

INVESTIGATION REPORT

Date: October 23, 2013
Client: Mrs. O
Firm: Keybase Financial Group Inc. (Keybase)

CONFIDENTIALITY

This report is intended solely to assist the client and firm (the parties) in resolving their dispute and is not intended for broader use, circulation or publication. This document and its content is not to be provided to or discussed with anyone other than the parties and their professional advisors such as lawyers and accountants, if any, without prior written consent of the Ombudsman. The parties are reminded of their confidentiality obligations to the Ombudsman set out in the Consent Letter completed on November 9, 2010. The contents of our report are not intended to be, nor should they be interpreted to be, legal advice or opinion.

INVESTIGATION SUMMARY

Investment Advisor:	<ul style="list-style-type: none"> ▪ Mr. N 	
Account/Product:	<ul style="list-style-type: none"> ▪ Off-book mortgage investments in Locked-In Retirement Account (LIRA) 	
Period:	<ul style="list-style-type: none"> ▪ February 2003 to April 2010 	
Key Conclusions:	<ul style="list-style-type: none"> ▪ Mr. N recommended Mrs. O invest \$40,000 in a mortgage investment. The investment was made off of Keybase's books and records. However, Mrs. O reasonably believed it was approved by and made through Keybase. The mortgage investment was later lost. ▪ Mr. N made another mortgage investment for \$67,500 for Mrs. O without her authorization or knowledge, also off Keybase's books and records. This investment was also lost. ▪ Keybase is responsible for most of Mrs. O's losses although Mrs. O bears some responsibility for the loss on the first mortgage investment. 	
Recommendation:	\$71,636	Compensable losses
	\$2,248	Interest
	\$73,884	Total recommendation

STANDARD OF REVIEW

OBSI is obligated to assess and resolve complaints using a fairness standard, as set out in OBSI's Terms of Reference:

The Ombudsman shall make a recommendation or reject a Complaint with reference to what is, in the Ombudsman's opinion, **fair** in all the circumstances to the Complainant and the Participating Firm. In determining what is fair, the Ombudsman shall take into account general principles of good financial services and business practice, law, regulatory policies and guidance, professional body standards and any relevant code of practice or conduct applicable to the subject matter of the Complaint. (Emphasis added.)

While OBSI considers the rules and standards developed by other bodies, including regulatory bodies like the Investment Industry Regulatory Organization of Canada (IIROC) and the Mutual Fund Dealers Association of Canada (MFDA), the focus for OBSI is on what is fair between the parties in the particular circumstances. Therefore, OBSI's conclusions will not necessarily be the same as conclusions drawn by another body bound by specific rules or subject to a different standard.

OVERVIEW

Mrs. O had been a client of Mr. N since 1999 when she invested a \$74,752 retirement allowance in a new LIRA. She had no previous investment experience. In 2003, Mr. N changed firms and Mrs. O followed him. She opened an account at Keybase and transferred her investments.

In September 2003, Mr. N recommended Mrs. O invest part of her LIRA in a mortgage investment, which she says he described as safe and income-producing. The investment was actually a private mortgage on which Mrs. O was the second mortgagee. Mr. N arranged the mortgage investment off of Keybase's books and records, and Keybase was not immediately aware of it. In November 2004, Mrs. O received notice that the first mortgagee had filed for foreclosure. By February 2005, the foreclosure was complete and Mrs. O lost her investment.

Despite her losses on the private mortgage, Mrs. O continued to trust Mr. N and remained invested with him. In October 2006, Mr. N sold Mrs. O's remaining LIRA investments and invested the proceeds in another mortgage investment. The evidence supports Mrs. O's assertion that her signatures were forged and that she did not know of, or authorize, these trades. This mortgage investment was also arranged by Mr. N off Keybase's books and records. Mrs. O lost this investment as well.

Mrs. O has lost almost her entire LIRA investment. She complained to Keybase about the irregularities in her account and the money she lost. Keybase denies responsibility for compensating Mrs. O. It takes the position that she was aware of the trades and mortgage investments made on her behalf, must have understood the risks and is

responsible for the ensuing losses. Our investigation indicates, to the contrary, that Mrs. O was not a knowledgeable investor, that she trusted and relied heavily on Mr. N, and that she was unaware of the risks of the first mortgage investment. Also, because Mr. N redirected her account statements to his own postal box, she knew nothing of the second mortgage investment until years later.

Keybase further contends it was not involved in the mortgage investments and argues it could not supervise Mr. N with respect to them. However, when Mr. N was registered with Keybase, the Ontario Securities Commission imposed conditions on his registration that required Keybase to closely supervise his activities. Our investigation shows that Keybase had several opportunities to prevent both mortgage investments from ever happening.

For the reasons outlined in this report, Keybase should accept its responsibility and compensate Mrs. O for her losses.

BACKGROUND

- In 1999, Mrs. O received a lump sum payment from her former employer which she invested with Mr. N while he was an advisor at another investment firm. She says she was referred to Mr. N by a former colleague, Ms. S, who is Mr. N's sister.
- Mrs. O had never held an investment portfolio before and she says she was impressed with Mr. N's years of experience working with different financial institutions. She says he gave her the impression he was "excellent at what he did." She was enticed to become his client due in part to an illustration he prepared in March 1999, showing that her initial \$74,752 deposit invested to earn a 12% annual return would produce \$291,255 in retirement savings over 12 years. She says Mr. N told her he would initially invest her in mutual funds and would propose other good investments from time to time to help her achieve this goal.
- In December 1999, Mrs. O moved from Ontario to Alberta, where she held several administrative jobs. Mrs. O says that in 2001 she started working as an unlicensed assistant to a commodities broker and that her duties included filing, faxing, photocopying, preparing mailings, taking calls and transferring them to the broker.
- Mrs. O says that from the time she starting investing with Mr. N in 1999 until 2003, her investments increased in value. As a result, she believed Mr. N had given her good investment advice. She says she grew to trust him, relied solely on the information he shared with her about his investment recommendations and always followed his advice.
- On February 18, 2003, Mr. N changed employers and became an advisor at Keybase, a mutual fund dealer. The Ontario Securities Commission (OSC) placed a number of conditions on Mr. N's registration including, among others, that he could only sell mutual funds, he could not have business dealings with clients outside the sale of mutual funds, that Keybase would supervise and approve all of Mr. N's activities (often referred to as close supervision), and that Keybase would report to the OSC monthly about Mr. N's activities.
- On August 25, 2003, when she was 57 years old, Mrs. O signed a Keybase New Plan Application form (NPAF) to open a LIRA with Mr. N. She also signed a Tandem Account Application for a LIRA with [Trustco #1] showing Keybase as the dealer and Mr. N as the "Financial Advisor." While she agrees she opened the Keybase account and understood that [Trustco #1] would administer the account, she disputes the signatures on both forms.
- Mrs. O lived in Alberta while she was a Keybase client. Mr. N was not registered to service clients residing in Alberta. Mrs. O says that Mr. N asked her to provide him with an Ontario address as he did not want to send mail to Alberta. She says she trusted him and understood "this is the way he does it" so she "did what he asked." While she was a Keybase client, Mrs. O was documented as having various Ontario

addresses, one of which she says was a post office box set up by Mr. N to receive mail for out of town clients. Mrs. O says she received a few account statements in 2003 but none from 2004 to 2008.

- On September 15, 2003, \$78,653 in cash was transferred from her previous investment firm into the LIRA administered by [Trustco #1]. On September 17, 2003, the cash was used to purchase five mutual funds, including \$40,900 of Mackenzie Sentinel Cash Management fund. On September 26, 2003, the fund was sold. On September 30, 2003, on Mr. N's recommendation, Mrs. O invested \$39,957 (\$40,000 less interest adjustments of \$43) in a mortgage investment (which we will refer to as the first mortgage investment). Mrs. O was shown on the mortgage documents as the second mortgagee.
- Emails from Mrs. O to Mr. N in October, November and December 2003, and February and March 2004 show that she was inquiring about her account and/or requesting updates on the account activity. Mr. N did not respond to some of Ms. O's inquiries. With regard to others, his answers were delayed, short, and included information unrelated to the questions Mrs. O asked. However, in an email from Mr. N in April 2004, he apologizes for any miscommunication and says he would send account statements. Mrs. O says she did not know much about investments and she understood that Mr. N was busy, as she was. Therefore, the short answers he provided led her to believe "everything was good."
- On January 13, 2004, Mrs. O received \$2,000 in her savings account at her bank which she says Mr. N told her represented payments on the first mortgage investment.
- On October 21 2004, the first mortgagee filed a Statement of Claim (Mortgage Action – Foreclosure) for default of principal and interest in the amount of \$62,378.
- Between November 4, 2004 and February 23, 2005, [Trustco #1] sent Mrs. O three registered letters to her daughter's Ontario address, on which Mr. N was copied:
 - The first letter dated November 4, 2004, informed her of the Statement of Claim and the time allowed to file a Statement of Defense. [Trustco #1] recommended she promptly seek legal and financial advice.
 - The second letter dated January 20, 2005, indicated that with respect to Mrs. O's recent authorization to port the mortgage to a new property, documentation was missing and had to be received by a specified date. It also stated the first mortgagee had finalized the legal action and was in a position to foreclose on the property causing her mortgage to be extinguished and removed from her LIRA. [Trustco #1] "strongly recommended" a prompt resolution of the mortgage port.
 - The last letter dated February 23, 2005, confirmed the Order for Foreclosure had been completed and registered, that Mrs. O's first mortgage investment would be extinguished and deregistered from her LIRA and that a T4RSP for \$0.00 would be issued to her for the 2005 taxation year.

All the letters gave a contact number for the [Trustco #1] mortgage department should Mrs. O require assistance.

- Mrs. O says she had a personal experience with foreclosure. In August 1997, she and her husband received a Notice of Sale Under Mortgage for defaulting on their home mortgage payments. The Os could not pay the amount due by the deadline and lost their home.
- Mrs. O says when she received the first [Trustco #1] registered letter, she contacted Mr. N right away. She says he assured her he would take care of the situation for her and told her to advise [Trustco #1] as much. On November 23, 2004, she faxed Mr. N a copy of the November 4, 2004 [Trustco #1] letter on which she handwrote “please be advised that the above is being reconciled by Mr. N.” In her fax, she asked Mr. N to forward her note to [Trustco #1], whose fax number did not appear on its letter.
- Mrs. O says she also contacted Mr. N upon receipt of each additional letter and that he consistently assured her he was resolving matters. Mrs. O says she felt comfortable dealing with this situation through Mr. N as he had recommended the investment and she was confident he would handle the situation appropriately.
- On August 19, 2005, the first mortgage investment was removed from Mrs. O’s [Trustco #1] LIRA account.
- On August 21, 2006, documents were completed by Mr. N to open a new LIRA with [Trustco #2] and to transfer the money and mutual funds in Mrs. O’s LIRA to [Trustco #2]. The [Trustco #2] documents show Keybase as the dealer and Mr. N as the “Financial Advisor.” Mrs. O says she did not see or sign these forms but she acknowledges knowing the transfer was happening. She says she understood from Mr. N it was just an administrative change.
- On October 3 and 4, 2006, \$6,806.52 of cash and six mutual funds valued at \$61,638 were transferred in-kind from Mrs. O’s [Trustco #1] LIRA to her [Trustco #2] LIRA.
- On October 10, 2006, all of Mrs. O’s mutual funds were redeemed for \$60,694. On October 13, 2006, [Trustco #2] wired \$59,688 in trust to [a financial and paralegal services firm (Firm X)] for a \$60,000 mortgage investment (\$60,000 less interest adjustments of \$312), which we will refer to as the second mortgage investment. Mrs. O was the third mortgagee. [Firm X] represented the mortgage, Ms. S, Mr. N’s sister.
- On October 16, 2006, [Firm X] wrote to [Trustco #2] saying it wished to re-write the mortgage for \$67,500 since there was more money in the LIRA than originally anticipated when the \$60,000 mortgage was established. [Firm X]’s letter included a revised mortgage application and pre-authorized payment (commonly referred to as preauthorized credit, or PAC) documents that at first glance appear to have been signed by Mrs. O and witnessed by Mr. N the day before. However, Mrs. O says she never signed any documents for the second mortgage investment.

- On October 17, 2006, [Trustco #2] advanced \$7,469 to [Firm X] in trust (\$7,500 less an interest adjustment of \$31) to add to the second mortgage investment.
- On November 14, 2006, [Trustco #2] sent [Firm X] a letter requesting documents and copied Mrs. O on its correspondence. The letter to Mrs. O came back to [Trustco #2] marked “return to sender.”
- Monthly PACs of \$562.50 were deposited in Mrs. Os’s LIRA at [Trustco #2] starting on December 1, 2006.
- Mr. B, Keybase’s Branch Manager and Alternate Compliance Officer at the time, says that on January 15, 2007, his review of a quarterly trade blotter showed transactions where mutual funds had been transferred into several Keybase clients’ registered accounts and then sold, but the proceeds appeared not to have been reinvested in a reasonable timeframe. He says he tracked the trades to [Trustco #2]. [Trustco #2] provided him with a list showing that several Keybase clients, including Mrs. O, had in fact been reinvested in second and third mortgages, which had not been processed through Keybase’s books and records. Such transactions are often referred to as “off-book.” Off-book transactions are prohibited by securities rules. As a result of the off-book transactions, Mr. N was terminated from Keybase for cause on January 18, 2007. Keybase has provided us with a generic letter to unnamed clients indicating Mr. N had been terminated and assigning a new advisor. Although we requested it, we have not received any evidence that Keybase sent the letter to Mrs. O or that if one was issued, it was sent to her correct address. Mrs. O says she never received such a letter.
- On July 16, 2007, about six months after the PACs began, [Trustco #2] sent a letter by mail to Mrs. O informing her that the \$562.50 PAC for July had been returned by the bank due to insufficient funds. Again, the letter came back to [Trustco #2] marked “return to sender.” No subsequent monthly PACs were deposited in the [Trustco #2] account.
- On October 31, 2008, one day before the second mortgage investment was due to mature, \$9,562.50 was paid to Mrs. O’s [Trustco #2] account to cover 17 months of outstanding mortgage payments. Her principal was not repaid.
- Mrs. O says that in the latter part of 2008, she learned from her son that Mr. N had “disappeared” and began doing research. Mrs. O says her son had done some website design for Mr. N but the cheque he received for payment was returned due to insufficient funds. She says her son tried to locate Mr. N, but believed he had left the country. Correspondence shows Mrs. O was contacting Keybase and [Trustco #2], to try to track down what happened with her investments.
- Mrs. O says she learned of the second mortgage investment in 2009 through documentation she received from [Trustco #2], including mortgage documents showing Ms. S, a former colleague, as the mortgagee. [Trustco #2] advised Mrs. O that interest was paid up to November 1, 2008 (this was the loan’s maturity date).

Mrs. O says that after learning of this mortgage investment, she tried to communicate with Mr. N at his business and residential addresses and she spoke with his spouse by telephone. She was shocked to see Ms. S’s name on the documents because she knew her personally. She tried to contact Ms. S and her spouse by email and text message in an attempt to get them to “make good” on the mortgage investment. She also complained to [Trustco #2].

- Mrs. O says Mr. N communicated with her by email on a few occasions and then stopped. While the emails we have seen show that several of Mrs. O’s emails appear unanswered, on May 25, 2009, Mr. N emailed her from his personal email account saying “It seems that the updating of the arrears and a renewal for a short term is all that’s necessary. I will read carefully and be in touch during the day today. I must make my way down town (sic) for a meeting this morning. Mr. N.” Mr. N also emailed Mrs. O on June 5, 2009 attaching a Report to Mortgage Lender dated December 6, 2006 and other documents related to the second mortgage investment. He requested that she reply to the email “confirming you have received the attachment and that I have your authorization to retain Mr. F to address all areas of the S / O / [Trustco #2] file.” She did not provide such an authorization and instead complained to [Trustco #2]. About eight months after her June 2009 complaint, [Trustco #2] told Mrs. O her complaint pertains to and should be made to Keybase. Shortly after, she complained to Keybase.
- The [Trustco #2] records show that Mrs. O’s account received a total of \$13,500 (\$562.50 * the 24 months of the term of the second mortgage investment) in monthly payments up to October 2008 on the second mortgage investment less fees, leaving \$12,318.69 in her [Trustco #2] LIRA.
- We calculate Mrs. O’s total loss on the two mortgage investments as \$92,795, detailed in the table below:

Table 1: Mrs. O’s Loss

First mortgage investment	\$39,957
Plus: Second mortgage investment (\$59,688 + \$7,469)	\$67,157
Total Mortgage Investment	\$107,114
Less: income from first mortgage investment	\$2,000
Less: net income from second mortgage investment	\$12,319
Total Loss	\$92,795

COMPLAINT

- Ms. O first complained to [Trustco #2] in June 2009 and she was redirected by [Trustco #2] to Keybase in February 2010. Mrs. O says that although she requested information from both Keybase and [Trustco #2] in late 2008 and/or early in 2009, she received detailed documentation from [Trustco #2] first so she complained to [Trustco #2] about it.

- On April 29, 2010, Mrs. O wrote to Keybase saying:
 - She had been in communication with Mr. B to gather information about the account she held at Keybase, its status and value;
 - Her signatures were falsified on some documents; and
 - There was an unauthorized mortgage investment and money was missing from her account.
- Mrs. O did not specify the amount of compensation she was seeking.

KEYBASE'S RESPONSE

- On August 11 and September 28, 2010, Keybase wrote to Mrs. O saying:
 - Mrs. O had a LIRA worth \$100,000. She lent \$40,000¹ in 2003 as a mortgage which was foreclosed in 2005. She also lent \$60,000² in 2006 as a mortgage which may also have been lost. Mrs. O was a direct party to the mortgages. She must have been aware of the risks and she is responsible for them;
 - Both mortgage investments were off-book transactions held in [Trustco #1] and [Trustco #2] accounts separate from the Keybase account. Keybase had no agreement with [Trustco #1] or [Trustco #2] to allow clients to hold mortgages. None of the correspondence or documentation indicates Keybase was involved in the mortgage transactions. Keybase was unaware of the transactions and Keybase could not supervise them;
 - Mr. N was terminated from Keybase for conducting similar off-book trades.
- Keybase did not offer Mrs. O compensation.

OBSI ANALYSIS

In the course of our investigation, we reviewed documentation provided to us by the parties. In addition to interviewing Mrs. O regarding her complaint, we interviewed Mr. B, Keybase's Branch Manager and Alternate Compliance Officer at the relevant time, and discussed the file with Mr. P, Ombudsman at [Bank #1]³. We were not able to interview Mr. N since he is no longer registered in the investment industry. We have also considered the applicable industry rules, regulations and practices.

¹ The first mortgage investment's face value was \$40,000. Mrs. O invested \$39,957 in the first mortgage investment.

² The second mortgage investment's face value was \$67,500. Mrs. O invested \$67,157 in the second mortgage investment.

³ Trustco #1 was a wholly-owned subsidiary of [Bank #1].

OBSI examined the following key issues in respect of Mrs. O's complaint:

1. Did Mrs. O know of and authorize the mortgage investments?
2. If she knew of and authorized the mortgage investments, did Mrs. O reasonably believe they were approved by and made through Keybase?
3. Did Mrs. O suffer financial harm as a result of the mortgage investments?
4. Who bears responsibility for the financial harm, if any?

Issue 1 – Did Mrs. O know of and authorize the mortgage investments?

- There were two mortgage investments in Mrs. O's LIRA:
 - \$39,957 in September 2003 administered by [Trustco #1], and
 - \$67,157 in October 2006 administered by [Trustco #2].
- Keybase says Mrs. O was aware of and agreed to both mortgage investments.
- Mrs. O says she knew of and signed documents to make the first mortgage investment in 2003. However, she says she was unaware of the second mortgage investment until [Trustco #2] provided documents to her in 2009 after she began doing research on her account.
- Mrs. O says that in 2006, Mr. N told her he was not getting along with someone at [Trustco #1] and that he preferred to switch her LIRA to [Trustco #2]. She says she had no concern with what she understood was an administrative change. However, she says she never signed any forms to open the [Trustco #2] LIRA or to make any investments in the [Trustco #2] LIRA. Rather, she says that when she requested copies of documents from [Trustco #2], she received mortgage documents and [Trustco #2] account documents on which she says her signature was forged.
- We reviewed the [Trustco #2] documents and, while we are not handwriting experts, compared to Mrs. O's signature on her letter of complaint and other earlier documents, it appears that some of the signatures on the [Trustco #2] and mortgage documents are not Mrs. O's. In addition, some signatures appear to have been copied and pasted from earlier documents. These signatures have darker shading in a box around the signature and the signatures appear to be somewhat blown up. Further, the signature on the \$60,000 mortgage investment document is exactly the same as the signature on the subsequent \$67,500 mortgage investment document. We find the problems with the signatures consistent with Mrs. O's contention that she did not know about the second mortgage investment.

- In addition, although Mrs. O moved from Ontario to Alberta in 1999, her address was recorded at various Ontario locations. The documents we have seen show the following:

Table 2: Summary of Ontario address information

Date	Document	Address
2003	Keybase NPAF	[redacted Address 1] Whitby, ON
2003	[Trustco #1] account application	
July 2003 to June 2004	[Trustco #1] account statements	
November 2004 to February 2005	[Trustco #1] registered letters	[redacted Address 2] Toronto, ON
July 2004 to June 2006	[Trustco #1] account statements	
2004 and 2005	Keybase annual account statements	
2003	Keybase annual account statement	[redacted Address 3] Toronto, ON
September and October 2006	[Trustco #1] account statements	
2003, 2006	Keybase yearly account statements	
2006	[Trustco #2] account application	
2006	[Trustco #2] Transfer Authorization for Registered Accounts	
November 2006 and July 2007	[Trustco #2] letters about the second mortgage investment	

- Mrs. O says that:
 - [redacted Address 1] belonged to her and that she opened it when she moved to Alberta in 1999 to receive mail sent to her former Whitby, Ontario address. She initially provided this address to Mr. N;
 - [redacted Address 2] address is her daughter's address; and
 - [redacted Address 3] was Mr. N's to receive mail for out of town clients.
- In particular, we note that the [Trustco #2] account application and other [Trustco #2] documents show [redacted Address 3], which belonged to Mr. N. Mrs. O says she never received [Trustco #2] account statements or any other information from [Trustco #2] until she requested it in late 2008 and early 2009. In fact, we note that

correspondence sent or copied to Mrs. O by [Trustco #2] in 2006 and 2007 was returned to [Trustco #2] marked “return to sender.”

Conclusion

Mrs. O acknowledges she knew of and authorized the first mortgage investment. However, Mrs. O says she was unaware of the second mortgage investment and she never signed any documents pertaining to [Trustco #2]. The signatures on the [Trustco #2] documents are inconsistent and some do not appear to be Mrs. O’s. In addition, there is apparent copying and pasting of signatures on the second mortgage investment documents. Furthermore, Mrs. O did not receive [Trustco #2] correspondence or documentation until 2009 after she requested it. Instead, it was sent to Mr. N’s [redacted Address 3]. In the circumstances, we accept Mrs. O’s contention that she was unaware of the second mortgage investment, and we conclude she did not authorize it.

Issue 2 – If she knew of and authorized the mortgage investments, did Mrs. O reasonably believe they were approved by and made through Keybase?

- Mrs. O only knew about the first mortgage investment and says it never occurred to her that it might not be approved by Keybase. Mrs. O says she believed Mr. N was recommending an investment in his capacity as a Keybase advisor and with Keybase’s approval in the same manner that he had always recommended investments. She did not make a distinction between Keybase and Mr. N who was her Keybase advisor. Further, she understood [Trustco #1] and [Trustco #2] provided an administrative function but understood her account was with Keybase.
- Mrs. O says Mr. N proposed the first mortgage investment to her by telephone shortly after she had opened her Keybase account and purchased mutual funds. She says he described it as a good alternative to her mutual fund investments and that it offered a 10% rate of return over a one-year period.
- Keybase says Mrs. O should have known that it was not involved in the mortgage investments. Keybase says none of the mortgage documents or correspondence indicate that it was involved in the transaction. Keybase further argues that the [Trustco #1] account is separate from the Keybase account and that [Trustco #1] traded in securities independent of Keybase.
- In contrast to Keybase’s assertions, our review of the documentation shows that:
 - the [Trustco #1] account application form and the first mortgage investment application show Keybase as the dealer and Mr. N as the advisor;
 - the form used in August 2003 to transfer Mrs. O’s LIRA money to [Trustco #1] shows Keybase as the dealer and Mr. N as the advisor;
 - section 9 of the August 25, 2003 Keybase NPAF shows “Rep’s Notes” stating

- “Funds in cash (MFC298) to be used for mortgage”;
- The mutual fund redemptions that were placed to make cash available for the first mortgage investment were processed by and through Keybase. In fact, as discussed further below, Mr. N specifically contacted Mrs. O by email in 2003 about the mutual fund redemption needed to complete the first mortgage investment;
 - The [Trustco #1] account statements Mrs. O says she received via her [redacted Address 1] for September, October, November and December 2003, show the mortgage investment, Keybase as the dealer and Mr. N as the advisor. Similarly, [Trustco #1] account statements we have seen up to October 2006 show Keybase as the dealer and Mr. N as the advisor;
 - Mr. N completed all of the Keybase, [Trustco #1] and mortgage investment paperwork and arranged to get what appears at first glance to be Mrs. O’s signature (on closer inspection, it is not) to open accounts and to authorize mutual fund transactions and the first mortgage investment. In particular, we note that in August 2003, he signed Keybase’s LIRA application form and the NPAF in his capacity as a Keybase advisor. He also signed [Trustco #1] forms as a witness, specifically, the [Trustco #1] Mortgage application and the [Trustco #1] Mortgage Direction and Undertaking for Self-Directed Mortgages form.
- We find Mrs. O’s contention that she believed she was dealing with Keybase and that the first mortgage investment was made through and approved by Keybase to be entirely consistent with the dealer and advisor information appearing on the documentation.
 - Further, Mrs. O recalls telephoning Mr. N regarding the first mortgage investment at his Keybase office number. An email dated September 26, 2003 from Mr. N substantiates Mrs. O’s recollection. Specifically, although he sent it from his personal email address at [email redacted], Mr. N wrote “I need you to call me right away in the office [telephone number redacted] [Trustco #1] did not redeem the funds required for the mortgage. I need you to sign a redemption form.” The telephone number matches the number shown on Keybase annual account statements we have seen from 2004 to 2006 next to Mr. N’s name. Although Mrs. O does not recall receiving these statements and has no record of them, the consistency of the phone number shows that Mrs. O spoke with Mr. N about the first mortgage investment at his Keybase authorized office using his Keybase contact information. We find the documentation clearly shows Mr. N recommended and facilitated the first mortgage transaction in his role as a Keybase investment advisor.
 - Furthermore, Mrs. O says she did not make a distinction between transactions through Keybase or [Trustco #1] and says Mr. N never differentiated between them. She says she understood [Trustco #1] was an administrator, Mr. N was her advisor and Keybase was the firm she was dealing with. In our view, given the information on the

documentation and on the [Trustco #1] account statements she received in 2003 and the advice and investment recommendations Mr. N provided in his capacity as her Keybase advisor, Mrs. O reasonably believed that the investments she authorized, specifically the mutual fund purchases and the first mortgage investment, were made through and authorized by Keybase.

- Keybase further contends that Mrs. O knew she was not dealing with Keybase because neither it nor Mr. N was authorized to sell mortgage investments or any security aside from mutual funds.
- Mrs. O says she did not know that Mr. N's registration was limited to certain products, nor should she be expected or required to. She did not verify, or even know how to verify, his registration category. As evidence that Mrs. O had no knowledge or appreciation of Mr. N's registration category or limitations, she continued to deal with him as she always had while she lived in Alberta, not knowing that Mr. N was not registered to sell investments of any kind in Alberta (and in fact he hid her residency from Keybase by asking her to use Ontario addresses). She says Mr. N never informed her about his registration status and she automatically assumed that as a Keybase representative, he was appropriately qualified and licensed. Therefore, Mrs. O did not know to question or enquire about Mr. N's registration or even consider, let alone ask about whether he was qualified to sell her a mortgage investment.
- Limitations imposed by certain registration categories is a matter for the compliance and enforcement regimes at firms and regulators to control, not clients who are investing based on recommendations from someone being presented by a firm as qualified to sell and advise on investments. It is our view that to Mrs. O, Mr. N's authority extended to selling her the investments he recommended, including the first mortgage investment. Therefore, we cannot see that his registration can be considered to have any bearing on determining whether Mrs. O believed she was making an investment approved by and made through Keybase.

Conclusion

Mr. N recommended and facilitated Mrs. O's mutual fund and first mortgage investments. Mrs. O believed Mr. N had the authority to sell her mortgage investments in his capacity as her Keybase advisor. Keybase is in fact shown as the dealer and Mr. N as the advisor on all application and transaction documents, as well as on Keybase and [Trustco #1] account statements. She did not know or have any reason to question Mr. N's registration category or restrictions. Mrs. O did not differentiate whether transactions were placed at [Trustco #1] or Keybase, simply and reasonably believing that Mr. N was her Keybase advisor and her account was a Keybase account. In all the circumstances, we find Mrs. O reasonably believed that the first mortgage investment was made through and approved by Keybase.

Issue 3 – Did Mrs. O suffer financial harm as a result of the mortgage investments?

- Mrs. O invested \$39,957 in her first mortgage investment and received \$2,000 in income, for a loss of \$37,957.
- Mr. N used \$67,157 of her money for the second mortgage investment on which Mrs. O received \$12,319 in income (net of fees) for a loss of \$54,838.
- Mrs. O agreed to Mr. N's recommendation for the first mortgage investment. However, her understanding was that she would receive a fixed and steady flow of income from this investment, that it would contribute to the growth of her portfolio for her retirement and that it was safe. In Mrs. O's circumstances, we believe a low-risk fixed income investment would have been suitable. Therefore, to calculate Mrs. O's financial harm, we compared her actual \$37,957 loss on the first mortgage investment to the performance of cashable GICs to represent safe, fixed income investments.
- We calculate that \$39,957 invested at the average 1-year GIC rate of 1.73% from September 30, 2003, when she invested in the first mortgage, until April 29, 2010, when Mrs. O complained to Keybase, would have earned interest income of \$4,777 and she would not have lost any of her capital. Therefore, her financial harm on the first mortgage investment includes the \$37,957 of lost capital and \$4,777 in lost income, for a total of \$42,734.
- Mrs. O was unaware of and did not authorize the second mortgage investment in her [Trustco #2] LIRA. On October 10, 2006, the mutual funds in Mrs. O's LIRA were redeemed for \$60,694, which was combined with \$6,806.52 of cash in her account and was advanced in two lots for the \$67,157 second mortgage investment. Considering none of these transactions should have taken place, we have compared the \$54,838 loss on the second mortgage to the performance of the mutual funds and the cash in the [Trustco #2] LIRA as though they had not been sold.
- We calculate that if Mrs. O had remained invested as she was before the second mortgage investment, she would have had a gain of \$1,712 from October 10, 2006, when the mutual fund redemptions took place, until April 29, 2010, when Mrs. O complained to Keybase. Therefore, her financial harm on the second mortgage investment is \$56,550 (\$54,838 + \$1,712).
- In total, we calculate that Mrs. O incurred \$99,284 (\$42,734 + \$56,550) in financial harm as a result of the two mortgage investments.

Issue 4 – Who bears responsibility for the financial harm, if any?

- Keybase argues that it is not responsible for the mortgage investments saying they are not related to its business. Below, we examine how the principle of vicarious liability applies to Keybase in this case and the opportunities it had to identify and or prevent losses through its supervisory activities. We also consider whether Mrs. O and/or [Trustco #2] should be held responsible for a portion of her loss.

Vicarious Liability

- Mr. Justice D.J. Gordon said in *Blackburn v. Midland Walwyn Capital Inc.* [2003] O.J. No. 621 (OSCJ), affirmed on appeal [2005] O.J. No. 678 (OCA), at para. 191 regarding vicarious liability that: “... a firm is absolutely responsible for the conduct of its stockbroker.” The reasons for holding investment firms liable for the conduct of their investment advisors were explained by McLachlin J., as she then was, in *Bazley v. Curry*, [1999] 2 S.C.R. 534 (S.C.C.), at para. 31:

Vicarious liability is arguable fair in this sense. The employer puts in the community an enterprise which carries with it certain risks. When those risks materialize and cause injury to a member of the public despite the employer’s reasonable efforts, it is fair that the persons or organization that create the enterprise and hence the risk should bear the loss. This accords with the notion that it is right and just that the person who creates a risk bear the loss when the risk ripens into harm.

- Mr. N was registered as a Keybase investment advisor from February 18, 2003 to January 18, 2007. Both of the mortgage investments in Mrs. O’s LIRA occurred in this period. Keybase says Mr. N was not registered or authorized to sell mortgage investments, and therefore it should not be responsible for Mrs. O’s losses. When Keybase focuses on the fact the activity was outside of Keybase’s or Mr. N’s license, it is failing to consider the whole context of Mr. N’s dealings with Mrs. O. In the Alberta Court of Queen’s Bench decision in *S. Maclise Enterprises Inc. v. Union Securities Ltd.*, [2008] 12 W.W.R. 539 the trial judge said “Courts should avoid a single element theory such as “unusual transaction” or “to whom the check was made”, or “activity outside of the employer’s license”, as these concepts are overly simple and do not properly engage in the *Bazley* analysis.” The Alberta Court of Appeal in reviewing the *Union Securities* trial decision [2009] A.J. No. 1405 went further and said “Even if they stepped outside their actual authority, that would not relieve Union Securities of vicarious liability. The solicitation of funds by Ferguson and Hochhausen from Maclise Enterprises was at the core of their responsibilities as employees of Union Securities.”
- Regardless of his registration, Mr. N was apparently acting on behalf of Keybase when he recommended the first mortgage investment, when he sold mutual funds to

make cash available for the first (and second) mortgage investment and when he completed paperwork and signed documents for the mortgage transactions as Mrs. O's Keybase advisor or as a witness. In these circumstances, there was, as McLachlin, J. said in *Bazley*, "a significant connection between the creation of the risk" (registering Mr. N and employing him to sell securities) "and the wrong that accrued from it" (selling and facilitating mortgage investments, one of which appears to have been fraudulent). Therefore, Keybase should be held vicariously liable for Mrs. O's losses.

Supervision

- On February 18, 2003, when Mr. N became an advisor at Keybase, the OSC imposed terms and conditions on his registration, including a requirement that Keybase would closely supervise Mr. N. In particular, Keybase was required to review, approve and regularly report to the OSC, among other things, about all buy, sell and sales contracts, investment suitability, client address and any address amendments, handling of client money or securities, and transfers of money or securities between client accounts.
- Keybase says it has controls in place to prevent "mutual funds only" registrants like Mr. N from dealing in any securities other than mutual funds through Keybase, but that it cannot monitor a person's activity or interactions with others that take place outside of Keybase. It argues it could not have supervised Mr. N's mortgage investment activities because they were placed at or by [Trustco #1] or [Trustco #2] without Keybase's knowledge or involvement. Yet, Keybase's Branch Manager and Alternate Compliance Officer at the time, identified mortgage investments at [Trustco #2] for Mrs. O and other clients as a result of routine trade reviews. Further, he tells us he recalls having had several discussions with Mr. N "warning him that Keybase would not accept any 2nd or 3rd mortgages." Therefore, we question Keybase's assertion that it could not or did not know of Mr. N's mortgage investment activities.
- Regardless, section 9 of the August 25, 2003 Keybase new account application shows "Rep's Notes" stating "Funds in cash (MFC298) to be used for mortgage." Keybase says the note on the August 2003 account application was not specific enough to flag Mr. N's off-book or outside business activity. Yet, in our view, this note alone makes it clear that Mrs. O was going to make an investment that was not a mutual fund and, since Mr. N was not authorized or registered to sell anything but mutual funds, we find the note should have led Keybase to investigate the proposed transaction and Mr. N's activities pertaining to it, particularly given the conditions relating to Mr. N's registration. Keybase was unable to provide any evidence that it made inquiries in this regard.
- Shortly after Mrs. O bought mutual funds in her LIRA in 2003, the Mackenzie money market fund, MFC298, was sold. However, it was not reinvested in mutual funds and

since the money was in a LIRA, it could not be withdrawn. Similarly, in 2006, all of the remaining mutual funds in her LIRA were sold but were not reinvested in mutual funds. They also could not be withdrawn. We have not seen any evidence that Keybase investigated what happened with the proceeds from Mrs. O's mutual fund sales. Had Keybase done so in a timely manner, particularly in light of the conditions of Mr. N's registration, it is likely it would have identified the off-book mortgage investment at [Trustco #1] in 2003 and could have prevented the apparently fraudulent second mortgage investment at [Trustco #2] from ever happening.

- As it turns out, Keybase missed or disregarded the mortgage note on the new account application and the mutual fund sale with no reinvestment in 2003. Therefore, Keybase enabled the apparently fraudulent mortgage to take place in 2006. It was only in January 2007, three years after Mrs. O's first mortgage investment, that Keybase identified Mr. N was involved in off-book trading activity, and in particular that he was selling mortgage investments not only to Mrs. O, but to other clients as well.
- Further, we note that Keybase signature guaranteed the [Trustco #2] LIRA account application form, the [Trustco #2] transfer form to transfer the LIRA from [Trustco #1] to [Trustco #2], and the Keybase NPAF all dated in 2006, just before the apparently fraudulent second mortgage investment was made. The signature guarantee suggests to [Trustco #2] that it can rely on the signatures as Mrs. O's. Yet, based on our review of these signatures compared to Mrs. O's earlier signatures, they are notably different and some do not appear to be Mrs. O's. While Keybase likely accepted the signatures because Mr. N had also signed the forms, if Keybase had investigated in 2003 when the first mortgage investment occurred, it would not have signature guaranteed [Trustco #2] documents that were used to facilitate the apparently fraudulent second mortgage.
- For all of these reasons, we find that Keybase missed important opportunities to prevent Mrs. O's losses.

Mrs. O's Responsibility

- While Mrs. O invested with Mr. N at Keybase, she was documented as having three different Ontario addresses while she resided in Alberta. She says Mr. N requested an Ontario address and that she followed Mr. N's instructions to show an Ontario address on her Keybase documents without understanding the potential implications of doing so.
- Keybase says that liability for Mrs. O's losses associated with her mortgage investments falls entirely on her because she agreed not to provide her Alberta address on the Keybase account opening documentation.
- We must consider Mr. N's careful preparation of this situation. To discourage Mrs. O from reviewing her account activity, he directed her account statements to

Ontario addresses, one of which he controlled, preventing or at least delaying delivery and limiting any questions Mrs. O would likely ask. Further, Mr. N had been Mrs. O's advisor since 1999 at another firm. Mrs. O says she did not have much investment experience or knowledge and she relied on his advice. She says she grew to trust him implicitly over the years she had dealt with him, believing she was in good hands. Mr. N relied on Mrs. O's trust and familiarity when he asked her to use another address as a convenience to him.

- In addition, Mrs. O says Mr. N was always very busy and that when she asked for account information, as the email evidence in 2003 and early 2004 shows, he provided short, quick updates regarding her investments. In fact, the email evidence suggests that he systematically failed to respond to most of Mrs. O's requests for account information and statements. Mrs. O says that since she knows little about investments, the short answers she received left her understanding that "everything was good." In April 2004, Mr. N indicated that he would send account statements. Even then, statements were not sent to an address where Mrs. O would have received them directly, but rather to Ontario addresses, including Mr. N's own [redacted Address 3] from which she would not receive them at all. She says she was not worried because she believed Mr. N had looked after her well in the past and she did not feel she needed to closely monitor her account. She says she was confident based on Mr. N's assurance that she would have all her investments "intact" at retirement.
- Further, as noted above, there is evidence Mrs. O made account information inquiries in 2003 and early 2004. Mrs. O recalls only receiving account statements in 2003 with none thereafter. While perhaps she could have continued making requests, and we note that in fact [Trustco #1] account statements were sent to her daughter's address until June 2006, it was not until after August 2006 that account statements would have shown anything she did not know about or that would raise concern. Specifically:
 - After August 2006, the [Trustco #1] statements showed that the first mortgage investment had been lost and removed from her account. However, the address was changed on [Trustco #1]'s records after June 2006, presumably by Mr. N, and the September and October 2006 [Trustco #1] statements were sent to Mr. N's [redacted Address 3];
 - The apparently fraudulent second mortgage investment was made in October 2006. However, [Trustco #2] correspondence and account statements were addressed to Mr. N's [redacted Address 3].

From the beginning, Mr. N had consistently sent mail for Mrs. O to other addresses, including his [redacted Address 3], delaying or outright preventing important information from being provided. By 2006, when [Trustco #1] and [Trustco #2] statement information would have alerted her of problems, Mrs. O had accepted a

lack of statements as normal and did not question it. We fail to see how Keybase can impute responsibility to Mrs. O in this regard.

- Rather, while Mrs. O agreed not to provide her Alberta address, it was at Mr. N's request in the context of their financial advisory relationship. Therefore, responsibility for failing to disclose Mrs. O's correct address to Keybase lies with Mr. N who, by virtue of his financial industry education and the conditions on his registration, knew or should have known that Keybase could not allow him to service an Alberta client without being properly registered. The fact that he asked for an Ontario address speaks to his knowledge that he would not be permitted to do so and to the fact that his request was intentional.
- However, in November 2004 and February 2005, Mrs. O received three registered letters from [Trustco #1] mailed to her daughter's address in Toronto about the foreclosure on the first mortgage investment. Mrs. O says she contacted Mr. N each time who assured her he would rectify the situation. In fact, the second [Trustco #1] letter refers to the fact that it needed some documents to port the mortgage as instructed. Mrs. O says she did not provide such instruction to [Trustco #1], suggesting to her that Mr. N was in fact taking steps to address the problem as he had assured her he would. Although the last letter indicates her investment had been "extinguished," she trusted Mr. N's repeated affirmation that matters had been resolved and she expected the money from the first mortgage investment was in her LIRA.
- Despite her trust in Mr. N, given the seriousness of the situation and the urgency communicated in [Trustco #1]'s letters, and in light of her personal experience with foreclosure in 1997, we believe Mrs. O should have known that there was a high risk of losing her first mortgage investment and it would have been reasonable for her to take additional steps beyond calling Mr. N. For example, she worked in the investment industry. Although she had an unlicensed administrative function, she had access to and could have discussed the situation with colleagues with expert investment knowledge or she could have contacted [Trustco #1] directly at the number indicated on its letters. Finally, after the last [Trustco #1] letter, she could have specifically requested confirmation of her account value to verify Mr. N's representation that he had looked after the matter. Although she may not have been able to fully prevent the loss, by not taking some additional action, we believe Mrs. O bears 25% responsibility her losses on the first mortgage investment.
- However, Mrs. O did not know of and did not receive information about the second mortgage investment until years after Mr. N had apparently fraudulently established it in her account and as such, we cannot find that she bears any responsibility for the financial harm she incurred in relation to it. Rather, we think that when she learned in late 2008 that Mr. N may have disappeared, we believe she took prompt and reasonable steps to try to ascertain what happened, including contacting Mr. N as she had always done, still believing he was her Keybase advisor (she never received correspondence from Keybase that he had been terminated and a new advisor had

been assigned and although he emailed her in 2009 from his personal email address, he had used his personal email address with her as far back as 2003). In addition, she contacted Ms. S, who she knew as a former colleague, and raised her complaint with [Trustco #2] and Keybase as reliable information became available to her.

[Trustco #2]’s Responsibility

- As noted above, Keybase signature guaranteed several [Trustco #2] documents on which [Trustco #2] relied to open Mrs. O’s LIRA. However, once the account was opened, [Trustco #2] accepted documents from [Firm X] for the second mortgage investment that, based on our review, apparently show Mrs. O’s signature is copied and pasted. In addition, the signatures were not consistent with the signatures on the account opening and transfer forms that Keybase signature guaranteed. [Trustco #2] missed the opportunity to identify these obvious problems and inconsistencies.
- Further, in November 2006 and July 2007, [Trustco #2] sent letters to Mrs. O regarding her account. Both letters came back to [Trustco #2] marked “return to sender.” We have seen no evidence that [Trustco #2] attempted to verify or obtain Mrs. O’s actual address, although it would have been reasonable for [Trustco #2] to do so.
- For these reasons, we find [Trustco #2] shares responsibility with Keybase for Mrs. O’s losses on the second mortgage investment and accordingly, Keybase’s compensation for Mrs. O’s second mortgage investment financial harm should be reduced by 30%.

Conclusion

In our view, Keybase is vicariously liable for Mr. N’s actions. It missed important red flags that it should have investigated and which would have prevented the second mortgage investment.

We find Keybase is primarily responsible for Mrs. O’s losses and that it was best positioned to prevent them. However, we find Mrs. O bears 25% responsibility for the losses associated with the first mortgage investment for failing to be more proactive when she received [Trustco #1]’s registered letters. With respect to the second mortgage investment, [Trustco #2] appears to have relied on questionable signatures and it failed to follow up when it became clear its address records were not correct. In the circumstances, we conclude that Keybase’s responsibility for the losses related to the second mortgage investment should be reduced by 30%.

Recommendation

As stated earlier, OBSI is obligated to assess and resolve complaints according to what is fair to the parties in the particular circumstances of the case. In all of the circumstances of this complaint, we believe it is fair to recommend that Keybase compensate Mrs. O \$71,636 (75% of \$42,734 + 70% of \$56,550) plus interest of \$2,248⁴ for total compensation of \$73,884.

⁴ Interest is calculated using the average 3-month Canadian Treasury Bill yield of 0.89% (as calculated by the Bank of Canada) compounded annually from the date of the complaint on April 29, 2010 to the date OBSI's report is final.