization raised more capital than was required at the time. In order to mitigate the cost of having excess cash earning a nominal return in the respective LP, the LP would lend the idle cash to another FLG entity until the LP that originally raised the funds required access to the capital. These loans between LPs were facilitated through FL Finance, and were subject to written agreements setting out commercial terms, and supported by a guarantee from FLWM. LPs that did not acquire assets were merged with another FLG entity such as WALP or FLEX LP. (Testimony of Chien, June 10, 2013, pp. 66-69; Testimony of Phillips, June 19, 2013, p. 116; Exhibit 1 -- Grant Thornton Report, p. 18)

[64] The sources of payments of distributions or interest to FLG Investors (as defined below) who had invested in an LP within the FLG organization came from cash flow from properties or investments, loan repayments from related parties, bank financing or mortgages, and interest on promissory notes. (Testimony of Krieger, June 5, 2013, pp. 119-120; Exhibit 1 -- Grant Thornton Report, Organizational Chart at Appendix "B", p. 82 (right side))

iv. Key Investment Vehicles

WALP

[65] WALP was established in July 1992 and is considered the U.S. real estate LP within the FLG organization. WALP was created to consolidate FLG's Texas real estate holdings. WALP has a portfolio which holds properties in Texas, including 11 different apartment complexes. WALP owns the F.L. Master Texas Ltd., ("**Master Texas**"), F.L. Master Sherman Ltd. ("**Master Sherman**") and F.L. Sedona Creek Ltd. ("**Sedona**") which own multi-unit residential buildings are located in Texas. Master Texas owns six Limited Partnerships that each owns one apartment complex in the Dallas/Ft. Worth area. Master Sherman owns four LPs that each owns one apartment complex in the Sherman, Texas area. Sedona owns an apartment complex in the Dallas area. (Testimony of Krieger, June 5, 2013, pp. 124-126; Exhibit 1 -- Grant Thornton Report, pp. 25-26 and Organizational Chart at Appendix "B", p. 85)

[66] As at June 30, 2011, WALP had 226 investors and had raised $46.77 million. Equity was raised directly by WALP, which paid annual distributions of 4% as return of capital. Debt was raised by WALP for the Master Texas properties through First Leaside Fund ("**FL Fund**"), First Leaside Properties Fund ("**FL Properties Fund**") and Wimberly Fund in order to facilitate the ongoing cash requirements for certain properties. (Exhibit 1 -- Grant Thornton Report, pp. 94-96)

[67] FL Fund was opened to investment in 2005. As at June 30, 2011, FL Fund had raised $43.3 million in debt with an annual interest rate of 9%. FL Fund debt instruments had maturity dates varying from 2015 to 2019, with an option to extend or renew for an additional 10 years at the discretion of Master Texas. (Exhibit 1 -- Grant Thornton Report, p. 96)

[68] Wimberly Fund was opened to investment in 2010 and had raised $9.3 million in debt bearing an annual interest rate of 8% and an additional $1.2 million in debt bearing an annual interest rate of 7% as at June 30, 2011. Wimberly Fund debt instruments had maturities from 2019 to 2021 with an option to extend or renew for an additional 10 years at the discretion of WALP. (Exhibit 1 -- Grant Thornton Report, p. 96)

[69] The Grant Thornton Report disclosed that FLG Management intended to convert approximately $20 million of the $43 million in debt of FL Fund to equity in WALP, bearing a dividend yield of 4.375% in order to better position FLG "from a cash flow perspective as it will be able to reduce the distribution it pays to its unit holders". FLG Management was of the view that the opportunity to earn distributions in the form of return of capital would compensate for the reduction of yield as the after-tax benefit would be attractive to investors in the highest income tax bracket. (Exhibit 1 -- Grant Thornton Report, p. 96)

FLEX LP

[70] FLEX LP is a Canadian real estate LP in the FLG organization. FLEX LP is an open fund that is considered the Canadian real estate fund for FLG. FLEX LP began raising capital in 2005 and has 262 investors. FLEX LP raised funds from investors in two different ways: (i) Equity units, which provided for a dividend at a yield that had recently been changed from 7.5% per year to 6% per year, as was announced at the Annual General Meeting of FLEX LP held on June 4, 2012 ("**FLEX AGM**"); and (ii) Debt, which provided for interest at a rate of 7.75% per year, was raised from investors, through notes issued to investors by Development Notes LP ("**Development**

Notes") and the money is then lent by Development Notes LP to FLEX LP at the same rate and amount, with a 30-month term.

[71] By August 2011, FLEX LP owned several LPs and real estate assets, including First Leaside Growth Limited Partnership ("**Growth LP"**), First Leaside Unity Limited Partnership ("**Unity LP**"), and First Leaside Entities Limited Partnership ("**Entities LP**").

[72] Growth LP held a fully tenanted 70,000 square feet industrial building located in Brampton, Ontario. Unity LP held 2.74 acres of land in Wheatley, Ontario, zoned for a residential townhome complex with plans for 16 townhomes, for which construction was planned for 2012. Entities LP owned two properties in downtown Uxbridge: (i) a 1.57 acre property, used as a parking lot for the construction workers who were engaged in constructing nearby office buildings for FLEX LP; and (ii) a 0.59 acre parcel of vacant land that was not producing income.

[73] FLEX LP also owned 100% of 1.04 acres of land in downtown Uxbridge, Ontario, which was being developed by FLG into a platinum LEED, 58,182 square feet, 4 floor office building (the "**Victoria St. Building**"), and which was planned to be FLG's head office, with FLWM to be the main occupant. As of the Grant Thornton Report, the total costs incurred for the property were approximately $5.13 million. The property was in the excavation stage of development and the foundations were expected to be poured in September 2011. The total cost of the Victoria St. Building was anticipated to be $31.5 million. The Grant Thornton Report disclosed that the Victoria St. Building was expected to be completed and occupied by FLWM in September 2012, with a projected Net Operating Income ("**NOI**") (after third party debt) of approximately $1.2 million. FLEX LP also owned Queenston Manor Limited Partnership ("**QM LP**"), a 77 unit retirement living apartment complex in St. Catharines, Ontario, which had an occupancy rate of 92%.

[74] In the summer of 2011, FLG Management closed FLEX LP and opened the FLEX Fund to investors, offering debt with interest at 6% per year and the option to re-invest the monthly interest payments so that interest accumulates and is compounded on a monthly basis and paid out when the investment matures.

[75] FLEX LP was projected to raise equity in the amounts of $11.5 million in 2011 and $5.5 million in 2012 as well as secure construction financing of $9 million in 2012 and an additional $3 million (refinanced into a mortgage) in 2013. As at June 30, 2011, FLEX LP had raised $12.4 million of debt at a 7.75% interest rate. FLG Management expected to convert three-quarters of the debt holders to equity in 2012 and the balance in 2013. As discussed in [71] above, the annual distributions on FLEX LP's equity were reduced from 7.5% to 6%, which was announced at the FLEX AGM.

Venture LP

[76] Venture LP was opened by FLG in 2011 and had raised $886,000 in equity as of June 30, 2011, paying distributions of 5% by way of return of capital. As of August 2011, Venture LP was in the advanced stage of negotiations to acquire three retirement home complexes in Ottawa called (i) The Palisades, (ii) The Palisades Condo Club and (iii) The Redwoods. Venture LP was projected to raise $14.4 million, $3.1 million and $2.16 million by sales of equity in the following three years, respectively. FLG Management anticipated that the purchase of the three Ottawa properties would close on August 26, 2011. (Exhibit 1 -- Grant Thornton Report, p. 28 and p. 48)

[77] FLG Management advised Grant Thornton that funds for Venture LP's acquisition of the three Ottawa properties would be raised from two sources:

> (i) PrimeTime Living LP would refinance three of its properties (Shores, Cherry Park & Orchard Valley) and would lend Venture $4.5 million (through FL Finance) by way of a Promissory Note with interest-only payments of 7% per year, which FLG Management expects would be repaid before the end of 2011; and
>
> (ii) Venture LP has arranged mortgage financing with CIBC in the amount of $40 million with an interest rate of 5.00% per year, amortized over 25 years, maturing in September 2016 as well as a vendor take-back ("**VTB**") mortgage financing in the amount of $17.5 million with Kingsett Capital Partners. The Grant Thornton Report stated that the majority of the cash deficiency is due to the VTB arrangements which require a principal payment at the end of each of the next three years of $4.4 million, and the balance of $4.3 million at the end of 2014. (Exhibit 1 -- Grant Thornton Report, p.117)

Special Notes LP

[78] The Special Notes Limited Partnership ("**Special Notes LP**") offered debt to investors by way of Special Notes that provide for interest at a rate of 10.1% per annum, payable monthly and are callable after 30 months. Special Notes were offered to FLG investors along with Venture LP equity by group email to investors dated September 9, 2011 from Wilson ("**Wilson's Group Email**"). Wilson's Group Email about the Special Notes LP offering described its features and indicated that there was a limited supply and that he expected the Special Notes "to be fully subscribed rather quickly".

(Testimony of Wilson, June 20, 2013, pp. 107-110; Exhibit 7 -- Hearing Brief: Lists of Sales During Sales Period and Marketing Material, Tab 2; Submissions of Staff dated August 1, 2013, pp. 147-148, para. 429)

v. Key Personnel

[79] The senior management team of FLG ("**FLG Management**") included Phillips, Wilson, Joanna Hampton ("**Hampton**"), Director of Finance, Leon Efraim ("**Efraim**"), Corporate Counsel and Chief Compliance Officer and Joan Wilson, Director of Real Estate. (Testimony of Phillips, June 19, 2013, pp. 9-11)

[80] Hampton oversaw a staff of four accountants, and was the President of FL Accounting and Joan Wilson oversaw a team of two people and liaised with the third party property managers. Joan Wilson also reviewed and reported on all real estate acquisitions for the Company. Phillips' wife, Margaret Davis ("**Davis**"), was a director and the Secretary of FLWM, and the Vice-President and Treasurer of FL Finance.

(Testimony of Phillips, June 19, 2013, pp. 9-11; Exhibit 1 -- Grant Thornton Report, p. 21; Testimony of Krieger, June 5, 2013, pp. 156-157; Testimony of Phillips, June 19, 2013, pp. 7-8, p. 97 and p. 99; Exhibit 4 -- Hearing Brief: Corporate and Registration Documents, Tabs 1, 3, 4 and 9)

vi. The FLG Sales Teams

[81] The FLG sales teams consisted of three "tiers". Tier 1 employees "cold called" people in order to find leads. Tier 2 employees followed up on the cold call leads in order to book a meeting for a tier 3 salesperson. A tier 3 salesperson was a registered representative, who then met with individuals with the intention of getting them to invest with FLG. (Testimony of Chien, June 10, 2013, pp. 62-63)

[82] In 2011, there were six FLG sales teams led by Phillips, Wilson, Edmund Chien ("**Chien**") and three others (collectively the "**Senior Sales Team**").

[83] The Senior Sales Team worked in an open concept space on the second floor of a barn on the Uxbridge property at Phillips' Residence. Phillips worked out of his home, which was on the same property. Phillips' dedicated work space was the atrium, a glass structure with a fireplace on the main floor of the house. (Testimony of Chien, June 10, 2013, pp. 65-66, pp. 71-73 and p. 76; Testimony of Wilson, June 20, 2013, pp. 93-94)

[84] Phillips was at the top of the reporting structure within FLG. All of the tier 3 salespeople at FLSI reported to Phillips and Phillips signed off on trades for everyone who was selling in the FLG organization. (Testimony of Chien, June 10, 2013, pp. 65-66 and pp.76-80; Testimony of Phillips, June 19, 2013, p. 112 and pp. 114-115)

vii. FLG Investors

[85] The Grant Thornton Report disclosed that there were approximately 1,000 investors within FLG (the "**FLG Investors**"), the majority of whom were accredited investors with liquid assets in excess of $1 million. FLG Investors were characterized as middle-aged and older and primarily from Southern Ontario. They were primarily in the highest tax bracket for personal income taxes and were motivated to invest in tax-efficient instruments in order to reduce their personal income taxes while earning reasonable yield. FLG Investors were also seeking predictable distribution payments. Capital appreciation was a secondary investment objective of FLG Investors. Investments in FLG securities were presented to prospective clients as offering real estate income and, at the same time, providing tax relief or tax management. (Exhibit 1 -- Grant Thornton Report, p. 18; Testimony of Krieger, June 5, 2013, pp. 140-141; Testimony of Chien, June 10, 2013, p. 61 and pp. 80-81)

[86] Each accredited FLG Investor was required to invest a minimum of $25,000. Each non-accredited FLG investor was required to invest a minimum of $150,000 per investment. (Exhibit 1 -- Grant Thornton Report, p. 17; Testimony of Krieger, June 5, 2013, pp. 140-141)

[87] Directors and FLG Management were also heavily invested in different FLG investments. Some of the units held by FLG Management and directors were received as compensation and others were acquired by investing cash or obtaining a loan to finance their purchases of units. (Testimony of Collins, June 10, 2013, p. 42)

[88] On July 20, 2011, Leo De Bever ("**De Bever**"), a director of FLWM, made an investment of approximately $1 million and on July 25, 2011, John Cook ("**Cook**"), another director of FLWM, invested $250,000. These investments were made during the period when Grant Thornton was working on the review of FLG. On July 28, 2011, the spouse of De Bever made an investment

of $90,834 and on August 3, 2011, the spouse of Cook made an investment of $250,000. On October 17, 2011, Ian De Bever, a family member of De Bever, invested $96,000. (Testimony of Collins, June 10, 2013, pp. 40-41; Exhibit 7 -- Hearing Brief: Lists of Sales During Sales Period and Marketing Material, Tab 1)

F. THE INVESTIGATION OF FLG

i. The Investigation of FLG by Staff and the Grant Thornton Engagement

[89] On November 24, 2009, Staff commenced an investigation into FLG. Phillips was made aware of Staff's investigation when he was served with a summons from the Commission on or about March 16, 2010. (Exhibit 13 -- Phillips and Wilson Transcripts, Tab 16)

[90] Staff interviewed Phillips over a period of three days in September 2010, as part of the investigation. There were ongoing discussions between Staff and FLG Management, which started in the fall of 2010, with respect to FLG retaining an independent valuator to prepare valuations of the WALP properties. FLG provided Staff, in December 2010, with third party valuations for various properties, which FLG owned in Texas. These valuations raised concerns among Staff as to the financial viability of FLG.

[91] In March 2011, Staff requested that a viability study be carried out on FLG and Staff provided FLG Management with a short list of firms that Staff deemed suitable for the engagement. Grant Thornton was included on that list. On the advice of Peter Dunne ("**Dunne**"), a partner with the law firm of Cassels Brock & Blackwell LLP ("**Cassels Brock**"), counsel to Phillips and FLG, FLG Management selected Grant Thornton. (Testimony of Phillips, June 19, 2013, pp.11-12 and pp 22-23)

[92] Grant Thornton was engaged by Cassels Brock, on behalf of FLG, for the purpose of reviewing, reporting and making recommendations on the business, assets, affairs and operations of FLG and to assess the viability of FLG. By engagement letter dated March 5, 2011 (the "**Grant Thornton Engagement**"), Grant Thornton agreed to review, report and make recommendations on the business, assets, affairs and operations of FLG. Cassels Brock, Grant Thornton and Staff communicated regularly on the progress being made by Grant Thornton on the viability report. (Exhibit 1 -- Grant Thornton Report, pp. 3-4, pp. 77-78 and pp. 38-39; Exhibit 2 -- Affidavit of Stephanie Collins sworn May 23, 2012, p. 7 para. 20; Opening Statements of the Respondents dated June 5, 2013, pp. 3-5)

ii. The Phillips' Undertaking

[93] During the course of the Grant Thornton review, Staff, Dunne and Ellen Bessner, another partner of Cassels Brock, agreed that FLG could continue to raise funds during the period of that review. However, Staff requested that Phillips provide an undertaking so that it would be incumbent upon Phillips to ensure that there were no sales of certain FLG securities. On March 18, 2011, Phillips undertook as follows:

> As agreed with Staff of the Ontario Securities Commission ("Staff"), Grant Thornton LLP ("Grant Thornton") has been retained to conduct a viability review (the "Review"). During the Review, and for a one week period after the delivery

to Staff of the final report prepared by Grant Thornton as a result of the Review, David C. Phillips undertakes that no sale will be made to any investors of any debt or equity in Wimberly Apartments Limited Partnership ("WALP") nor any of its subsidiaries. This undertaking includes an agreement not to sell any units of WALP, Wimberly Fund or First Leaside Fund during the relevant time. (the **"Phillips' Undertaking"**)

(Exhibit 5 -- Hearing Brief: Correspondence and Notes, Undertaking of Phillips dated March 18, 2011, Tab 25; Opening Statements of the Respondents dated June 5, 2013, pp. 3-5)

2. THE FACTS

[94] There is no agreed statement of facts between the parties. However, the Respondents agree that they:

(i) were aware of the Grant Thornton Engagement;
(ii) received and reviewed the Grant Thornton Report;
(iii) sold approximately $18.76 million of securities of FLG entities to investors during the Sales Period; and
(iv) did not disclose to investors the fact of the Grant Thornton Engagement or the Grant Thornton Report.

(Opening Statements of the Respondents dated June 5, 2012, p. 2, para. 5 and p. 7)

3. THE ISSUES

[95] Staff's allegations raise the following issues for consideration:

(a) Did the Respondents, Phillips and Wilson, each directly or indirectly engage or participate in an act, practice or course of conduct relating to securities which they each knew, or reasonably ought to have known, would perpetrate a fraud on investors, contrary to subsection 126.1(b) of the Act;

(b) Did the Respondents, Phillips and Wilson, each make statements a reasonable investor would consider relevant in deciding whether to enter into or maintain a trading or advising relationship, which statements were untrue or omitted information necessary to prevent the statements from being false or misleading in the circumstances in which they were made, contrary to subsection 44(2) of the Act;

(c) Did the Respondents, Phillips and Wilson, each fail to deal fairly, honestly and in good faith with their clients, contrary to section 2.1 of Commission Rule 31-505; and

(d) Did the Respondents, Phillips and Wilson, each engage in conduct which was contrary to the public interest and harmful to the integrity of the capital markets.

4. THE STANDARD OF PROOF

[96] The standard of proof in this hearing is the civil standard of proof on a balance of probabilities. The Supreme Court of Canada has stated that the "...evidence must always be sufficiently clear, convincing and cogent to satisfy the balance of probabilities test". (*F.H. v. McDougall*, [2008] 3 S.C.R. 41 ("***McDougall***") at paras. 46 and 49) The Panel must scrutinize the relevant evidence with care in deciding whether it is more likely than not that the alleged event has occurred (*McDougall, supra* at para. 49).

5. THE EVIDENCE PRESENTED

A. Witnesses

[97] Staff called eight witnesses at the hearing: Jonathan Krieger ("**Krieger**"), a partner with Grant Thornton LLP and a Senior Vice-President of Grant Thornton; Stephanie Collins ("**Collins**"), a Senior Forensic Accountant with Staff; Chien, a salesperson formerly employed by FLSI; and five investor witnesses Mr. H., Mr. M., Dr. Z. and Mrs. Z. and Mrs. C.

[98] Each of Phillips and Wilson testified at the hearing. In addition, the Respondents called Douglas Hyatt ("**Hyatt**"), a member of the Boards of FLWM and 960510 Ontario Inc., the general partner of WALP (the "**WALP GP**"), and Dunne.

B. Krieger

[99] Krieger is a chartered accountant licensed in the Province of Ontario and is a chartered insolvency and restructuring practitioner. He is also a trustee in bankruptcy. He was admitted to the CA Institute in 1997 and became a CIRP in 2000 and a trustee in bankruptcy in 2001. At the time of the Merits Hearing, Krieger had been with Grant Thornton for approximately 19 years and had been trained at the firm. His area of expertise includes restructuring and insolvency which comprises a number of different areas but primarily viability reviews, financial reviews and formal restructuring.

[100] Grant Thornton LLP is a firm of chartered accountants in three primary areas of practice (i) auditing, (ii) tax and (iii) advising services. Its specialty fields include restructuring, forensic accounting, business risk services and corporate finance. (Testimony of Krieger, June 5, 2013, pp. 70-72)

[101] Krieger testified on June 5, 6 and 7, 2013. The Grant Thornton Report and Monitor's Report (as defined in [172] below were entered as exhibits in the Merits Hearing during the course of Krieger's testimony.

C. Collins

[102] Collins is a charted accountant who is a member of the Institute of Chartered Accountants in England and Wales and a member of the Institute of Chartered Accountants of Ontario. She has been a member of the Staff for more than 15 years. She was engaged in the investigation of FLG that preceded the Merits Hearing.

[103] Collins testified on June 7 and 10, 2013. Nine hearing briefs and certain other materials

were entered as exhibits in the Merits Hearing during the course of Collin's testimony.

D. Chien

[104] Chien was a leader of one of the six FLG sales teams and was one of the Senior Sales Team. Chien was also a tier 3 salesperson and ran the 90-day training program for registrants. Chien had approximately 200 clients and a book of business of approximately $37 million in assets under management. Aside from Phillips and Wilson, Chien had the next largest book of business. (Testimony of Chien, June 10, 2013, pp. 64-65 and pp. 115-117) Chien testified on June, 10, 2013. One document was entered as an exhibit in the Merits Hearing during the course of Chien's cross-examination.

E. Investor Witnesses

i. Mr. H.

[105] Mr. H. is a 66 year old retired pastry chef. Prior to investing with FLG, Mr. H. had invested primarily in mutual funds, which were investments that he funded by using the proceeds of real estate transactions and the sale of his bakery business. Mr. H.'s portfolio had grown to just over $1,000,000 before he was approached by FLG. Mr. H. considered himself to have a low risk tolerance. (Testimony of Mr. H., June 10, 2013, pp. 170-174)

[106] On September 6, 2011, Mr. H. and his wife Mrs. H., on their own behalf and on behalf of H. Co. (their company) made a number of investments, totalling $163,317 in FLG securities. Their investments are as follows:

Investor	Date of Purchase	First Leaside Product	Number of Units Purchased	Amounts of Purchase	Sales Person
Mrs. H.	September 7, 2011	FLEX Fund Class B	1,375	$1,375	Chien
Mrs. H.	September 7, 2011	FLEX Fund Class B	12,297	$12,297	Chien
Mrs. H.	September 7, 2011	FLEX Fund Class C	11,500	$11,500	Chien
Mr. H.	September 7, 2011	Flex Fund Class B	1,375	$1,375	Chien
Mr. H.	September 7, 2011	FLEX Fund Class B	18,770	$18,770	Chien
Mr. H.	September 7, 2011	FLEX Fund Class C	18,000	$18,000	Chien

H. Co.	September 13, 2011	Special Notes LP	100,000	$100,000	Chien
TOTAL			163,317	$163,317	

(Exhibit 15 -- Hearing Brief: EH, Tabs 22 23, 24, 25, 26, 28 and 32; Exhibit 14 -- Five-page spreadsheet titled "First Leaside Securities Inc. Trading Data", FLSI Trading Data for Mr. H., Mrs. H., and H. Co.)

[107] Confirmation notices and a certificate of LP units were sent to Mr. H., Mrs. H. and H. Co. shortly thereafter, and the transactions were reflected on their respective client statements for the various accounts provided at month's end. Although Mr. H. received an offering memorandum dated August 1, 2011 for FLEX Fund, Mr. H. did not receive any financial information about any of the LPs or FLG funds in which he invested, and he never received any financial statements. Mr. H. testified that Phillips had indicated, at the FLEX AGM in June 2011, that financial statements would be forthcoming. Mr. H. did not attend the WALP AGM in September 2011, and FLG did not provide him with the financial statements thereafter. (Testimony of Mr. H., June 11, 2013, pp. 38-40)

[108] Mr. H. testified that when he invested in FLG securities in September 2011: he did not understand that Grant Thornton had done a review and issued a report with respect to FLG; he had not heard anything about Grant Thornton being involved; no one at FLG had any discussions with him about Grant Thornton's involvement whatsoever prior to signing all the documents dated September 6, 2011; and he did not have the Grant Thornton Report. (Testimony of Mr. H., June 11, 2013, pp. 43-44)

[109] Mr. H. testified that no disclosure was provided to him about the Grant Thornton Report until November 7, 2011 and he "was overwhelmed" by the Grant Thornton Report after it was disclosed to FLG investors on November 7, 2011. Mr. H. testified that after receiving the Grant Thornton Report, he wanted to know the companies that he was actually invested in and he phoned the FLG office. (Testimony of Mr. H., June 11, 2013, p. 44 and p. 51)

ii. Mr. M.

[110] Mr. M. is a 75 year old industrial designer. His investment experience consists mostly of purchasing mutual funds and Canadian and American equities over the years. He considers himself relatively risk tolerant when it comes to his investments. At the time when Mr. M. became involved with FLG, he had financial assets totalling approximately $300,000, held at another brokerage firm, which included a registered retirement savings plan ("**RRSP**") valued at $230,000, a margin account holding some securities, and some cash. (Testimony of Mr. M., June 11, 2013, pp. 104-106)

[111] Mr. M. testified that he dealt primarily with Phillips from 2007 to 2011, that he attended the WALP AGM on September 17, 2011 where Phillips introduced a sales brochure on the Venture LP to Mr. M. and that he met with Phillips on September 27, 2011 to discuss an investment by Mr. M. in Venture LP. On October 25, 2011, Mr. M. bought 150,000 units of Venture LP with Phillips as the salesperson as follows:

Investor	Date of Purchase	First Leaside Product	Number of Units Purchased	Amount of Purchase	Salesperson
Mr. M.	October 25, 2011	Venture LP	150,000	$150,000	Phillips
TOTAL			150,000	$150,000	

(Testimony of Mr. M., June 11, 2013, pp. 123-124, pp. 131-133 and pp. 136-138; Exhibit 9 -- Hearing Brief: 45-106 Forms and Manual Payment Transmittal Forms Filed by Filing Date (Volume 2 of 2), Tab 60; Exhibit 11 -- Hearing Brief: Analysis of Sales During the Sales Period, Tabs 5, 10, 16 and 20)

[112] Mr. M. testified that prior to November 7, 2011 he had never heard of the review by Grant Thornton nor of the Grant Thornton Report and had never been given the Grant Thornton Report prior to his $150,000 investment in Venture LP. Mr. M. further testified that when he read the Grant Thornton Report after it was made available to FLG Investors on November 7, 2012, he had mixed feelings. He stated that he was "hoping that something could be done to have a going concern and save the company, but [he] was hopeful". Mr. M. testified that he was "angry" because "the Grant Thornton Report should have been published and that investors should have known about it long before the 7th of November". (Testimony of Mr. M., June 11, 2013, p. 152 and pp. 157-158)

iii. Mrs. C.

[113] Mrs. C. is a manager of customer service information systems with Air Canada. She is also a vice-president in a private software development company ("**C. Co.**"), which she owns with her husband, Mr. C. Mr. C. and Mrs. C. made their investment decisions together, and they both have moderate investment knowledge. Prior to investing with FLG, Mr. C. and Mrs. C. had an investment advisor and mainly held mutual funds. Mrs. C. has a very low risk tolerance, allocating about 80 percent to low risk investments, because she was self-employed and had no pension. Mrs. C. was saving for retirement and, therefore wanted a good, secure vehicle to increase her savings. (Testimony of Mrs. C., June 17, 2013, pp. 5-8)

[114] Mr. C. and Mrs. C. began dealing with FLG in 2003, after a FLG representative, Ermo Ou ("**Ou**"), contacted Mr. C. about the investment vehicles that FLG offered for small businesses in order to reduce the tax burden. Mr. C. made an investment in Spring Valley LP, for approximately $50,000. (Testimony of Mrs. C., June 17, 2013, pp. 8-9) In 2008, Ou left FLG, and Phillips became advisor to Mr. C. and Mrs. C. Since Ou left FLG, they have only dealt with Phillips. Mrs. C. brought her elderly parents to meet Phillips, and they became FLG clients around 2008. (Testimony of Mrs. C., June 17, 2013, p. 9 and pp. 20-21; Testimony of Phillips, June 20, 2013, pp. 40-41)

[115] Phillips met Mrs. C. and Mr. C. for dinner on September 6, 2011 and over the course of two to three hours discussed FLG's plans and FLG investment opportunities. In addition, Mrs. C. and Mr. C. attended the WALP AGM (as defined in [164] below) on September 17, 2011. Phillips did not disclose the Grant Thornton Report to Mrs. C. or Mr. C. on September 6 or September 17, 2011 nor did Phillips disclose that there was any concern about the future viability of FLG. Shortly

after in September, 2011, Mrs. C. invested $250,000, which she understood would be used by FLG to assist FLG in FLG's purchase of a controlling interest in PrimeTime Living LP. This investment was combined with other cash in the C. Co. account for a total investment of $283,700. Mrs. C. received the FLEX Fund offering memorandum prior to making these investments, however, no other offering memorandum or marketing materials and no financial statements were provided to Mrs. C, Mr. C. or C. Co. prior to making the investment. Subscription agreements were signed for the purchase of Special Notes LP on September 17, 2011. Subsequently, a confirmation and certificate dated September 23, 2011 was sent to C. Co. indicating its registered ownership of 283,700 LP units in the Special Notes LP. (Testimony of Mrs. C., June 17, 2013, pp. 19-20, pp. 32-33 and pp. 37-39; Exhibit 18 -- Hearing Brief: VC, Tabs 2, 5, 18 and 19)

[116] In addition, Mrs. C., Mr. C. and C. Co. made a number of other investments during the Sales Period, "repurposing" proceeds of $95,784 from other FLG investments to investments in FLEX Fund Class B units in order to maximize their tax benefits. The investments made by Mr. C., Mrs. C. and C. Co. in FLG products during the Sales Period are as follows:

Investor	**Date of Purchase**	**First Leaside Product**	**Number of Units Purchased**	**Amount of Purchase**	**Salesperson**
Mrs. C. RRSP	Sept 20, 2011	FLEX Fund Class B	26,150	$26,150	Phillips
Mrs. C. Spousal RRSP	Sept 20, 2011	FLEX Fund Class B	12,171	$12,171	Phillips
Mrs. C. TFSA	Sept 20, 2011	FLEX Fund Class B	1,307	$1,307	Phillips
Mr. C. RRSP	Sept 20, 2011	FLEX Fund Class B	54,849	$54,849	Phillips
Mr. C. TFSA	Sept 20, 2011	FLEX Fund Class B	1,307	$1,307	Phillips
C. Co.	Sept 23, 2011	Special Notes LP	283,700	$283,700	Phillips
TOTAL			379,484	$379,484	

(Testimony of Mrs. C., June 17, 2013, pp. 11-18 and pp. 30-33; Exhibit 18 -- Hearing Brief: VC, Tabs 2, 4, 6, 8, 9, 13 and 14)

[117] Mrs. C. testified that she first learned about the Grant Thornton Report in the beginning of November, 2011. Mrs. C. testified that she received a letter dated November 7, 2011 from FLG (Exhibit 18 -- Hearing Brief: Mrs. C., Tab 24) and the Grant Thornton Report was posted on the FLG website. (Testimony of Mrs. C., June 17, 2013, pp. 39-40) Upon receiving the Grant Thornton Report, Mrs. C. was concerned because she had "no idea that things were as serious as they were indicated in this letter." Mrs. C. testified that she was shocked to read the statement "The future viability of the FL Group is contingent on their ability to raise new capital". She further testified:

> "The future viability of FL Group…" seemed to us to be a huge jump from "We have some challenges with WALP" to now the entire group was threatened.

(Testimony of Mrs. C., June 17, 2013, pp. 40-41)

[118] Mrs. C. testified that after reading the Grant Thornton Report, she and Mr. C. were "horrified". Mrs. C. testified "we had no idea. We thought that all of the assets were far more siloed than, in fact, they appeared to be. So our risk tolerance for about 10 percent of WALP was non-existent. We were exposed to a high, a much higher risk in that funds that we'd invested were propping up WALP. So we were horrified. I was also horrified because I had encouraged friends and family to participate in First Leaside, so it was pretty devastating." (Testimony of Mrs. C., June 17, 2013, p. 42)

iv. Dr. Z. and Mrs. Z.

[119] Dr. Z. is a 51 year old chiropractor and his wife, Mrs. Z., is a 48 year old "medical aesthetician." They both reside in Newmarket. Dr. Z. and Mrs. Z. have been married for 25 years. Dr. Z. met both Phillips and Wilson, initially as patients of Dr. Z. Dr. Z. first met Phillips in 2007 when Phillips was referred to Dr. Z. as a patient. Phillips continued as a patient until 2009. Dr. Z. saw Wilson as a patient, on average one appointment every three weeks, from 2007 to 2011.

[120] When Phillips came to see Dr. Z. for appointments, he would give Dr. Z. information about FLG, including the number of investors they had and the amount of money that FLG was managing. Over time, Dr. Z. eventually decided to move his RRSP to FLG. Prior to investing with FLG, Dr. Z. held mutual funds with Dundee Wealth Management for many years. His portfolio also contained mostly Canadian equity and a cash account. Dr. Z. thought that his portfolio was not doing much and that it had reached a point where he thought that his financial advisor was doing as much as he could, but "it [was not] really going anywhere." (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 6) Dr. Z. and Mrs. Z. transferred $380,000 "near to the end of 2007", which was the entire amount of their RRSP to FLG. (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 17)

[121] Dr. Z. described himself as having "low to medium investment knowledge" and Mrs. Z describes her investment knowledge as "limited to low." (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, pp. 8, 11)

[122] During the Sales Period, Dr. Z. and Mrs. Z. had meetings with Wilson who solicited new investments and reinvestments by them in FLG securities. Dr. Z. signed documents, with Wilson, to invest $100,000 in the Special Notes LP. On September 7, 2011, Dr. Z. deposited approximately $100,000 from his bank account into his FLG account. Dr. Z. received a certificate dated September 9, 2011 indicating he was the registered owner of 100,000 LP units in the Special Notes LP. (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, pp. 38-39 and pp. 46-47; Exhibit 17 -- Hearing Brief: HZ and BZ, Tabs 3 and 9)

[123] On September 9, 2011, Dr. Z. also purchased, through Wilson, $3,341.78 of FLEX Fund Class C, and Mrs. Z. purchased $9,643 of FLEX Fund Class C, both in their RRSPs, for a total of $12,984.78.

[124] On October 13, 2011, Dr. Z. purchased $210,000 of FLEX LP, and Mrs. Z. purchased $105,000 of FLEX LP, both outside their RRSPs, for a total of $315,000, which they rolled over from their previous investments in another FLG security. The investments were made through Wilson. The source of funds was the maturity of Development Notes, which they had held for

some time and which were maturing. The investments made by Dr. Z. and Mrs. Z. in FLG products during the Sales Period are as follows:

Investor	Date of Purchase	First Leaside Product	Number of Units Purchased	Amount of Purchase	Salesperson
Dr. Z.	September 9, 2011	Special Notes Limited Partnership Units	100,000	$100,000	Wilson
Dr. Z.	October 13, 2011	FL Expansion Limited Partnership Units	210,000	$210,000	Wilson
Mrs. Z.	October 13, 2011	FL Expansion Limited Partnership Units	105, 000	$105, 000	Wilson
Dr. Z.	September 9, 2011	Flex Fund Class B and C Units	9,560	$9,560	Wilson
Mrs. Z.	September 9, 2011	Flex Fund Class B and C Units	3,313	$3,313	Wilson
Mrs. Z.	October 13, 2011	FLEX LP	105,000	$105,000	Wilson
Mrs. Z. (Penson ITF)	September 9, 2011	FLEX LP Class C	9,560	$9,560	Wilson
Dr. Z.	September 9, 2011	Special Notes	100,000	$100,000	Wilson
Dr. Z.	October 13, 2011	FLEX LP	210,000	$210,000	Wilson
Dr. Z. (Penson ITF)	September 9, 2011	FLEX Fund Class C	3,313	$3,313	Wilson
TOTAL			855,746	$855,746	

(Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 48; Exhibit 17 -- Hearing Brief: HZ and BZ, Tabs 8, 10, 12 and 17)

[125] Dr. Z. testified that he did not receive a copy of the Grant Thornton Report prior to November 7, 2011 and he had an "awful" reaction to the Grant Thornton Report after it was released. Dr. Z. testified that when he read the Grant Thornton Report two points stuck out in his mind (i) he didn't know "how a company can run a business when they can't produce a financial statement when they needed to"; and (ii) FLG needed money, more new money to keep going to fund projects that he did not even know what he was invested in. Dr. Z. testified that he concluded that FLG was not a viable company going forward and it would not meet its target in 2013. Dr. Z.

testified that at that point he was "really freaking out". (Testimony of Dr. Z. and Mrs. June 12, 2013, pp. 52-54)

[126] Dr. Z. testified that "because [he] had dealings with [Wilson] in September and October… [he] couldn't believe a person that [he] felt was [his] friend would do that to [him]. Dr. Z. testified that "[Wilson] didn't tell [him] about the [Grant Thornton] report. [Wilson] said that he wasn't allowed to tell me about the report. So, basically, we blew everything on that." (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 54)

F. Dunne

Dunne was legal counsel to the FLG entities for a number of years. Dunne was called to the bar in 1988 and has been working with Cassels Brock since then. Phillips was one of Dunne's first clients. As Phillips' business evolved into FLG, Dunne became counsel to FLG. (Testimony of Dunne, June 24, 2013, pp. 46-48). Dunne testified on June 24, 2013 about communications between Cassels Brock and certain of its clients up to and including September 5, 2011. (Testimony of Dunne, June 24, 2013, pp. 44-45)

G. Grant Thornton Report

[127] On August 19, 2011, Grant Thornton completed its review and provided the Grant Thornton Report to Cassels Brock. Phillips testified that he received the Grant Thornton Report from Dunne by way of an email communication from Dunne that was forwarded to Phillips by Hampton. Also, on August 19, 2011, Dunne provided the Grant Thornton Report to Staff. (Testimony of Phillips, June 19, 2013, pp. 50-51; Exhibit 19 -- Respondents' Hearing Brief, Tab 28)

[128] The information presented in the Grant Thornton Report is information of FLG that was provided to the team at Grant Thornton by Hampton and Phillips, which included, among other things, financial statements of FLG, forecasts prepared for the various LPs and business ventures for the fiscal years ended December 31, 2011 to 2013; 2007 – 2008 Audited Financial Statements for WALP prepared by KPMG; 2009 – 2010 Draft Audited Financial Statements for WALP prepared by KPMG; FLG Organization Charts; Offering Memoranda for the various LPs; Minutes of Meetings of the Boards of Directors; and FLG marketing materials for the various LPs. (Exhibit 1 -- Grant Thornton Report, p. 3)

[129] The observations and conclusion in the Grant Thornton Report were those of Grant Thornton. However, Grant Thornton staff relied on information provided by FLG for the analysis and review by Grant Thornton. (Testimony of Krieger, June 6, 2012, p. 6)

[130] As part of their analytical procedures, Grant Thornton staff compared the financial information provided by Phillips and Hampton to, among other things, historical financial information, previous results of FLG, discussions with FLG Management, and other avenues in which Grant Thornton staff could analyse or review the information that was presented. (Testimony of Krieger, June 6, 2012, p. 18)

[131] The cash flow projections of FLG were compiled in integrated cash flow worksheets,

which were confirmed by FLG Management as an "an accurate reflection" of their projections for the next three years in the various FLG entities. FLG's integrated cash flow model was presented as the Base Model (as defined below) in the Grant Thornton Report. (Testimony of Krieger, June 6, 2012, pp. 16-20)

i. Findings Made by Grant Thornton in the Grant Thornton Report

[132] The Grant Thornton Report concluded that the future viability of FLG is contingent on its ability to raise new capital. If FLG was restricted from raising new capital, it would likely be unable to continue its operations in the ordinary course, as it would have insufficient revenue to support its infrastructure, staffing costs and distributions, and to meet their funding requirements for existing projects. (Exhibit 1 -- Grant Thornton Report, p. 12)

[133] The Grant Thornton Report concluded after its assessment that FLG's ability to be viable was contingent on its ability to raise new capital, in addition to achieving a number of other parameters as set out in FLG's projections and FLG's assumptions. The reference to the "viability" of FLG was a qualified term. The Grant Thornton Report articulated a finding that there was "a possibility prospectively of viability if certain things took place." (Testimony of Krieger, June 7, 2013, pp. 68-69)

The Base Model

[134] The base model set forth in the Grant Thornton Report (the **"Base Model"**) was a compilation of FLG's cash flow forecasts and financial projections for 2011 to 2013 for each FLG LP that was consolidated and compiled by Grant Thornton from the cash flow forecast and information provided by FLG into an integrated cash flow model and was supported by a number of stated assumptions that were based on management's view. FLG Management prepared the projections at the request of Grant Thornton. The Base Model contains significant assumptions surrounding the timing and quantum of operating income or loss, capital expenditures, distributions, financing requirements and capital raising. There were 20 Base Model assumptions that were provided by FLG Management and are set out in the Grant Thornton Report. (Testimony of Krieger, June 6, 2013, pp. 15-20; Exhibit 1 -- Grant Thornton Report, p. 42 and p.52)

[135] The Base Model was FLG Management's view and was premised on certain financial assumptions and business behavioural assumptions provided by FLG Management. In order for the Base Model to be achieved, a certain number of financial elements had to occur over the 2011 to 2013 period, and certain business behavioural changes also had to occur. In particular, the Base Model required FLG Management to change the way it deployed capital, in that new investor money could not be used to fund existing projects (including the payment of distributions to earlier investors) nor could cash be moved between LPs. (Testimony of Krieger, June 6, 2013, pp. 131-134; Exhibit 1 -- Grant Thornton Report, p. 71)

[136] The Base Model had to be prepared because Grant Thornton determined that there were a significant number of inter-company transactions that were taking place within FLG. Accordingly, "just looking at the individual cash flow projections of each [FLG] business on its own did not tell a sufficient enough story as to what the overall financial picture of [FLG] would look like over a period of three years, 2011 through 2013." (Testimony of Krieger , June 6, 2012, pp. 16-20)

[137] The Base Model also contained an assumption by FLG Management that after 2013, FLG

would generate enough cash to fund all distributions in the foreseeable future, provided that there are no further property rehabilitations beyond 2013 and that the assets continued to generate operating cash flows at the forecasted 2013 levels. This included projections by FLG that it would raise $223 million in new financing over the three year period, 2011 to 2013, on which FLWM would earn fees of 17 ½ percent on these capital raises. (Testimony of Krieger, June 6, 2013, pp. 26-27; Exhibit 1 -- Grant Thornton Report, p. 43)

[138] The Base Model also included an assumption by FL Management that all new investments, going forward, would be cash flow neutral; that is 82.5% of new capital remaining, after the deduction of fees to be paid to FLWM, would be deployed by FLG in cash-neutral investments, and would not be a burden on the cash flow or operating income of FLG. (Testimony of Krieger, June 6, 2013, pp. 27-32; Exhibit 1 -- Grant Thornton Report, p. 44)

[139] The Base Model also assumed that there would be no further inter-LP movement of funds in order to meet cash flow requirements. Prior to the development of the Base Model, FLG LPs or entities loaned money to FL Finance, which then loaned the money to other LPs or entities that had a cash flow requirement. With the implementation of the Base Model, it was assumed that movement of funds would stop, and new funds would be siloed within each of the new investments, and might be reinvested or distributed to investors of the LP. Phillips understood that this assumption would be an element of the Base Model, and in his view, FLG would be able to operate with that change. (Testimony of Krieger, June 6, 2013, pp. 48-49 and pp. 37-38; Exhibit 1 -- Grant Thornton Report, pp. 52 and 49; Testimony of Phillips, June 20, 2013, pp. 25-27)

[140] Another key assumption was that senior management and certain significant investors would advance $5 million in 2011 in order to "shore up a portion of the recurring WALP cash flow deficiency." FLG was of the view that the "investment of Management's personal resources on a subordinated basis would demonstrate their support for their Base Model and projections for the period 2011 to 2013 and a commitment to the Company." FLG Management would raise unsecured, subordinated debt of $5 million, with restricted repayment terms and no cash payments during the term, in order to rectify a portion of the recurring WALP cash flow deficiency, Grant Thornton understood that these funds would come from people within management or involved on the Board. (Testimony of Krieger, June 5, 2013, pp. 165-167; Testimony of Krieger, June 6, 2013, pp. 46-47; Exhibit 1 -- Grant Thornton Report, pp. 94, 48 and p. 52) Krieger testified that "In the absence of the advance of that $5 million, the Base Model would have a cash flow deficiency'. (Testimony of Krieger, June 6, 2013, pp. 134-136; Testimony of Krieger, June 7, 2013, pp. 73-74; Exhibit 1 -- Grant Thornton Report, pp. 71 and 9) In the end, there no evidence that his capital contribution was made.

[141] The Grant Thornton Report disclosed that:

> "Based on third party information and information provided by Management, we calculate the total FMV of the Assets is $319.2M, with total third party mortgages of $136.2 for a total FMV of the net assets of $182.9M. All 19 of the LPs/companies have a positive FMV of net assets. Once [FLG] investor debt of $115.8M is removed from the FMV of net assets we calculate the FMV of equity at $67.1 M. Based on this analysis, there is a significant shortfall compared to raised equity of approximately $200M. Only WALP and Mortgage Fund appear to have insufficient Net Asset Value to cover their invested debt amounts."

(Exhibit 1 -- Grant Thornton Report, p. 66)

[142] In the absence of raising additional capital, the Grant Thornton Report concluded that FLG would not be able to continue as a going concern. (Testimony of Krieger, June 6, 2012, p. 14) There were significant funds lent between entities in FLG through FL Finance on commercial terms, which allowed FLG to operate as a perpetually going concern, as it has generally had access to capital to meet cash flow shortfalls, using new investor money in some cases. (Exhibit 1 -- Grant Thornton Report, p. 9)

[143] The conclusions in the Grant Thornton Report were based on the assumption that FLG would follow the Base Model assumptions in order to achieve its results. (Testimony of Krieger, June 6, 2013, pp. 15-20 and pp. 38-40; Exhibit 1 -- Grant Thornton Report, p. 42 and pp. 51-52)

[144] According to the Grant Thornton Report, if FLG followed the Base Model and the assumptions and achieved its financial projections, it should have sufficient cash flows within FLG over the three-year period. However, the Base Model represented "a major or drastic departure from the manner in which the company conducted business in the past." (Testimony of Krieger, June 6, 2013, pp. 23-26; Exhibit 1 -- Grant Thornton Report, p. 43; Testimony of Krieger, June 7, 2013, p. 72)

[145] Grant Thornton, in its analysis, "sensitized" certain assumptions in the Base Model because FLG Management's projections were not fully supported by the information presented, nor its historical trends. Grant Thornton noted that "once the Base Model was sensitized, the FL Group has a cash flow deficiency of approximately $15.9 [million] over the three year period of 2011 to 2013".

[146] The Grant Thornton Report also disclosed that in order to address the sensitivities raised by Grant Thornton, FLG Management has identified certain management levers,

> "which it believes it can implement to ensure that [FLG's] obligations can be met and allow their Assumptions to still stand, while in their view having little impact on their ordinary course operations and capital raising efforts going forward. Once the Base Model is sensitized, and all of the Levers are applied, the Company forecasts that it should still be able to satisfy its obligations (aside from intercompany loans)."
>
> (Exhibit 1 -- Grant Thornton Report, p. 11)

[147] Grant Thornton also disclosed that:

> "We have prepared the Asset Valuation of [FLG], using the highest third party valuation figures available for the WALP properties. In this regard, we have calculated an aggregate equity surplus (represented as asset FMV, less third party mortgages and investor debt) of approximately $67M, while there is raised equity in [FLG] of approximately $200M. In this regard, there is a significant equity deficit based on the Asset Valuation. However, the invested equity of $200M does not take into account the grind down of investor's Adjusted Cost Base through return of capital, nor does it include imputed tax benefits the investor receives on their investment. We have shared with Management our Asset

> Valuation in the Report, and they disagreed with the analysis. As set out in the Report, Management has provided us with details of FMV adjustments which they believe are appropriate, which contemplates that equity investors are almost whole. We have not been able to support much of Management's FMV adjustments based on the information presented but we have disclosed same in the Report as a comparative."
>
> (Exhibit 1 -- Grant Thornton Report, p. 12)

[148] Grant Thornton indicated in the Grant Thornton Report that they had not undertaken a review of the flow of funds to specifically conclude where money had been spent. However, through discussions with FLG Management and a review of balance sheets for each FLG LP and FLWM, it would appear the majority of funds loaned to FL Finance by Select LP, Elite LP, Premier LP and Ultimate LP have been loaned by FL Finance to WALP to fund the "rehab" and operating losses of WALP. (Exhibit 1 -- Grant Thornton Report, p.31)

ii. Recommendations Made by Grant Thornton in the Grant Thornton Report

[149] The Grant Thornton Report made the following recommendations:

- Management should take steps to improve its accounting capacity and financial systems, so that it can better accommodate its financial reporting requirements, budgeting process, external auditor liaison, and investor communications;

- FLG should ensure that there are external financial statements available for every entity which holds investors' money. In addition to the entities currently subject to audit, FLG should obtain audits of the FLWM and FL Finance financial statements, to enhance the integrity of its financial reporting. They should further ensure that better reporting and disclosure be made to investors;

- Management should continue with the exercise of maintaining an integrated model, so that it can better prepare and modify projections, identify cash flow requirements and understand the interrelation and impact between the various LPs/companies in the FLG;

- Notwithstanding demonstrable steps that FLG is improving its governance in the past 12 months, the Board should better document its governance policies and procedures, and establish better governance protocols. Further, Management should consider a division of responsibilities as it relates to the executive function, so that there are greater checks and balances in the organization;

- Management should take immediate steps to ensure its investment strategy and business activities align with the projections and assumptions it has set out in the Base Model, and consider having strict Board oversight and/or a third party monitoring program in place to supervise its implementation and the results therefrom on a timely basis; and

- Should Management not achieve its Base Model, it should ensure it is sufficiently agile to implement appropriate [sic] the Levers as it has identified to protect investor's

interests going forward. (Exhibit 1 -- Grant Thornton Report, p. 75)

[150] It is suggested in the Grant Thornton Report that, if FLG is able to achieve its Base Model, or implement sufficient levers to counteract any deficiencies as represented by the sensitivities, there should be minimal erosion to existing investors' equity going forward, and greater investor value may be created as the rehabilitation projects are completed. That statement was made subject to certain qualifications such as real estate market corrections, cost overruns on rehabilitations, or credit restrictions when it comes time to refinance the properties, which Grant Thornton was not able to anticipate at that time. (Exhibit 1 -- Grant Thornton Report, p. 75)

H. September 1, 2011 Meeting

[151] On September 1, 2011, Krieger along with his partner Tim Oldfield ("**Oldfield**") met with Staff, counsel to the Commission, Collins, Andy Wilczynski ("**Wilczynski**") of PricewaterhouseCoopers LLP, a chartered accountant and bankruptcy and insolvency expert retained by Staff, Dunne and Bessner from Cassels Brock, and Hampton to discuss the findings from the Grant Thornton Report (the "**September 1, 2011 Meeting**"). (Testimony of Krieger, June 6, 2013, pp. 146-148 and June 7, 2013, pp. 25-27; Testimony of Collins, June 7, 2013, p. 104 and pp. 116-125; Exhibit 5 -- Hearing Brief: Correspondence and Notes, Tab 17)

[152] The September 1, 2011 Meeting was a question and answer session, with Krieger and Oldfield responding to Staff and Wilczynski. Staff and their advisors challenged some of the bases on which the Grant Thornton Report was presented and asked questions of Krieger to test and ensure that the Grant Thornton Report was reasonable. The questions went to "breaking down the report, breaking down the conclusions into individual business units and [whether] the individual business units were viable or not viable and what would happen if there were no sales…." Krieger indicated that if FLG was unable to raise additional capital, FLG would be unable to continue in the ordinary course. (Testimony of Dunne, June 24, 2013, pp. 72-74 and pp. 81-82; Testimony of Krieger, June 7, 2013, pp. 65-66; Testimony of Collins, June 7, 2013, p. 104 and pp. 116-125)

[153] Collins and Wilczynski also asked questions of Bessner and Dunne about FLG's business. Bessner also stated that FLG was continuing to comply with the Phillips' Undertaking; however, she did not mention that FLG was raising capital through FLEX LP, FLEX Fund Class B and C, Venture LP, FLWM Fund, PrimeTime Living LP or Beverages LP. (Testimony of Collins, June 7, 2013, pp. 118-121 and pp. 123-124; Exhibit 5 -- Hearing Brief: Correspondence and Notes, Tab 17, pp. 44 and 45)

[154] Staff was told that $5 million special financing (the "**Special Financing**"), would be raised, of which $1 million would be contributed by Phillips, and the other directors would make up some of the remaining $4 million If $4 million was not raised from the other directors, then they would contact the longest standing FLG Investors to see if they would invest. The Special Financing was described as high risk, with no distributions, for a term of three years, and payback would be linked to an objective or a milestone of the company. (Testimony of Phillips, June 20, 2013, pp. 49-50)

[155] After the September 1, 2011 Meeting concluded, Dunne and Bessner were asked by Kathryn Daniels ("**Daniels**"), Deputy Director of Enforcement Staff, to stay behind where Daniels advised that Staff had not accepted the Grant Thornton Report nor the Base Model. Daniel also

advised that there were "no plans for immediate action" by Staff. (Testimony of Dunne, June 24, 2013, pp. 72-74 and pp. 81-82; Exhibit 5 -- Respondents' Hearing Brief, Tab 33 and Tab 34)

[156] Collins recalled that at the September 1, 2011 Meeting, Bessner stated that FLG was continuing to comply with the Phillips' Undertaking. Collins stated that she did not make a note of this comment; at the time, she wondered why Bessner made the comment, because Collins had forgotten that the Phillips' Undertaking expired a week after receipt of the Grant Thornton Report. So, when Bessner made the remark, Collins did not realize that Bessner was saying something of substance. (Testimony of Collins, June 7, 2013, pp. 123-124; Exhibit 5 -- Hearing Brief: Correspondence and Notes, Tab 17)

I. September 5, 2011 Board Meeting

[157] On September 5, 2011, a meeting of the board of directors of FLWM and 965010 was held (the "**September 5 Board Meeting**"). The Grant Thornton Report was the main point of discussion. As a preliminary matter, Phillips explained, and all directors agreed, that "more detailed minutes of the meetings were required and greater care had to be taken in developing resolutions out of discussions of the Board and recording Board approval of same." (Exhibit 19 -- Respondents' Hearing Brief, Tab 37)

[158] Phillips indicated to the Board, with respect to the Grant Thornton Report, that "it was a positive report in respect of what management was hoping for in that the report concluded that First Leaside overall was viable, with certain qualifications based on the correctness of forecasts." Phillips told the Board that he thought that the recommendations in the Grant Thornton Report "were all things that management wants to implement and will implement" and that FLG Management was making arrangements to retain the services of various consultants to help implement the recommendations set forth in the Grant Thornton Report. (Exhibit 19 -- Respondents' Hearing Brief, Tab 37)

[159] Phillips also explained to the Board that the Commission had received and reviewed the Grant Thornton Report and had made no comment or taken any action, which Phillips construed as a positive sign. In the minutes of the September 5 Board Meeting it is recorded that "Dunne explained that the OSC has not endorsed the [Grant Thornton] Report but he concurred with Mr. Phillips that the lack of response from the OSC could be taken as positive. Dunne stated that "the more time that passed without an OSC response, the better it looked for the outcome, however this was not certain". Phillips also stated at the September 5 Board Meeting that increasing FLG's governance and financial reporting procedures would likely satisfy the OSC. (Exhibit 19 -- Respondents' Hearing Brief, Tab 37; Testimony of Phillips, June 19, 2013, pp. 62-65; Testimony of Dunne, June 24, 2013, pp. 75-76)

[160] Dunne further explained that FLG, from a financial perspective, was not in "a bad situation through to 2013", however there was a projected large cash shortfall for WALP in 2012. Dunne explained that if this "hole" was left unaddressed it might encourage the Commission to take some form of action. The "hole" was $5 million, representing cash required to finish the rehabilitation project and pay distributions to investors. (Exhibit 19 -- Respondents' Hearing Brief, Tab 37)

[161] Dunne explained that Grant Thornton suggested beginning with Step 3 – the Special Financing – and that the Special Financing should be structured in a form of equity to be issued in

2011 or early 2012, which would fix the $5 million dollar shortfall. (Exhibit 19 -- Respondents' Hearing Brief, Tab 37)

[162] Phillips explained that the Grant Thornton Report indicated the Special Financing should be raised from investment from Directors and Trustees, particularly Phillips. He explained to the Board that he would contribute $500,000 and has already done so. Phillips, however, explained that the idea that the Board members should have to fund the Special Financing exclusively is not palatable as it gives the impression that they have somehow benefitted wrongly. (Exhibit 19 -- Respondents' Hearing Brief, Tab 37)

[163] Hyatt testified that he expressed concern that FLG would be offside of the Phillips' Undertaking by raising those funds and asked Phillips whether there was a restriction on raising of capital and Phillips indicated that there was none. There was no reference to that exchange in the minutes of the September 5 Board Meeting. (Testimony of Hyatt, June 24, 2013, p. 35-37)

[164] The Board resolved that management was "authorized to develop an investment structure that complies with the recommendations of the [Grant Thornton Report] to raise $5 million for WALP for presentation to the Board." (Exhibit 19 -- Respondents' Hearing Brief, Tab 37)

[165] Late in the September 5 Board Meeting, an in-camera session of the independent directors was held where it was determined that Dunne would prepare a letter to the Commission outlining the Board's reaction to the Grant Thornton Report and the Board's proposed responses to the recommendations outlined by Grant Thornton. (Exhibit 19 -- Respondents' Hearing Brief, Tab 37)

J. September 8, 2011 Meeting

[166] On September 8, 2011, the independent members of the Board of FLWM met with Grant Thornton, including Krieger, at the offices of Cassels Brock to discuss the Grant Thornton Report and received further insight into the mandate of Grant Thornton, the process they followed to complete the Grant Thornton Report, and their conclusions and recommendations (the "**September 8, 2011 Meeting**"). The meeting was by way of conference call with the Board of Directors of FLWM. Not all of the Board members were on the call. Phillips was not on the call. (Opening Statements of the Respondents dated June 5, 2012 at p. 6; Testimony of Krieger, June 6, 2013, pp. 148-149; Testimony of Hyatt, June 24, 2013, pp. 20-21)

K. September 12, 2011 Letter to Staff

[167] On September 12, 2011, Dunne sent a letter to Daniels (the "**September 12 Letter**"), copied to all members of the FLWM Board, Phillips, Hampton, Efraim and Bessner, setting out the preliminary response of the FWLM Board to the Grant Thornton Report and to inform Daniels of the steps that had been taken, steps in process and steps being contemplated in response to the Grant Thornton Report. Dunne stated in the September 12 Letter that the FLWM Board understood the general thrust of the Grant Thornton Report, the implications for the FLG organization, the key operating assumptions in the Base Model presented in the Grant Thornton Report, and appreciated the benefits to the FLG organization and to its investors of following the recommendations set out in the Grant Thornton Report. Dunne also indicated in the September 12 Letter that the Board and FLG Management was in the process of structuring the Special Financing. (Testimony of Collins, June 7, 2013, pp. 125-127; Exhibit 5 -- Hearing Brief:

Correspondence and Notes, Tab 18, pp. 46-47; Testimony of Phillips, June 19, 2013, pp. 92-93; Testimony of Dunne, June 24, 2013, pp. 82-83 and pp. 106-108)

L. September 17, 2011 WALP Annual General Meeting

[168] On September 17, 2011, FLG held the WALP Annual General Meeting (the "**WALP AGM**"). Several hundred people were in attendance, including those who owned WALP equity or Funds or who were invested in seed capital deals related to the U.S. real estate, long-time investors and prospective clients. Phillips, who was introduced by Efraim, was the only speaker. (Testimony of Phillips, June 19, 2013, pp. 89-91 and pp. 119-121; Exhibit 19 -- Respondents' Hearing Brief, Tab 40)

[169] Phillips gave a PowerPoint slide presentation consisting of 114 slides, at the WALP AGM which took approximately one hour. Phillips provided an overview of WALP's real estate properties, the WALP financial statements prepared by KPMG, and conducted a question and answer period. Phillips did not, however, discuss the financial statements in their entirety nor did he mention or discuss or, in any way, disclose the Grant Thornton Report. Phillips also addressed challenges for WALP in terms of rehabilitating the rental units, the declining real estate market, and occupancy rate issues. Phillips' PowerPoint slides presentation included references to "new cycles of opportunity" and the "sound financial position" of FLG. When one investor asked a question about the going concern note contained in the financial statements, Phillips indicated that there were matters in dispute, and that they were trying to have the going concern note removed from the financials. (Testimony of Mrs. C., June 17, 2013, pp. 36-38; Exhibit 18 -- Hearing Brief: V.C. , Tab 3; Testimony of Phillips, June 19, 2013, pp. 122-125; Testimony of Chien, June 10, 2013, pp. 159-169; Exhibit 19 -- Respondents' Hearing Brief, Tab 40, p. 6)

M. Investments During the Sales Period

[170] FLG sales team continued to raise capital in FLG entities during the Sales Period. The total value of investments sold to FLG Sales Investors by FLG salespeople during the Sales Period was $18,765,168. (Testimony of Collins, June 7, 2013, pp. 156-158 and pp. 169-183; Exhibit 11 -- Analysis of Sales During the Sales Period Brief, Tab 1) The completed sales were as follows:

Entity	**Subscription Price for Units Sold**
Special Notes LP	$8,077,328
First Leaside Expansion LP	$3,927,102
Flex Fund – Class B and C	$3,029,990
First Leaside Venture LP	$1,921,359
FLWM Fund	$1,265,931
First Leaside Primetime Living LP	$335,000
First Leaside Beverages Group LP	$130,010
Wimberly Apartments LP	$78,448
Total	**$18,765,168**

(Amended Statement of Allegations, April 25, 2013, paragraph 26; Exhibit 7 -- Hearing Brief: Lists of Sales During Sales Period and Marketing Material; Exhibit 11 -- Hearing Brief: Analysis

of Sales During the Sales Period; Testimony of Chien, June 10, 2013, pp. 86-102; Testimony of Phillips, June 19, 2013, pp. 76-84; Testimony of Phillips, June 20, 2013, pp. 14-17; Testimony of Collins, June 7, 2013, pp. 158-169; Exhibit 8 -- Hearing Brief: 45-106 Forms and Manual Payment Transmittal Forms Filed by Filing Date (Volume 1 of 2); Exhibit 9 -- Hearing Brief: 45-106 Forms and Manual Payment Transmittal Forms Filed by Filing Date (Volume 2 of 2); Exhibit 10 -- Hearing Brief: First Leaside Subscription Agreements)

[171] During the Sales Period, Wilson sold a total of $8,945,865 of units to 94 FLG Sales Investors, with an average of almost $900,000 of securities during each week of the Sales Period. Phillips sold a total of $3,388,626 of units to 46 FLG Sales Investors. Chien sold a total of $2,268,081 of units to 40 FLG Sales Investors, the majority of which was to existing clients. (Testimony of Collins, June 7, 2013, pp. 156-158 and pp. 169-183; Exhibit 11 -- Hearing Brief: Analysis of Sales During the Sales Period Brief Tabs 1, 10, 11 and 12; Testimony of Phillips, June 20, 2013, pp. 13-14; Testimony of Wilson, June 20, 2013, pp. 104-107; Testimony of Chien, June 10, 2013, pp. 82-84)

N. Grant Thornton Monitor's Report

[172] Staff submitted the Grant Thornton Confidential Report of Monitor, First Leaside Group of Companies dated December 9, 2011 (the "**Monitor's Report**") which gave a retrospective analysis of the business of FLG Entities between August 19, 2011 and November 1, 2011 (the "**Monitor's Review Period**") and the total source of funds received into the FLG Group.

[173] The Monitor's Report revealed that the total source of funds received in FLG during the Monitor's Review Period was $24.1 million, of which $20 million was raised from new investors. Funds raised from FLG Sales Investors were placed into nine different accounts, three of which were Special Notes (CAD), Special Notes (USD) and Beverages LP. The total use of funds was approximately $25.6 million, of which $8.4 million was used to close the purchase of the three Ottawa properties by Venture LP, $4.43 million was used to buy out all of the Development Notes by FLEX LP, and $3.7 million was distributed to FLG Investors. The remainder related to other expenditures.

[174] The Monitor's Report also indicated that during the Monitor's Review Period, the FLG Management did not follow the siloed approach to maintain its funds as set out in the Base Model. There were significant internal transfers between the First Leaside accounts totalling over $83 million, a portion of which was used to fund a portion of operating costs within the WALP portfolio of properties. (Testimony of Krieger, June 6, 2013, p. 166, paras. 3-11; Exhibit 3 -- Monitor's Report, p. 7)

[175] The Monitor's Report identified that $10,175,000 of the initial proceeds of the Special Notes LP raised were indirectly deposited into FL Finance. In particular, $3,789,000 went to WALP in the Canadian account related to the Texas Properties. And then the WALP Canadian account transferred $3,724,00 to WALP U.S. dollar account and then the WALP U.S. dollar account disbursed $3,534,000 to a number of different entities including $2.3 million to Master Texas and $619,000 was transferred to FL Fund which was related to the WALP portfolio, and $340,000 went to fund distributions within WALP. Another $128,000 was transferred back to FL Finance. (Testimony of Krieger, June 6, 2013, pp. 173-175)

[176] The Monitor's Report also disclosed that Phillips made a loan of $500,000 to FLG on

September 2, 2011 and FLG paid $80,000 to Phillips on September 8, 2011 and repaid the amount of $500,000 to Phillips on November 3, 2011. (Testimony of Krieger, June 6, 2013 p. 167; Exhibit 3 -- Monitor's Report, p. 7)

6. ANALYSIS

A. Did the Respondents, Phillips and Wilson, each directly or indirectly engage or participate in an act, practice or course of conduct relating to securities which they knew, or reasonably ought to have known, would perpetrate a fraud on investors, contrary to subsection 126.1(b) of the Act and contrary to the public interest?

i. The Applicable Law

[177] Subsection 126.1(b) of the Act provides that:

> *A person or company shall not, directly or indirectly, engage or participate in any act, practice or course of conduct relating to securities, derivatives or the underlying interest of a derivative that the person or company knows or reasonably ought to know,*
>
> ……..
>
> *(b) perpetrates a fraud on any person or company.*

[178] Fraud is "one of the most egregious securities regulatory violations" and is both "an affront to the individual investors directly targeted" and something that "decreases confidence in the fairness and efficiency of the entire capital market system" *(Re Capital Alternatives Inc., 2007* ABASC 79 at para. 308, citing D. Johnston & K. D. Rockwell, *Canadian Securities Regulation*, 4th ed., Markham: LexisNexis, 2007 at 420) ("***Capital Alternatives***").

[179] The term "fraud" is not defined in the Act, however subsection 126.1(b) of the Act has been considered by the Commission in *Re Al-tar* (2010), 33 O.S.C.B. 5535 ("***Al-tar***") and subsequent decisions of the Commission provided by Staff including *Re Lehman Cohort* (2010), 33 O.S.C.B. 7041 ("***Re Lehman Cohort***"), at paragraphs 86-100; *Re Global Partners* (2010), 33 O.S.C.B. 7783 ("***Re Global Partners***"), at paragraphs 238-245; and *Re Borealis International Inc.* (2011), 34 O.S.C.B. 777 ("***Re Borealis***"), at paragraphs 65-67.

[180] The Supreme Court of Canada discussed the elements necessary to establish fraud in *R. v. Théroux,* [1993] 2 S.C.R. 5 ("***Théroux***") at paragraph 27. Justice McLachlin (as she then was) stated that since the *mens rea* of an offence is related to its *actus reus,* it is helpful to begin the analysis by considering the *actus reus* of the offence of fraud (*Théroux, supra* at para. 16). The *actus reus* of the offence of fraud, is established by proof of:

> (a) the prohibited act, be it an act of deceit, a falsehood or some other fraudulent means; and
> (b) deprivation caused by the prohibited act, which may consist in actual loss or the placing of the victim's pecuniary interests at risk.
> (*Théroux, supra* at para. 27)

[181] With respect to deceit and falsehood, in the first branch of the *actus reus* of fraud, the

Supreme Court of Canada held that "all that need be determined is whether the accused, as a matter of fact, represented that a situation was of a certain character, when, in reality, it was not" (*Théroux*, supra, at para. 18)

[182] Where it is alleged that the *actus reus* of a particular fraud is "other fraudulent means", the Supreme Court of Canada held that the existence of such means is "determined objectively, by reference to what a reasonable person would consider to be a dishonest act" (*Théroux*, supra, at paras. 17 and 18; and *R. v. Olan*, [1978] 2 S.C.R. 1175 (S.C.C.) ("***Olan"***) at p. 1180). The concept of "other fraudulent means" is intended to encompass all other means, other than deceit or falsehood, which can be properly characterized as dishonest (*R. v. Zlatic*, [1993] 2 S.C.R. 29 ("***Zlatic***") at para. 31 citing *Olan*, supra at p.1180) "Other fraudulent means" includes the non-disclosure of important facts (*Zlatic*, supra at para.31; and *Théroux*, supra, at para. 18).

[183] The second branch of the *actus reus* of fraud, deprivation, is "established by proof of detriment, prejudice or risk of prejudice to the economic interests of the victim caused by the dishonest act" (*Théroux, supra*, at paras. 16 and 27). In establishing deprivation, it is not necessary to prove that an accused ultimately profited or received an economic benefit or gain from the conduct or that actual deprivation or actual economic loss occurred (*Théroux, supra,* at para. 19).

[184] The element of "deprivation" is satisfied on proof of: (i) actual loss to the victim; (ii) prejudice to a victim's economic interest; or merely (iii) the risk of prejudice to the economic interests of a victim even though no actual loss has been suffered. (*Théroux*, above, at paras. 16-17 and 27)

[185] The establishment of fraud also requires proof of the necessary mental element (the *mens rea*) on the part of the accused. The Supreme Court of Canada in *Théroux* held that the mental element 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).

   (*Théroux*, supra at para. 27)

[186] The Supreme Court of Canada in *Théroux* observed that subjective awareness of the consequences can be inferred from the act itself (*Théroux, supra*, at para. 23) and that it is not necessary to show precisely what was in the mind of the accused at the time of the fraudulent act. The Court stated in *Théroux,* in respect of awareness of the risk of deprivation that:

> [t]he accused must have subjective awareness, at the very least, that his or her conduct will put the property or economic expectations of others at risk. As noted above, this does not mean that the Crown must provide the trier of fact with a mental snapshot proving exactly what was in the accused's mind at the moment the dishonest act was committed. In certain cases, the inference of subjective knowledge of the risk may be drawn from the facts as the accused believed them to be… [W]here the accused tells a lie knowing others will act on it and thereby

> puts their property at risk, the inference of subjective knowledge that the property of another would be put at risk is clear.
>
> (*Théroux*, supra at para. 29)

[187] To establish the *mens rea* of fraud requires proof that the Respondents "undertook the acts which constitute the falsehood, deceit or other fraudulent means, and that the accused was aware that deprivation could result from such conduct." (*Théroux*, supra at para. 39) A sincere belief or hope that no risk or deprivation would ultimately materialize does not establish an absence of fraud. The Supreme Court of Canada has held that "the fact that the accused may have hoped the deprivation would not take place, or may have felt there was nothing wrong with what he or she was doing, provides no defence" and further stated that "the better view is that the accused's belief that the conduct is not wrong or that no one will in the end be hurt affords no defence to a charge of fraud". (*Théroux*, supra, at para. 24 and para. 35).

[188] The Supreme Court of Canada in *Théroux* stated:

> A person who deprives another person of what the latter has should not escape criminal responsibility merely because, according to his moral or her personal code, he or she was doing nothing wrong or because of a sanguine belief that all will come out right in the end. Many frauds are perpetrated by people who think there is nothing wrong in what they are doing or who sincerely believe that their act of placing other people's property at risk will not ultimately result in actual loss to those persons. If any offence of fraud is to catch those who actually practise fraud, its *mens rea* cannot be cast so narrowly as this.
>
> This approach conforms to the conception of the offence of fraud which imbues this Court's decision in *Olan*. *Olan* points the way to a conception of fraud broad enough in scope to encompass the entire panoply of dishonest commercial dealings. It defines the *actus reus* accordingly; the offence is committed whenever a person deceives, lies or otherwise acts dishonestly, and that act causes deprivation (including risk of deprivation) to another. To adopt a definition of *mens rea* which requires subjective awareness of dishonesty and a belief that actual deprivation (as opposed to risk of deprivation) will result, is inconsistent with *Olan*'s definition of the *actus reus*. The effect of such a test would be to negate the broad thrust of *Olan* and confine the offence of fraud to a narrow ambit, capable of catching only a small portion of the dishonest commercial dealing which *Olan* took as the target of the offence of fraud
>
> (*Théroux*, supra at paras. 36 and 37)

[189] The Supreme Court of Canada's test for fraud was applied in respect of securities regulatory proceedings by the British Columbia Court of Appeal in *Anderson v. British Columbia (Securities Commission)*, 2004 BCCA 7 ("***Anderson***") (at para. 27) in its consideration of section 57(b) of the British Columbia Securities Act and adopted by the Commission in *Al-tar, supra* at para. 217).

ii. Analysis and Findings

[190] This Panel finds that the Respondents sold securities of FLG Entities during the Sales Period, without disclosing the Grant Thornton Report and, in particular, the important facts in the

Grant Thornton Report, to FLG Sales Investors, which they knew would perpetrate a fraud within the meaning of subsection 126.1(b) of the Act. Phillips and Wilson had the subjective knowledge that by not disclosing the Grant Thornton Report and, in particular, the important facts in the Grant Thornton Report, to FLG Sales Investors they put the financial or pecuniary interests of FLG Sales Investors at risk.

The Actus Reus and Mens Rea of Fraud

[191] We find that the Grant Thornton Report contained important facts with respect to the business of FLG, which ought to have been disclosed to prospective FLG Sales Investors, but were not disclosed to prospective FLG Sales Investors. Particularly, the Grant Thornton Report disclosed the following:

> (a) [t]he future viability of the [FLG] is contingent on their ability to raise new capital, in addition to achieving a number of other parameters as set out in their projections and underlying assumptions. One of the largest sources of revenue in [FLG] is the fees it generates in FLWM on the raising of new capital. If [FLG] was restricted from raising new capital, it would likely be unable to continue its operations in the ordinary course, as it would have insufficient revenue to support its infrastructure, staffing costs, distributions, and to meet their funding requirements for existing projects.
>
> (Exhibit 1 -- Grant Thornton Report, p. 66)
>
> (b) there is a significant equity deficit based on the Asset Valuation.
>
> (Exhibit 1 – Grant Thornton Report, p. 12 and p. 66)
>
> (c) [FLG] would have a cash flow deficiency of approximately $15.9 million over the three year period of 2011 to 2013.
>
> (Exhibit 1 – Grant Thornton Report, p. 9)

[192] Both Phillips and Wilson maintained throughout their respective testimony that the Grant Thornton Report concluded that FLG was viable. Phillips testified that the Grant Thornton Report was positive in terms of "what management was hoping for and that the report concluded that First Leaside overall was viable, with certain qualifications based on the correctness of forecasts." Wilson testified that he wanted to publish the Grant Thornton Report. He testified that "…my own personal reason for wanting to publish the report was that it was going to confirm that we had a viable plan going forward three years which would have, in my opinion, been good news for those people." (Testimony of Wilson, June 20, 2013, p. 75)

[193] However, we find, and Krieger confirmed, that the Grant Thornton Report does not contain language that FLG is viable, but that:

> [t]he report qualifies that the company's ability to be viable is contingent on its ability to raise new capital, in addition to achieving quite a number of other parameters as set out in their projections and the assumptions that support that. So, it was a reference to viability as a qualified term.

(Testimony of Krieger, June 5, 2013, pp. 407-408)

[194] We find that both Phillips and Wilson had the subjective knowledge that the Grant Thornton Report contained those important facts, which they did not disclose to prospective FLG Investors.

[195] As directing mind and as member of the Board, Phillips had a copy of the Grant Thornton Report and knew of its contents and conclusion. Hyatt testified that Phillips presented a management summary of the Grant Thornton Report at the September 5 Board Meeting. (Testimony of Hyatt, June 24, 2013, p. 16)

[196] We also find that Wilson had the subjective knowledge that the Grant Thornton Report contained those important facts because as a member of the Board, he too had a copy of the Grant Thornton Report and was at the September 5 Board Meeting where its contents and conclusions were discussed.

[197] Phillips did not address in his testimony at the Merits Hearing, why FLG Investors did not need to know that, without the fees that FLG generates in FLWM, FLG would likely be unable to continue its operations or that there is a significant equity deficit based on the Asset Valuation or that FLG would have a cash flow deficiency of approximately $15.9 million over the three year period of 2011 to 2013. However, the Grant Thornton Report disclosed that FLG Management, which included Phillips and Wilson, was "reluctant to reduce distributions entirely as it does not want to signal to current investors (and potential investors) that the LP cannot cover its own stated distributions." We find that Phillips and Wilson had the subjective awareness that FLG Investors would find the fact that FLG LPs could not cover stated distributions from the operations of the respective LP or that there is a significant equity deficit based on the Asset Valuation or that FLG would have a cash flow deficiency of approximately $15.9 million over the three year period of 2011 to 2013 were important facts, and were important enough for the Respondents to conceal, thereby putting the investors' financial or pecuniary interests at risk.

[198] Failing to disclose important information to investors constitutes a dishonest act. Courts have included the non-disclosure of important facts to be within the meaning of "other fraudulent means" (See *Théroux,* supra at para. 18; *Zlatic*, supra at para. 31; *R. v. Émond* (1997), 117 C.C.C. (3d) 275 (Que. C.A.), leave to appeal denied, [1997] S.C.R. No. 335 ("***Émond***"). In *Émond*, the Quebec Court of Appeal found fraud on the basis, in part, of the accused's "intended and planned non-disclosure of the objective reality" of certain investment transactions. In that case, the accused specifically represented to investors that he had negotiated the best price for various real estate investments, yet failed to disclose hidden profits of several hundred thousand dollars which he was making through each sale. (*Émond,* supra at pp. 278-279 and 286).

[199] Both Phillips and Wilson knew that FLG's viability was contingent on FLG adopting the Base Model, which required management to change the way it deployed capital, in that new investor money could not be used to fund existing projects (including the payment of distributions to earlier investors) nor could cash be moved between LPs. The Base Model represented "a major or drastic departure" from the manner in which the FLG conducted business. Without the Grant Thornton Report, FLG Sales Investors were deprived of important facts, which were in the hands of the Respondents, and, as a result, the financial or pecuniary interests of FLG Sales Investors were put at risk. (Testimony of Krieger, June 7, 2013, p. 72)

[200] Phillips and Wilson knew that, in light of Grant Thornton's findings, as disclosed in the Grant Thornton Report, they failed to disclose important information to FLG Sales Investors during the Sales Period with respect to the cash flow deficiencies in FLG entities, regarding the use of proceeds raised from investors, the state of FLG in the statements they made at the September 17, 2011 WALP AGM, on the FLG Website, and in Marketing Materials and in their communications with FLG Sales Investors.

[201] We infer from all of the facts that Phillips and Wilson knew that the Grant Thornton Report contained these important facts. We find that the evidence establishes that both Phillips and Wilson committed dishonest acts by failing to disclose important information to FLG Sales Investors, which caused deprivation by putting the financial or pecuniary interests of FLG Sales Investors at risk.

Representations made at the September 17, 2011 WALP AGM

[202] During the Sales Period, Phillips made representations that it was "business as usual" to Mr. M. and at the September 17, 2011 WALP AGM. Phillips also reported at the September 17, 2011 WALP AGM to FLG Investors and FLG Sales Investors that "sales had never been better." Wilson, during the Sales Period, created an impression that "the company [was] doing fantastic" and then he encouraged Dr. Z. to invest in the Special Notes LP. Wilson said "[i]f you have anything more to invest, we have this great product coming out. It's going to pay 10.1 percent. You will only be exposed for a year." Wilson also told Dr. Z. that "[w]e were having our best year on record." (Testimony of Mr. M., June 2013, p. 135, paras. 9-15, p. 132, paras. 17-18 and p. 150, para. 23; Testimony of Wilson, June 20, 2013, p. 12, paras. 16-19; and Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 27, para. 15 and p. 43, paras. 3-4)

[203] We are troubled that Phillips represented to investors that it was "business as usual" at FLG and that Wilson created an impression that "the company [was] doing fantastic" during the Sales Period. In light of the conclusions made in the Grant Thornton Report, this was a deliberate falsehood. As the directing mind of FLG, Phillips knew that the Grant Thornton Report disclosed that it was anything but "business as usual" at FLG since the Board had resolved at the September 5 Meeting to authorize FL Management "to develop an investment structure that complies with the recommendations of the [Grant Thornton Report] to raise $5 million for WALP for presentation to the Board" and that this, together with stopping the movement of funds such that new funds be siloed within each of the new investment entities, would represent "a major or drastic departure" from FLG's way of doing business. (Testimony of Mr. M., June 11, 2013, p. 135, paras. 9-15, Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 27, para. 15; Testimony of Hyatt, June 24, 2013, p. 35, paras. 1-5)

[204] Additionally, both Phillips and Wilson knew that the Grant Thornton Report disclosed that funding losses and property rehabilitation programs would have a negative short term cash flow impact on FLG because FL Finance will have to pay 7% related party interest to the lending LP (to cover the distribution payments) but FL Finance would not receive 7% related party interest from the borrowing LP (WALP in this case) if the borrowed money is being used to fund operating losses and rehabilitation programs that are not yet generating income. Accordingly, in instances such as this, the related party balance owing to FL Finance from the borrowing LP would continue to grow with accruing interest. Both Phillips and Wilson also knew that Grant Thornton had determined that "FLG would have a cash flow deficiency of approximately $15.9M over the three year period of 2011 to 2013." (Exhibit 1 -- Grant Thornton Report, p. 9)

[205] We find that each of the Respondents, as a matter of fact, represented that the state of FLG was of a certain character, when in reality, it was not. We find that the Respondents' actions were deliberate and formed part of a willful strategy to continue to raise capital for FLG in order to meet its obligations across the spectrum of its entities.

[206] Phillips testified that he did not have any concerns personally about selling securities to investors without them having any awareness of the Grant Thornton Report because "we didn't think we were allowed to give out the report, and I thought that we were taking great pains to try to disclose what was needed to be disclosed to whoever was investing in their respective deals." (Testimony of Phillips, June 19, 2013, p. 92, paras. 18-22) Notwithstanding Phillips' testimony, he did not disclose to FLG Sales Investors the important facts and other contents of the Grant Thornton Report in the Marketing Materials that were given to FLG Sales Investors, and in respect to the Special Notes, there were no offering documents.

[207] It is not necessary for this panel to consider whether Phillips considered his actions to be dishonest in order to find Phillips contravened subsection 126.1(b) of the Act. Nor does the fact that both Phillips and Wilson believed that their respective conduct was not wrong, provide a defence for fraud. As the Supreme Court of Canada has held "the fact that the accused may have hoped the deprivation would not take place, or may have felt that there was nothing wrong with what he or she was doing, provides no defence" (*Théroux*, supra at para. 24). "The question is whether the accused subjectively appreciated that certain consequences would follow from his or her acts" (*Théroux*, supra, at para. 22). Further, in para 21 in *Théroux*, the Court states that "the test is not whether a reasonable person would have foreseen the consequences of the prohibited act, but whether the accused subjectively appreciated those consequences at least as a possibility".

[208] We find that the evidence established that the Grant Thornton Report contained facts with respect to the business of FLG Group that a reasonable investor would consider important. We also find that the fact that the Respondents continued to sell securities of FLG entities, without disclosing the Grant Thornton Report, was detrimental to, and deprived FLG Sales Investors of important facts that put their financial or pecuniary interests at risk.

[209] We find that Phillips deliberately and intentionally withheld the Grant Thornton Report and, in particular, the important information contained within it from FLG Sales Investors. In so doing, Phillips was aware that deprivation or risk of deprivation could follow as a likely consequence, putting the financial or pecuniary interests of FLG Sales Investors at risk.

[210] We find that Wilson deliberately withheld the Grant Thornton Report and, in particular, the important facts contained in the Grant Thornton Report from FLG Sales Investors. In so doing, Wilson was aware that deprivation or risk of deprivation could follow as a likely consequence, putting the financial or pecuniary interests of FLG Sales Investors at risk.

[211] This panel is satisfied that, on a balance of probabilities, in these circumstances, there is clear, convincing and cogent evidence that Staff has proven the *actus reus* and *mens rea* of fraud on the part of both Phillips and Wilson. We find that each of the Respondents engaged in or participated in an act, practice or course of conduct relating to securities that they knew would perpetrate a fraud on FLG Sales Investors, contrary to subsection 126.1(b) of the Act and contrary to the public interest.

iii. Reliance on Legal Advice

[212] Both Phillips and Wilson testified that they received legal advice that they could not disclose the Grant Thornton Report. The Commission has previously held that even if a defence of reliance on legal advice is available, that defence will fail unless the respondent can establish four things:

> 1. The lawyer had sufficient knowledge of the facts on which to base the advice;
> 2. The lawyer was qualified to give the advice;
> 3. The advice was credible given the circumstances under which it was given; and
> 4. That the respondent made sufficient enquiries and relied on the advice.
>
> (*Mega-C Power Corp. (Re)* (2010), 33 O.S.C.B. 8290, para. 261;)

[213] There was no evidence submitted or produced by the Respondents to support a finding that legal advice was given not to disclose the Grant Thornton Report during the Sales Period and that the Respondents relied on that advice. Phillips testified that he was given legal advice at the September 5 Board Meeting, but acknowledged that the advice did not appear in the minutes of the September 5 Board Meeting. (Testimony of Phillips, June 20, 2013, p. 26) On cross-examination of Phillips by Staff, the following exchange occurred:

> Q. No one asked Grant Thornton for their consent to disclose that report, did they?
>
> A. I asked the attorneys if we could send it out, and I was told no. I don't see why I would then go and ask the author if I can when my lawyer's already said I can't.
>
> Q. So you didn't say to Mr. Dunne, 'Well, that may be your considered view, Mr. Dunne, but I'm euphoric about this report, and I think that you should go to Mr. Krieger and ask him if I can share it with my investors'?
>
> A. My attorney has just told me that I will be violating the law if I do it, and you're asking me to then say I should have overruled him? He's my attorney, it's his advice that I need to take, and he told me you can't send it out.
>
> Q. And you didn't take any other steps or ask any other questions in respect of that?
>
> A. No, ma'am, I did not.
>
> Q. Okay. Because we know, of course, from Mr. Krieger's testimony he was absolutely clear he was only asked twice for his consent to disclose the report: First, on August 19, 2011, and again in early November 2011. Isn't that right?

A. That's Mr. Krieger's testimony.

(Testimony of Phillips, June 20, 2013, p. 28-29)

[214] Phillips acknowledged that no opinion letter was provided, nor was he aware of any email containing the legal advice but stated that "I believe Mr. Dunne is a witness, and he will give his testimony." (Testimony of Phillips, June 20, 2013, pp. 29-30)

[215] On his direct examination, Wilson was asked about sales and disclosure of the Grant Thornton Report:

Q. Did anyone say you couldn't sell at that meeting?

A. Never came up.

Q. Did anyone --

A. Well, except for the Wimberly, except for the U.S. assets which were under the undertaking. And to our -- to my knowledge, what I was -- that it was understood that that had expired or it had been fulfilled, and so that was behind us as well. So that did get discussed, but that was...

Q. Okay. Did anyone discuss disclosing the Grant Thornton report more broadly than the board of directors?

A. It was certainly discussed.

Q. Can you tell us what was said?

A. Um, there was an interest by one of the independent directors, would that be possible to publish the report.

Q. Do you remember who that was?

A. I believe it was Doug Hyatt, but I can't be a hundred percent certain.

Q. What was the response, then, to the question?

A. My understanding is the response was no, it would not be, like, possible. I'm sorry, I'm trying to remember the actual expression, and I don't. "Not likely" might have been the expression.

Q. Do you remember who gave the response?

A. My recollection, I'm afraid, is -- it was either -- in my recollection, I wasn't certain. It was either David Phillips, Leon Efraim, or Grant -- or Peter Dunne.

> Q. Whoever responded, did they tell you -- was there a reason given why it was unlikely?
>
> A. Oh, the reason was understood to be section 16, that it was not -- that it was part of a... It was production of the investigation and it was a part investigation, and as such, it was clearly covered by section 16.
>
> (Testimony of Wilson, June 20, 2013, pp. 73-74)

[216] Wilson testified that he understood that the Grant Thornton Report was part of the "gag order." Wilson said that it was his "own conclusion" that the Grant Thornton Report was naturally part of the Commission process. However, Wilson also testified that he was not necessarily told that in those words by Phillips or Efraim, but "it would have become clear in those discussions in that meeting [on September 5] that it was, um, protected by section 16, if you will." Wilson testified that:

> My own interpretation of why it would have been logically, then, it's because it's part of the OSC review and that's why it would be covered by section 16. So I simply deduced that from why it would be covered.
>
> (Testimony of Wilson, June 20, 2013, pp. 117-119; Exhibit 13 -- Phillips and Wilson Transcripts, Tab B, pp. 111-130)

[217] Hyatt, the Chair of the FLWM Board, testified that the ability to disclose the Grant Thornton Report was discussed at the September 5 Board Meeting. Hyatt said that he understood that the report was confidential. Hyatt explained that Dunne had said that the Grant Thornton Report formed part of the Commission's investigation, and as a consequence, the report could not be disclosed. (Testimony of Hyatt, June 24, 2013, pp. 17 and 37)

[218] Hyatt testified that at that September 5 Board Meeting, Dunne did not give advice that, on the one hand, First Leaside could sell, for example Special Notes, without, on the other hand, disclosing the Grant Thornton Report at that time. As Hyatt said, "I'm not sure that issue came up in that way." Similarly, at the September 5 Board Meeting, Dunne did not give advice that First Leaside could sell, for example, FLEX LP, without disclosing the Grant Thornton Report. As Hyatt stated, "I don't know that he connected those two things. We were simply told that the report could not be disclosed." (Testimony of Hyatt, June 24, 2013, p. 37)

[219] While the minutes of the September 5 Board Meeting do not refer to it, Hyatt testified that at that meeting, there were discussions about whether FLG was permitted to raise capital. Hyatt indicated that the discussions with respect to whether or not FLG was permitted to raise capital arose in the context of the WALP Undertaking, which was relevant to the $5 million Special Financing. Hyatt testified that he was not certain at the time of the September 5 Board Meeting whether the Phillips' Undertaking was still in effect. Hyatt testified that he had asked Phillips whether there were any other restrictions on raising capital, and Phillips said there were none. Hyatt said that no one else at that meeting, including Dunne, provided any advice on that issue. According to Hyatt, Dunne did not contribute to the discussion in respect of capital raising, other than with regard to the $5 million Special Financing, nor did he give any advice in regard to FLG's projected sales or future sales efforts.

[220] Dunne, on the other hand, testified directly that he never provided an opinion letter or email in which he connected two things: (i) that First Leaside could not disclose the Grant Thornton Report; and (ii) that First Leaside could go ahead and sell its LPs and Funds in those circumstances. Dunne testified firmly that "I was not asked for an opinion." (Testimony of Dunne, June 24, 2013, p. 105)

[221] Dunne testified, without hesitation, that at the September 5 Board Meeting, he did not give FLG advice that First Leaside could sell Special Notes without disclosing the Grant Thornton Report. Dunne stated that I wasn't asked, didn't give." Dunne said he similarly did not give advice that FLG could sell FLEX LP, or any other LP or Fund sold in September and October 2011, without disclosing the Grant Thornton Report. (Testimony of Dunne, June 24, 2013, pp. 101-102 and p. 104)

[222] In the Hyatt Affidavit, Hyatt stated that he was surprised by Dunne's evidence in respect of the disclosure of the Grant Thornton Report. Hyatt stated that he recalled Dunne giving advice at the September 5 Board Meeting and reiterating the advice during the November 13, 2011 Meeting. Neither the minutes of the September 5 Board Meeting nor the minutes of the November 13, 2011 Meeting record or reflect Dunne giving any legal advice or opinion that FLG could not disclose the Grant Thornton Report or that FLG could sell its LPs and Funds without disclosing the Grant Thornton Report. The minutes of the November 13, 2011 Meeting do contain a sentence that does note that "the Corporation was precluded from disclosing to investors the Grant Thornton Report or the [OSC] investigation that gave rise to the [Grant Thornton] Report"; that note however, is not attributed to Dunne or anyone in particular in those minutes and is placed after a sentence that sets forth a discussion of the Independent Committee.

[223] In addition, Collins testified that at the September 1, 2011 Meeting, she did not recall any discussion concerning the disclosure of the Grant Thornton Report nor did she recall a discussion about a "gag order" that would prevent the discussion or disclosure of the Grant Thornton Report to FLG Investors. (Testimony of Collins, June 7, 2013, p. 124)

[224] We find that the Respondents did not produce any evidence of a legal opinion or advice in the minutes of the September 5 Board Meeting which was held during the Sales Period, or any other evidence to substantiate a defence of reliance on legal advice other than their own testimony and that of Hyatt as to his recollection that advice was given. This was directly contradicted by the testimony of Dunne, the lawyer whom they said had provided the legal opinion and advice; Dunne, on the other hand, testified firmly that he was not asked for an opinion and never provided the alleged opinion or advice. We accept the testimony of Dunne on this point that he did not provide any legal advice or opinion that FLG could not disclose the Grant Thornton Report or that FLG could sell its LPs and Funds without disclosing the Grant Thornton Report.

[225] *In Springer v. Aird & Berlis LLP* (2009), 96 O.R. (3d) 325 ("***Springer***"), the Court held that the "most satisfactory judicial test of truth lies in its harmony or lack of harmony with the preponderance of probabilities disclosed by the facts and circumstances in the conditions of the particular case". (*Springer*, supra at para. 14 citing *R. v. Pressley* (1948), 94 C.C.C. 29). In cases where there is conflicting testimony and where the trier of fact is deciding whether a fact occurred on a balance of probabilities,

> provided the judge has not ignored evidence, finding the evidence of one party credible may well be conclusive of the result because that evidence is inconsistent with that of the other party. In such cases, believing one party will mean explicitly or implicitly that the other party was not believed on the important issue in the case.
>
> (*McDougall, supra*, at para. 86)

[226] We made assessments of the credibility of the witnesses who testified before the panel. As we have stated above, we accept as credible the testimony of Dunne that he did not provide any legal advice or opinion that FLG could not disclose the Grant Thornton Report or that FLG could sell its LPs and Funds without disclosing the Grant Thornton Report. As we have noted above, there was no evidence of a legal opinion or advice on this issue in the minutes of the September 5 Board Meeting or the November 13, 2011 Meeting. We do not accept as credible the testimony of Phillips and Wilson, with respect to having received such legal advice or opinion from Dunne.

[227] Accordingly, we find that legal advice in respect of non-disclosure of the Grant Thornton report was not given by Dunne during the Sales Period. As such, the Respondents cannot rely on reliance on legal advice as a defence. Therefore, the test set out in *Mega-C Power Corp.* is not applicable.

B. Did the Respondents, Phillips and Wilson, each make statements that a reasonable investor would consider relevant in deciding whether to enter into or maintain a trading or advising relationship, which statements were untrue or omitted information necessary to prevent the statements from being false or misleading in the circumstances in which they were made, contrary to subsection 44(2) of the Act and contrary to the public interest?

i. The Applicable Law

[228] Subsection 44(2) of the Act provides that:

> *No person or company shall make a statement about any matter that a reasonable investor would consider relevant in deciding whether to enter into or maintain a trading or advising relationship with the person or company if the statement is untrue or omits information necessary to prevent the statement from being false or misleading in the circumstances in which it is made.* 2009, c. 18, Sched. 26, s. 9.

[229] In *Re Winick,* the Commission articulated the test to make a finding that a person or company has breached subsection 44(2) as requiring that the panel must be satisfied that:

> the respondent made a statement about a matter that a reasonable investor would consider relevant in deciding whether to enter into or maintain a trading or advising relationship with the respondent, which is untrue or omits information necessary to prevent the statement from being false or misleading in the circumstances.
>
> (*Re Winick* (2013), 36 O.S.C.B. 8202 at para. 156)

[230] In *Re Carter*, a decision of the Director of the Commission found marketing materials of an entity affiliated with Carter Securities Inc. violated subsection 44(2) of the Act since the materials contained statements that were "misleading, unsupported or not accurate" (Re *Carter Securities Inc*. (2010), 33 O.S.C.B. 8691 ("***Carter***") at para. 53 and 74).

ii. Analysis and Findings

[231] This panel finds that during the Sales Period, each of the Respondents made statements with respect to FLG that a reasonable investor would consider relevant in deciding whether to enter into or maintain a trading or advising relationship with each of the respondents, which statements were untrue or omitted information necessary to prevent the statements from being false or misleading in the circumstances.

[232] In deciding whether each of Phillips and Wilson breached subsection 44(2) of the Act, we considered whether the statements made by each of Phillips and Wilson to existing and prospective FLG investors were relevant to a reasonable investor in deciding whether to enter into or maintain a trading or advising relationship with each of the Respondents, respectively, and whether the statements were untrue or omitted information necessary to prevent the statements from being false or misleading in the circumstances. We also considered the marketing materials provided by the Respondents, including (i) the PowerPoint Slide Presentation at the September 17 WALP AGM, (ii) the FLG website during the Sales Period, (iii) Wilson's Group Email, as well as the evidence of FLG Sales Investors as to their reaction to learning of the Grant Thornton Report after the Sales Period.

The PowerPoint Slide Presentation at the September 17, 2011 WALP AGM

[233] The PowerPoint slide presentation made by Phillips at the September 17, 2011 WALP AGM contained the following statements:

> The time for new opportunities appears as we approach a market 'bottom'.
>
> Because of our sound financial position, and strategy of maintaining no stock market risk, the partnership's exposure to market risk is unchanged. In fact, the partnership can now entertain a brand new suite of options and opportunities.
>
> (Exhibit 19 -- Respondents' Hearing Brief, Tab 40, p. 6)

[234] Phillips testified that this was his position at that time.

[235] During the Sales Period, Phillips made representations that it was "business as usual" to Mr. M. and at the September 17, 2011 WALP AGM.

[236] Phillips also reported at the September 17, 2011 WALP AGM to FLG Investors that "sales had never been better" while the evidence indicates that he was, at that time, funneling new investor money indirectly into WALP to keep it afloat; that use of investor money was not disclosed by Phillips to new investors during the Sales Period and was contrary to the recommendation of the Grant Thornton Report.

[237] The minutes of the September 5 Board Meeting disclose that Phillips asked Dunne why FLWM, if it is allowed to raise capital, cannot invest its capital in WALP. Dunne explained that the OSC would likely be concerned that by allowing FLWM to invest in WALP, "FLWM investors take disproportionate risk as FLWM is already significantly invested in WALP."

[238] We find that Phillips made representations that WALP and FLG had a "sound financial position" and it was "business as usual" to FLG Sales Investors in order to induce them to purchase units of the FLG entities. We are troubled that Phillips made representations to investors that WALP and FLG had a "sound financial position" and it was "business as usual" at FLG during the Sales Period. In light of the conclusions made in the Grant Thornton Report, these statements were untrue or omitted information necessary to prevent the statements from being false or misleading in the circumstances. As the directing mind of FLG, Phillips knew that the Grant Thornton Report disclosed that it was anything but "business as usual" at FLG because the recommendations in the Grant Thornton Report indicated that FLG's financial viability is contingent on the ability of FLG to raise the Special Financing to prevent a cash flow deficiency, that FLG stop the movement of funds, that new funds be siloed within each of the new investment entities and the Base Model represented "a major or drastic departure from the manner in which [FLG] conducted business in the past". (Testimony of Krieger, June 7, 2012, p. 72) We were not provided evidence that FLG or FLG Management took reasonable actions to change the way they did business and to implement the recommendations in the Grant Thornton Report.

FLG Website Marketing Material

[239] We find that the marketing materials set forth on the FLG website contained statements that were untrue or omitted information necessary to prevent the statements from being false or misleading in the circumstances. The FLG website included statements such as:

- "One of Canada's Fastest Growing Real Estate Portfolios". (Testimony of Krieger, June 7, 2013, p. 137);

- "With an 18-year track record, First Leaside proved that buying underperforming D grade properties in established neighborhoods and then repositioning them in the market could be very profitable". (Testimony of Krieger, June 7, 2013, p. 137);

- "Since 1992 First Leaside Limited Partners have received continuous monthly cash distributions." (Testimony of Krieger, June 7, 2013, p. 137); and

- "Exceptional investment Return Over the Past Two Decades" (Testimony of Krieger, June 7, 2013, p. 138)

[240] However, the reality was that the valuation of the FLG properties was less than the total amount outstanding under the mortgages and the promissory notes issued by FLG. This meant that the liabilities of FLG were greater than the assets of FLG and FLG had to service that debt, but the cash flow of FLG was negative. This was a solvency issue. (Testimony of Collins, June 10, 2013, pp. 43-44).

[241] In the balance sheet of the financial statements of WALP dated December 31, 2009 (Exhibit 2 -- Hearing Brief, Volume 1, Jonathan Krieger), under "WALP Liabilities", Collins said that there were mortgages payable of $50,077,299 and the promissory notes payable add up to $46,427,226 making the total of those two liabilities approximately $96.5 million. (Testimony of Collins, June 7, 2013, p. 97) while the valuation of the properties added up to either $58.0 million at the low end or $68.8 million at the high end (Testimony of Collins, June 7, 2013, pp. 98-99).

[242] Collins told the panel that Staff noted that:

> "Grant Thornton had identified significant financial reporting and corporate governance concerns, including a failure to provide adequate and timely financial statements."

It appears that these concerns were not disclosed to investors by FLG. (Testimony of Collins, June 7, 2013, pp. 140-141)

[243] Wilson described the websites as a very effective marketing tool. On its websites, captured on October 21, 2011, FLG indicated that it had "One of Canada's Fastest Growing Real Estate Portfolios" and "Continuous monthly cash distributions since 1992." The marketing material also referred to FLG's "exceptional investment return over the past two decades…allowing us continued access to additional investment capital." The FLG paper marketing materials said that the valuation of the assets or the properties held by WALP were worth over $100 million whereas the valuations of the WALP properties were in fact not more than $68.8 million. (Testimony of Collins, June 7, 2013, pp. 97-99). We find that all these statements made, *inter alia*, on marketing materials, were misleading, unsupported or not accurate.

Wilson's Group Email

[244] On September 9, 2011, Wilson sent Wilson's Group Email to investors trying to drum up sales in the Special Notes LP and Venture LP offerings. Wilson described the Special Notes LP and Venture LP offerings, as "compelling investment opportunities [for] our partners." Wilson also described the 10.1% per annum interest rate and other attributes of the Special Notes LP offering and advised "If you have an interest, contact me for further detail. There is limited supply, and we expect to be fully subscribed rather quickly." (Testimony of Wilson, June 20, 2013, pp. 107-110; Exhibit 7 -- Hearing Brief: Lists of Sales during Sales Period and Marketing Material, Tab 2)

[245] In respect of the Venture LP offering, Wilson wrote:

> For partners who can utilize a substantial tax deduction in 2011 and 2012, this new LP is ideal! This has the potential to be our best deal in 20 years, given the high deductions, and the substantial portfolio of real estate acquired. (Renovations for several retirement properties will provide the deductions).
>
> (Testimony of Wilson, June 20, 2013, pp. 107-110; Exhibit 7 -- Hearing Brief: Lists of Sales during Sales Period and Marketing Material, Tab 2)

[246] We find that during the Sales Period, Wilson induced Dr. Z. to invest in FLG by offering 5 percent bump investment incentives that he knew that FLG could not meet. Wilson also represented to Dr. Z. and Mrs. Z. that they had to reinvest the funds in FLG since they did not have

an opportunity to take the money out (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, pp. 78-79). Both Dr. Z. and Mrs. Z. wanted to take out $15,000 because they wanted to do some renovations to their home but were told by Mr. Wilson that they were not allowed to take out any money because in order to get the 5 percent bump "it was either all or none" because all of the money had to be reinvested in the fund. (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, pp. 50-51). In reality, the Grant Thornton Report concluded that FLG Group did not have sufficient cash to repay existing investors and had to keep raising capital in order to try to be viable.

[247] We find that based on the evidence, FLG Sales Investors did not understand the financial situation at FLG, particularly with respect to WALP. We find that FLG Sales Investors were not informed as to the type of company they were investing in. We find that they believed what they were told by Phillips and Wilson, including in FLG marketing materials, at the September 17, 2011 WALP AGM and in the sales pitches.

[248] We find that, on a balance of probabilities, each of the Respondents made statements about FLG that a reasonable investor would consider relevant in deciding whether to enter into or maintain a trading or advising relationship with the respective Respondent. We also find that, in making those statements, without disclosing the current state of FLG, in light of the findings and recommendations in the Grant Thornton Report, the Respondents each made statements that were untrue or omitted information necessary to prevent their respective statements from being false or misleading in the circumstances in which they were made. The actions of the Respondents constitute breaches of subsection 44(2) of the Act and were contrary to the public interest.

C. Did the Respondents, Phillips and Wilson each fail to deal fairly, honestly and in good faith with their clients, contrary to section 2.1 of Commission Rule 31-505 and contrary to the public interest?

i. The Applicable Law

[249] Section 2.1 of Commission Rule 31-505 – *Conditions of Registration* provides that every registrant, whether corporate or individual, has a statutory obligation to deal fairly, honestly and in good faith with clients. Section 2.1 states :

> (1) *A registered dealer or adviser shall deal fairly, honestly and in good faith with its clients.*
>
> (2) *A representative of a registered dealer or a registered adviser shall deal fairly, honestly and in good faith with his or her clients.*

ii. Analysis and Findings

[250] This panel finds that each of Phillips and Wilson, as registrants, had a duty to deal fairly, honestly and in good faith with FLG Sales Investors, who were their clients, and that each of the Respondents failed to meet that duty. Accordingly, each of the Respondents contravened 2.1(2) of Commission Rule 31-505 during the Sales Period and in so doing acted contrary to the public interest. The Respondents did not take appropriate steps to discharge their obligations as registrants with integrity and, as the ultimate designated person and directing mind of FLG,

Phillips failed to promote a culture of compliance with securities law at FLG.

[251] The Commission is given the responsibility by statute to "provide protection to investors from unfair, improper or fraudulent practices" and to "foster fair and efficient capital markets and confidence in capital markets" (section 1.1 of the Act). The Act stipulates that the "primary means" for achieving its purposes include "requirements for the maintenance of high standards of fitness and business conduct to ensure honest and responsible conduct by market participants" (section 2.1 of the Act, clause 2(iii)).

[252] Registrants act as gatekeepers of the integrity of the capital markets. They should not, by act or omission, facilitate conduct that brings the market into disrepute. As part of their gatekeeper role, registrants shall deal fairly, honestly and in good faith with clients. (Companion Policy to NI 31-103CP)

[253] The Respondents submit that section 2.1 "is no more than a generic statement of the duty of care of dealers and advisers." (Opening submissions of the Respondents dated June 5, 2012 at p. 18 para. 64) and that "if there was no requirement to disclose the Undisclosed Facts, then there is no basis to make finding of a breach of the duty of care of dealers and advisers". The Panel rejects the Respondents' submission. The duty to act fairly, honestly and in good faith "goes to the heart of what securities regulation is about and a breach of this obligation is especially serious." (*Re Norshield Asset Management (Canada) Ltd.* (2010), 33 O.S.C.B. 7171 at para. 79)

[254] Registrants hold positions of trust in the securities industry and towards their clients, creating a responsibility on their part to fulfill an important role directed towards the protection of investors and fostering fair and efficient capital markets and confidence in capital markets. (*Re Sawh* (2012), 35 OSCB 7431 ("***Sawh***") at para. 309). It is:

> …through the registration process, the Commission attempts to ensure that those who trade in securities meet the applicable proficiency requirements, are of good character, satisfy the appropriate ethical standards and comply with the Act. (*Re Limelight Entertainment Inc.* (2008), 31 OSCB 1727 ("***Limelight***") at para. 135)

[255] In *Re Cartaway Resources Corp.*, (2000) BCSECCOM 88 ("***Cartaway Resources***"), the B.C. Securities Commission held:

> …..that conduct by market participants that results in breaches of the letter and spirit of securities legislation is conduct that brings the capital markets into disrepute and undermines public confidence in the system. It is particularly egregious where it is demonstrated that registrants have taken advantage of their position and have been deceitful and misleading…
>
> (*Cartaway Resources*, supra at para. 239)

[256] Registration is a privilege and not a right, which is granted to individuals and entities that have demonstrated their suitability for registration (*Sawh*, supra at para. 142). Registrants have an obligation to act fairly, honestly and in good faith with their clients. This is an important standard and requires registrants to put the interests of their clients first. To participate in the capital markets in Ontario requires a registrant to embrace this standard.

Phillips

[257] Phillips testified that he understood that as a registrant, he had a duty to deal fairly, honestly, and in good faith with his clients. He understood that as a registrant, he had an obligation to his clients to make sure that they had all of the relevant facts and information they needed in order to decide whether to invest. Phillips also agreed that the other registrants he supervised in his role as UDP, including Wilson, had the same duty of honesty, and the same duty to all clients to ensure that they had the relevant information they needed to make an investment decision. However, his actions showed that he withheld important information from FLG Sales Investors and his Sales Team. (Testimony of Phillips, June 19, 2013, pp. 103-106; Exhibit 4 -- Hearing Brief: Corporate and Registration Documents, Tab 9)

[258] Phillips also testified that he understood the role as UDP to be very important and, and that as the UDP of a securities firm, he was responsible for supervising the firm's activities to ensure that everyone was compliant with securities law, and for promoting compliance with securities legislation by the firm and individuals acting on its behalf. (Testimony of Phillips, June 19, 2013, p. 7 and pp. 99-100; Exhibit 4 -- Hearing Brief: Corporate and Registration Documents. Tab 9)

[259] Phillips was aware of the findings of the Grant Thornton Report and failed to disclose those findings to existing and potential FLG Investors. Those findings were important and relevant for investors to make investment decisions. Phillips represented to investors during the Sales Period that it was "business as usual", notwithstanding that the Base Model, findings and recommendations of the Grant Thornton Report would be "a major or drastic departure" from FLG's way of doing business.

[260] Notwithstanding Phillips's testimony that he understood his duty as a registrant and role as UDP, we find that Phillips' actions (as discussed above) during the Sales Period demonstrated his disregard of this duty. We find that Phillips failed to deal fairly, honestly and in good faith with FLG Investors who were his clients and thereby contravened Section 2.1(2) of Commission Rule 31-505 during the Sales Period and in so doing acted contrary to the public interest.

Wilson

[261] Wilson testified that in his previous career selling industrial machinery, he had a duty of candour and honesty toward his clients. Wilson testified that he understood that as a registrant, he had a duty to act fairly, honestly and in good faith with his clients. He also understood that his duty included an obligation to his clients to make sure that they had all of the relevant facts they needed in order to decide whether to invest. Wilson agreed that this was a higher duty than the one he had as a salesperson of industrial machinery, because as a registrant, he was often dealing with someone's life savings, and their investment decisions could impact them profoundly, including in respect of whether or when they could retire. (Testimony of Wilson, June 20, 2013, pp. 87-89 and p. 98)

[262] Notwithstanding Wilson's understanding of his duty as a registrant, which included an obligation to make sure that his clients had all of the relevant facts they needed to decide whether to make an investment decision, we find that Wilson deceived and misled FLG Investors during the Sales Period by (i) creating the impression that "the company [was] doing fantastic," (ii) continuing to raise funds from FLG Investors, and (iii) ensuring that their maturing investments were not withdrawn. Even though Wilson knew about the questionable viability of FLG, as

disclosed in the Grant Thornton Report, Wilson encouraged Dr. Z. to invest additional funds in FLG products stating:

> "if you have any -- anything more to invest, we have this great product coming out. It's going to pay 10 percent. You will only be exposed for a year."

Wilson also offered a "bump" to Dr. Z. and Mrs. Z. if they rolled over all of their existing investments. (Testimony of Dr. Z. and Mrs. Z., June 12, 2013 pp. 42-46)

[263] On October 13, 2011, Dr. Z. and Mrs. Z. invested a total of $315,000 in FLEX LP under "Canadian Investment Accounts" (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 49). The source of the funds was a rollover from their previous investments in other FLG securities. (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 49-50). Mrs. Z. testified that they were unaware of what purpose their funds were being used for, however, they were aware that some of the funds were getting transferred and assumed that it was to make more money for FLW using their RRSP. (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 74). Mrs. Z. testified that she did not know that she was purchasing Wimberly Fund. She believed that she was investing $930,000 in the compounding interest fund. Mrs. Z. testified that John Wilson, her advisor, told her so. (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p.32) The risk factors in the cash margin and other accounts of Dr. Z. was 50 percent medium and 50 percent high risk on the form, however, Mrs. Z. told Staff that at the time they had filled out the form, the discussion with Wilson in 2007 was about their registered RRSPs, where they wanted 65 percent, low risk, 20 percent, medium risk, and 15 percent to be high risk for their investment profile. (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 67). Dr. Z. and Mrs. Z. were unaware of the change in their risk profile and confirmed that they would not have agreed to it. (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, pp. 68-69).

[264] Dr. Z. testified that "we did not think that we were invested in the States." (Testimony of Dr. Z. and Mrs. Z., June 12, 2013, p. 13)

[265] In *Re Marchment*, the Commission stated:

> The duty to know the client's investment objectives, financial means and personal circumstances, and to recommend only those investments which are suitable for the client is fundamental to the obligation of every dealer and registered representative dealing with the public.
>
> (*Re Marchment & Mackay Ltd.*, 1999 Carswell Ont 5644 at para. 13)

[266] In light of the detailed findings on the viability of FLG as disclosed in the Grant Thornton Report, we find that Wilson sold FLG Sales Investors investments which were not suitable for their investment objectives. As a registrant, Wilson knew the risks associated with investments in an entity that Grant Thornton had recently identified as having a $132.1 million equity deficit to equity holders of the FLG Entities (Testimony of Krieger, June 6, 2013, pp. 102 and 104) and whose viability was questionable. As a registrant, and in fulfilling his duty to act fairly, honestly and in good faith, Wilson ought to have explained and disclosed these facts to FLG Sales Investors as part of his obligation to determine whether the investments were suitable for FLG Sales Investors. Instead, Wilson misrepresented the level of risk associated with the investments during the Sales Period and in so doing, Wilson failed to act fairly, honestly and in good faith.

[267] We also find that the FLG Sales Investors were vulnerable because of their lack of investment knowledge and we accept their evidence that they relied on the advice of Wilson. We also find that this was or should have been evident to Wilson. While we recognize that clients have responsibilities to understand the potential risks and returns on their investments, this does not relieve Wilson of his duty as a registrant to make certain that investors have this understanding and to make appropriate recommendations, especially in circumstances where he is dealing with investors who have relatively little investment experience. (*Re Daubney* (2008), 31 O.S.C.B. 4817 at para. 201) The Respondents provided no evidence that they discussed the risks of investing in FLG products during the Sales Period with FLG Sales Investors.

[268] Notwithstanding Wilson's testimony that he understood his duty as a registrant, we find that Wilson's conduct (as discussed above) during the Sales Period demonstrated his failure to fulfill his obligations. We find that Wilson failed to deal fairly, honestly and in good faith with FLG Investors who were his clients and thereby contravened Section 2.1(2) of Commission Rule 31-505 during the Sales Period and so doing acted contrary to the public interest.

[269] We also find that the Respondents, by favouring their own interests to raise additional capital for FLG, prejudiced FLG Investors. The conduct of the Respondents, in not disclosing the risks associated with an investment in FLG products, including (i) the $132.1 million equity deficit to equity holders of the FLG Entities, (ii) the cash flow deficiency of approximately $15.9 million over the three-year period of 2011 to 2013, and (iii) the viability of FLG, the Respondents' conduct constituted a breach of their duties as gatekeepers of the integrity of the capital markets.

[270] Each of the Respondents had a duty to conduct themselves with integrity and have an honest character. However, in engaging in a course of conduct that perpetrated a fraud on investors, the Respondents did not conduct themselves with integrity and acted contrary to the public interest.

7. CONCLUSION

[271] For the reasons stated above, we find that each of the Respondents:

(a) breached subsection 126.1(b) of the Act;

(b) breached subsection 44(2) of the Act;

(c) breached section 2.1 of Commission Rule 31-505; and

(d) acted contrary to the public interest.

[272] An order will be issued as follows:

(i) Staff shall serve and file written submissions on sanctions and costs by 4:00 p.m. on February 18, 2015;

(ii) The Respondents shall serve and file responding written submissions on sanctions and costs by 4:00 p.m. on March 25, 2015;

(iii) Staff shall serve and file reply written submissions on sanctions and costs (if any) by 4:00 p.m. on April 15, 2015;

(iv) the hearing to determine sanctions and costs will be held at the offices of the Commission at 20 Queen Street West, 17th floor, Toronto, ON, on May 11, 2015 at 10:00 a.m., or such further or other dates as agreed by the parties and set by the Office of the Secretary; and

(v) upon failure of any party to attend at the time and place aforesaid, the hearing may proceed in the absence of that party, and such party is not entitled to any further notice of the proceeding.

DATED at Toronto this 14th day of January, 2015.

"Edward P. Kerwin"	*"C.W.M. Scott"*
Edward P. Kerwin	C.W.M. Scott