SCC File No. _____

IN THE SUPREME COURT OF CANADA
(ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO)

B E T W E E N:

CHRISTINE DEJONG MEDICINE PROFESSIONAL CORPORATION

Applicant
(Respondent)

- and -

DBDC SPADINA LTD. and THOSE CORPORATIONS LISTED ON SCHEDULE A HERETO

Respondents
(Appellants)

MEMORANDUM OF ARGUMENT

(CHRISTINE DEJONG MEDICINE PROFESSIONAL CORPORATION, APPLICANT)
(Pursuant to Rule 25(1)(c) of the *Rules of The Supreme Court of Canada*, S.O.R./2002-156)

Torys LLP
79 Wellington St. W., 30th Floor
Box 270, TD South Tower
Toronto, ON M5K 1N2
Fax: 416.865.7380

Jeremy R. Opolsky
Tel: 416.865.8117
jopolsky@torys.com

Counsel for the Applicant,
Christine DeJong Medicine Professional Corporation

SCHEDULE A – Respondents (Appellants)[*]

1. Dr. Bernstein Diet Clinics Ltd.
2. 2272551 Ontario Limited
3. DBDC Investments Atlantic Ltd.
4. DBDC Investment Pape Ltd.
5. DBDC Investments Highway 7 Ltd.
6. DBDC Investments Trent Ltd.
7. DBDC Investments St. Clair Ltd.
8. DBDC Investments Tisdale Ltd.
9. DBDC Investments Leslie Ltd.
10. DBDC Investments Lesliebrook Ltd.
11. DBDC Fraser Properties Ltd.
12. DBDC Fraser Lands Ltd.
13. DBDC Queen's Corner Inc.
14. DBDC Queen's Plate Holdings Inc.
15. DBDC Dupont Developments Ltd.
16. DBDC Red Door Developments Inc.
17. DBDC Red Door Lands Inc.
18. DBDC Global Mills Ltd.
19. DBDC Donalda Developments Ltd.
20. DBDC Salmon River Properties Ltd.
21. DBDC Cityview Industrial Ltd.
22. DBDC Weston Lands Ltd.
23. DBDC Double Rose Developments Ltd.
24. DBDC Skyway Holdings Ltd.
25. DBDC West Mall Holdings Ltd.
26. DBDC Royal Gate Holdings Ltd.
27. DBDC Dewhurst Developments Ltd.
28. DBDC Eddystone Place Ltd.
29. DBDC Richmond Row Holdings Ltd.

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[*] Companies are numbered in accordance with the Schedule A to the Reasons of the Court of Appeal for Ontario (C62822), dated January 25, 2018.

TO: **Lenczner Slaght Royce Smith Griffin LLP**
Barristers and Solicitors
130 Adelaide St. W.
Suite 2600
Toronto, ON M5H 3P5
Fax: 416.865.9010

Peter H. Griffin
Tel: 416.865.2921
pgriffin@litigate.com

Shara N. Roy
Tel: 416.865.2942
sroy@litigate.com

Lawyer for the Respondents (Appellants),
DBDC Spadina Ltd. and Those Corporations Listed on Schedule A Hereto

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PART I – OVERVIEW AND STATEMENT OF FACTS

Overview

1. This is a case of a complex commercial fraud that sees fraud victims pitted one against another. In this case, the DeJongs, a community obstetrician and a homebuilder, lost most of their savings to the fraudsters, the Waltons. While the companies they invested in retain some assets, the decision below would effectively give those assets over to another victim of the same fraud, through a dramatic extension of the doctrine of knowing participation.

2. There was no evidence in the record that any of these investment companies actually participated in the fraud in any way. All that was before the Court was an inspector's report that showed an incomplete snapshot: during a limited time period, on an cumulative basis, money moved from the respondent companies to the Waltons, and money moved from the Waltons to 54 other companies, 10 of which are named in this action. Indeed, two of these named companies, which hold much of the DeJongs' recoverable investment, were not even named in the report.

3. Instead, the majority of the Court of Appeal based its decision on the novel theory that since the *de facto* principal of all these companies was the fraudster, the companies themselves were liable for "knowing assistance." In doing so, it reversed the application judge, who had held that the companies did not knowingly participate in the fraud. He had also held that the actions of a fraudulent principal should not be attributed to the corporations that the principal had defrauded and stolen from.

4. The dissenting judge in the Court of Appeal would have upheld this decision. She held that the third party investor corporations were not participants in the scheme—they had been *used* by the fraudsters. Moreover, because the fraudsters were stealing from the investor real estate corporations, it would be inconsistent to attribute the fraudsters' knowledge and actions to the very companies that they were defrauding. Equity, in her view, should not be used to impose such unfair and prejudicial outcomes on innocent third parties.

5. This case asks this Court to confront the reality of complex commercial fraud in Canada and the availability of the doctrine of knowing participation for victims, in effect, to claim against each other. It raises three important questions:

(1) ***What does "participation" entail in knowing participation?*** Knowing participation is a fault-based doctrine. But this Court has never defined the requirements of a central element establishing culpability: whether participation in the breach of fiduciary duty must be (i) substantial or beyond *de minimis*; and/or (ii) have a causative impact on the harm suffered by the plaintiff. The majority of the Court of Appeal held that there are no such requirements. This is in contrast to the law in British Columbia, the United Kingdom and the United States, all of which require the assistance to be meaningful.

(2) ***How does the corporate identification doctrine apply in the context of knowing assistance?*** This case demonstrates the harm that arises from a loosened standard of imposing liability on the basis of the knowledge of a company's principal: the intention of the fraudster was attributed to the very corporations they were stealing from. This is not consistent with the public policy of the corporate identification doctrine.

(3) ***In cases like this one, must a Court consider the effect on third party investors when awarding remedies for knowing participation?*** The protection of third parties is a key tenet of equitable remedies, but the court below applied the equitable doctrine of knowing assistance without considering its prejudicial and unfair effect on innocent investors. In the wake of a fraud, equity should not be summoned in service of some innocents victims to the detriment of others.

6. This is a case of first impression; as the dissenting judge noted below, it is the first time that such a claim of knowing assistance has been made by one group of defrauded investors against another similarly situated group. Both groups of investors were lied to, defrauded and suffered breaches of fiduciary duty. Both invested with the fraudsters through exactly the same arrangement. But the application of knowing participation allowed the DeJongs' investment vehicles to be treated as complicit in the very fraud that befell them. This is not equity at work.

7. The Court should take this opportunity to consider these issues and provide clarity for swindled investors and courts grappling with fraud. Leave to appeal should be granted.

The Waltons' fraudulent scheme and its victims

8. This case arises from a multi-million dollar fraud that the application judge described as a "sorry saga."[1] The Waltons convinced investors to contribute money into project-specific corporations, as equal shareholders and equal contributors, with the intention of acquiring, improving and maintaining commercial real estate. Any decisions that differed from the project plan required the approval of both the Waltons and the investors.[2]

9. While some of these corporations acquired properties, the Waltons never invested significant funds of their own for the purchases. Rather, the Waltons misappropriated funds from other investors and fraudulently moved investor money into their own corporation, the Rose & Thistle Group Ltd., for their own benefit.[3] In short, the Waltons abused the trust of their investors and misappropriated millions of dollars for themselves that cannot now be recovered.

10. This appeal is between two of the many innocent victims of the Waltons' fraud:

(1) ***Dr. Bernstein*** owns a series of very successful diet and health clinics. Through his personal investment vehicles, the DBDC Applicants or "**Bernstein Applicants**", they invested approximately $111 million with the Waltons in approximately 31 projects.

(2) ***Dr. Christine DeJong*** is a community obstetrician and gynecologist, and her husband, Michael DeJong, is a homebuilder. Through Christine DeJong Medicine Professional Corporation ("DeJong PC"), Christine and her husband, Michael, invested approximately $4 million with the Waltons.[4] As one judge in these proceedings put it, they stood "at the receiving end of the Waltons' misconduct."[5]

11. The Waltons also stole the savings of other individual investors through their scheme. Dennis and Peggy Condos lost $160,000 through their investments. Gideon and Irene Levytam lost $337,000. Many other investors were defrauded of smaller amounts.[6]

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[1] *DBDC Spadina Ltd et al v. Norma Walton et al*, 2016 ONSC 6018 ("MJ Reasons"), para. 4, DeJong Leave Application ("LA"), Tab 2A.
[2] MJ Reasons, para. 50, LA, Tab 2A.
[3] *DBDC Spadina Ltd. v. Walton*, 2018 ONCA 60 ("CA Reasons"), para. 3, LA, Tab 2D.
[4] CA Reasons, para. 5, LA, Tab 2D.
[5] *DBDC Spadina Ltd. v. Walton*, 2014 ONSC 4644, para. 290.
[6] CA Reasons, paras. 6, 166, n 17, LA, Tab 2D.

12. While, Dr. Bernstein, the DeJongs, and the other investors were all the victims of the Waltons' fraudulent scheme, Dr. Bernstein was first to discover the fraud, first to sue on the fraud, and is trying as a result to get a claim on whatever proceeds remain. The application judge would not dislodge other victims' claims in his favour. But the Court of Appeal did.

Fraud is discovered and an inspector/manager is appointed for Bernstein companies

13. In the summer of 2013, Dr. Bernstein learned that the Waltons were not complying with the terms of their investment agreements.[7] In October 2013, at the request of the Bernstein Applicants, Justice Newbould appointed an inspector to investigate the corporations that the Bernstein Applicants had invested in,[8] and later, as a manager over the same corporations.[9]

14. DeJong PC was not a party to either of the proceedings before Justice Newbould. Christine and Michael had only become aware of a potential issue with their investments in November 2013.[10] By the time that the DeJongs had learned of the proceedings between the Bernstein Applicants and the Waltons, 20 orders had already been made in the proceedings.[11] One of those orders, for example, froze innocent investor assets with no notice to those investors.[12]

Relief requested before Justice Brown

15. In July 2014, as more facts became known about the Walton's scheme, the Bernstein Applicants moved for further relief against the Waltons before Justice D.M. Brown. This time they included a claim against certain Walton properties, including some properties that DeJong PC and other third parties had invested in with the Waltons.

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[7] *DBCD Spadina Ltd et al v. Norma Walton et al*, 2013 ONSC 6251, para. 8.
[8] *DBCD Spadina Ltd et al v. Norma Walton et al*, 2013 ONSC 6251, para. 32.
[9] CA Reasons, para. 10, LA, Tab 2D; *DBCD Spadina Ltd et al v. Norma Walton et al*, 2013 ONSC 6833, at paras. 46, 53.
[10] *Affidavit of Christine DeJong, sworn February 11, 2015*, at para. 9, LA, Tab 4A ("DeJong Affidavit").
[11] CA Reasons, para. 169, n 18, LA, Tab 2D.
[12] *Order of Justice Newbould, dated March 21, 2014*, LA, Tab 4B.

16. The Bernstein Applicants based their claim on one of the Inspector's Reports that detailed the "net transfer" of funds out of companies that were jointly owned by the Waltons and the Bernstein Applicants ("the Net Transfer Analysis").[13]

17. Justice Brown defined the entities and properties in dispute in relation to Bernstein:

(1) **Schedule B Companies** (here, "**Walton-Bernstein Companies**") – companies jointly owned by the Bernstein Applicants and the Waltons; [14]

(2) **Schedule C Companies** (here, "**Walton Companies**") – companies "controlled by the Waltons in which Dr. Bernstein did not have an ownership interest."[15] These are 54 Walton-controlled accounts, including Norma Walton's personal account.[16] Some of these companies were jointly owned by the Waltons and innocent investors, including the DeJongs, but some were entirely owned by the Waltons. The only unifying feature of the Walton Companies was that Dr. Bernstein had no ownership interest in any of them.

(3) **Schedule C Properties** (here, "**Third-Party Properties**") – properties owned by the Walton Companies.

18. The Net Transfer Analysis was not precise, nor was it intended to be. The Net Transfer Analysis provided limited information because:

(1) ***It was time limited***. The analysis only "intended to provide a snapshot of activity at a particular point of time," not an exhaustive treatment of all transfers.[17] It only captured transfers from October 2010 – October 2013.

(2) ***It was incomplete***. Because the Net Transfer Analysis was time-limited, it did not include all Walton Companies. The analysis excluded two corporations (and their properties) that DeJong PC had invested in with the Waltons (St. Clarens

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[13] *DBDC Spadina Ltd. v. Walton*, 2014 ONSC 4644, para. 16.
[14] Listed in Schedule A to this application.
[15] *DBDC Spadina Ltd. v. Walton*, 2014 ONSC 4644, para. 1.
[16] CA Reasons, para. 188-189, LA, Tab 2D.
[17] *DBDC Spadina Ltd. v. Walton*, 2014 ONSC 4644, para. 159.

Holdings Ltd. and Emerson Development Ltd.).[18] Those investment agreements were entered into after the Inspector conducted the Net Transfer Analysis [19] and when the Waltons no longer had access to Dr. Bernstein's money and assets. There was therefore no evidence of any transfer between those two corporate accounts and the Rose & Thistle account, let alone any Bernstein accounts.[20]

(3) ***It was cumulative***. The Net Transfer Analysis only captured the *cumulative* transfer of $23.6 million from the Walton-Bernstein Companies to the Rose & Thistle Group (the Waltons' clearing house) and the *cumulative* transfer of $25.4 million from the Rose & Thistle Group to the Walton Companies.[21] Except in a few circumstances, where a tracing analysis was conducted, the Net Transfer Analysis did not establish the transfer of any funds from a Walton-Bernstein Company to a Walton Company. The Analysis also could not identify the original source of the money transferred from Rose & Thistle to the Walton Companies – some of this money may have come from innocent investors.

(4) ***It treats the Walton Companies as one homogenous corporate group, which they were not.*** The Walton Companies included 54 accounts. While DeJong PC were joint-owners of a few of those Walton Companies,[22] this grouping also included other companies owned and controlled exclusively by the Waltons.

19. The Net Transfer Analysis provided only *limited* tracing analysis. It provided evidence for constructive trusts over only eight Third-Party Properties.[23] Justice Brown had no ability to trace funds into any other Walton Company or Third-Party Property. As he explained, the "state of the evidence at this point of time does not permit the making of constructive trust orders for fixed amounts in respect of other [Third-Party Properties]." [24]

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[18] CA Reasons, para. 189, n 22, LA, Tab 2D.
[19] DeJong Affidavit, para. 18, LA, Tab 4A.
[20] CA Reasons, para. 226, LA, Tab 2D.
[21] CA Reasons, paras. 16, 223, LA, Tab 2D.
[22] CA Reasons, paras. 33, 183, LA, Tab 2D.
[23] *DBDC Spadina Ltd. v. Walton*, 2014 ONSC 4644, paras. 264, 267.
[24] *DBDC Spadina Ltd. v. Walton*, 2014 ONSC 4644, para. 268.

20. Justice Brown granted a tracing order permitting the Bernstein Applicants to find more evidence, but they never undertook any such tracing.[25]

Application judge denies the Bernstein Applicants' request for relief

21. The Bernstein Applicants then sought to recover their net losses against the Waltons.[26] Justice Newbould found the Waltons liable for civil fraud and fraudulent misrepresentation.[27]

22. The Bernstein Applicants also claimed against ten of the 54 Walton Companies (the "**Investor Companies**"). All ten of these companies held innocent investor money. The Bernstein Applicants argued that the Investor Companies should be held liable, jointly and severally, for (i) knowing receipt and (ii) knowingly assisting the Waltons in transferring $23.68 million out of the Walton-Bernstein Companies.[28]

23. ***The properties at issue.*** The Receiver/Manager of those Investor Companies had sold the ten properties that the companies owned. The Bernstein Applicants wanted to share in these sale proceeds as unsecured judgment creditors, even though the Bernstein Applicants already had a constructive trust over four of the ten properties. After deducting the constructive trust amounts, $2,775,628 remained from the property sale.[29]

24. All of the money remaining was derived from the sale of properties out of Walton Companies that had received funds from innocent investors. Companies co-owned by DeJong PC accounted for 66.3% of it ($1,840,964), and Condos and Levytams accounted for 29.3% of the money ($812,510). These funds were the only amounts from which these innocent investors could recover following the fraud.

25. The sole basis for the Bernstein Applicants' knowing receipt and knowing assistance claims was the Investor Companies' *receipt* of the Bernstein Applicants' property. The Bernstein Applicants' pleading stated simply:

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[25] *DBDC Spadina Ltd. v. Walton*, 2014 ONSC 4644, paras. 268, 278; MJ Reasons, at para. 58, LA, Tab 2A.
[26] MJ Reasons, para. 19, LA, Tab 2A.
[27] MJ Reasons, para. 32, LA, Tab 2A.
[28] MJ Reasons, paras. 44, 54, LA, Tab 2A.
[29] CA Reasons, para. 182, LA, Tab 2D.

> the [Investor Companies] received property from the Applicants as a result of the Waltons' breach of their fiduciary duties owed to the Applicants … [and they] each received this property from the Applicants having knowledge that the property was transferred in breach of a fiduciary duty.[30]

26. The Bernstein Applicants' only evidence for this claim was the Net Transfer Analysis. But two of the Investor Companies claimed against were excluded from the Net Transfer Analysis (St. Clarens Holdings Ltd. and Emerson Development Ltd.). DeJong PC was the only outside investor in these companies, and the sale of its properties accounted for over $600,000.

27. ***Justice Newbould's findings.*** Justice Newbould rejected the knowing receipt claim, taking issue with the Net Transfer Analysis. This claim could not be made out on the record: "[t]he [net transfer] report does not state where the money came from." He held that "[w]hat happened to the money transferred to the [Walton-Bernstein Companies] and [Walton Companies] by Rose & Thistle is not in evidence."[31] Justice Newbould reasoned that the money transferred to the Walton Companies could very well have come from innocent investors.[32] All that is known is that the monies flowed to Rose & Thistle. The Bernstein Applicants had received a tracing order, which would have enabled them to introduce evidence to show if any of the money flowed into the Third-Party Properties. They declined to do so.

28. Justice Newbould also rejected the knowing assistance claim, refusing to attribute the Walton's fraudulent conduct to the Investor Companies. Under the investor agreements, Ms. Walton and her husband were only "50% owners with the right to exercise 50% of the significant decisions."[33] Because the investors, who had a 50% stake in the companies, knew nothing of the fraud, those companies could not have knowingly assisted in Ms. Walton's fraudulent breach.

29. The application judge concluded that it would defy logic to hold third party investors liable for knowingly assisting the Waltons. The Waltons breached their fiduciary duties to the Investor Companies and the innocent investors, just as they did to the Bernstein Applicants. The

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[30] CA Reasons, para. 218, LA, Tab 2D.
[31] MJ Reasons, paras. 57-58, LA, Tab 2A.
[32] MJ Reasons, para. 57, LA, Tab 2A.
[33] MJ Reasons, para. 51, LA, Tab 2A.

Waltons transferred money out of the Investor Companies for their own benefit, indistinguishable from the harm to Bernstein.[34] He stated:

> This issue raised by the applicants is not a contest between Dr. Bernstein and the Waltons. It is a contest between Dr. Bernstein and the investors in the [Investor Companies] who suffered from the same misconduct as did Dr. Bernstein. Ms. Walton knowingly breached her fiduciary obligations to the [Investor Companies] and the [Investor Company] investors.[35]

The Court of Appeal majority reverses the application judge on knowing assistance

30. A unanimous Court of Appeal upheld the application judge's conclusion on the knowing receipt claim.[36] But the majority reversed the finding on knowing assistance.

31. The majority held that because Norma Walton was the directing and controlling mind of the Investor Companies, her knowledge and conduct could be attributed to those companies. The majority held that the requirements of *Canadian Dredge* should be applied in a "less demanding fashion" in this civil context. The majority therefore concluded that since Ms. Walton had perpetrated the fraud, the Investor Companies should be deemed to have assisted in it. In the majority's words, "her perpetration of the scheme was their participation in the scheme."[37]

32. Justice Blair also relied heavily on the Net Transfer Analysis. Even though it included the amounts that *all* 54 Walton Companies either received from or transferred to Rose & Thistle, the majority quantified the loss at $22.6 million against each of the ten Investor Companies. It drew such conclusion despite the fact that there was no evidence any of the particular companies had a role in or benefited from the fraudulent scheme.[38]

33. Although the Investor Companies were the investment vehicles for innocent third party investors, Justice Blair held the companies jointly liable for the $22.6 million loss to the Bernstein Applicants. Justice Blair acknowledged that a court has a discretion not to apply the

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[34] MJ Reasons, paras. 52, 71-72, LA, Tab 2A.
[35] MJ Reasons, para. 53, LA, Tab 2A.
[36] CA Reasons, paras. 38, 205, LA, Tab 2D.
[37] CA Reasons, paras. 68, 70, LA, Tab 2D.
[38] CA Reasons, para. 87, LA, Tab 2D.

doctrine of knowing assistance where its criteria are met, but he declined to exercise that discretion. He found it "hard to conceive of a case" where this exception would apply.[39]

Dissenting reasons

34. Justice van Rensburg saw the fundamental unfairness of the Court basing its decision on the Net Transfer Analysis, which described transfers from Rose & Thistle to *all* 54 Walton Company accounts, to hold liable "ten such companies, the ones with valuable property and other defrauded investors, for the purpose of their knowing assistance claim."[40]

35. Justice van Rensburg disagreed in principle with the majority's approach on a number of legal questions:

(1) ***Participation requires more than broad-strokes involvement in unspecified conduct***. The Investor Companies did *not* knowingly "participate" in the Walton's fraud – even if the Investor Companies had been used in a general sense by the fraudsters, there is no evidence that any had individually participated in the Waltons' diversion of the Bernstein Applicants' assets.[41]

(2) ***No reason to relax Canadian Dredge***. *Canadian Dredge* was the minimum standard to impute Ms. Walton's actions and knowledge to the Investor Companies. There was "no justification in the circumstances of this case to lessen the requirement for knowledge before one victim of a fraud is tagged with the conduct of a fraudster."[42]

(3) ***Unjust result for innocent investors.*** There is no reason to apply the equitable doctrine of knowing assistance to benefit one category of victims at the expense of another. The majority's decision ultimately means that the third party investors would be overwhelmed by Dr. Bernstein's claims.[43]

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[39] CA Reasons, para. 123, LA, Tab 2D.
[40] CA Reasons, para. 199, LA, Tab 2D.
[41] CA Reasons, para. 221-224, LA, Tab 2D.
[42] CA Reasons, para. 237, LA, Tab 2D.
[43] CA Reasons, para. 245-248, LA, Tab 2D.

PART II – STATEMENT OF THE QUESTIONS IN ISSUE

36. The question in issue on this application is whether the proposed appeal raises an issue of national or public importance that warrants the granting of leave to appeal. It does.

37. This case raises numerous important issues. As Justice van Rensburg recognized, this is a "case of first impression" considering for the first time "a claim of knowing assistance in a breach of fiduciary duty is made by one group of defrauded investors against another similarly situated group."[44] This Court should discuss whether and how the doctrine can be used to prejudice victims of fraud in contests with other victims of the same fraudster.

38. In particular, this case raises the following issues that warrant this Court's consideration:

(1) What are the requirements of "participation" in a knowing assistance claim?

(2) How does the corporate identification doctrine apply in the context of knowing assistance?

(3) In granting a remedy under the equitable doctrine of knowing assistance, must a court consider its effect on third parties?

PART III – CONCISE STATEMENT OF ARGUMENT

National and Public Importance

39. Frauds continue to wreak financial ruin on Canadians at an alarming rate.[45] It is the nature of fraudulent schemes that there is never enough funds to fully reimburse the victims. To recover their losses – often their retirement savings – victims look for recovery against all potential sources. As a result, claims are frequently brought against the fraudster's intermediaries and third parties, often including claims for knowing receipt or knowing assistance. Over the past decade, knowing assistance has been raised in the context of Ponzi schemes and other fraudulent schemes in numerous reported decisions.[46]

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[44] CA Reasons, para. 160, LA, Tab 2D.
[45] *See e.g.* Barrie McKenna, "Largest Ponzi scheme in Canadian history exploited boom time Alberta" *The Globe and Mail* (15 February 2015), online: <https://www.theglobeandmail.com/report-on-business/largest-ponzi-scheme-in-canadian-history-exploited-boom-time-alberta/article23010870/>.
[46] See e.g. *1169822 Ontario Limited v.The Toronto-Dominion Bank*, 2018 ONSC 1631; *Toronto-Dominion Bank, N.A. v. Lloyd's Underwriters*, 2017 ONCA 1011; *Stanford International Bank*

40. The applicants are not aware of any other case in which knowing assistance is used by one group of defrauded investors to prioritize their claims against similarly situated investors. And this Court has not addressed the doctrine of knowing assistance in 20 years. This case therefore provides the Court an opportunity to clarify the law of knowing assistance and to ensure that it cannot be used to treat victims of fraud as being complicit in the very fraudulent scheme that robbed them.

Issue 1: What are the requirements of "participation" in a knowing assistance claim?

41. This Court has never considered what the requirement of "participation" in a breach of trust means in the test for knowing assistance. The level of participation and culpability required for liability is especially relevant for larger, complex frauds.

The law of knowing assistance: Air Canada and beyond

42. The Court has addressed the doctrines of knowing assistance and knowing receipt only in a trilogy of decisions in the mid-1990s, beginning with *Air Canada v. M & L Travel Ltd.*[47]

43. A defendant is liable for "knowing receipt" where the stranger receives trust property for its own benefit, with actual or constructive knowledge that the property came from a breach of trust or fiduciary duty.[48]

44. In contrast, culpability is at the core of knowing assistance; unlike knowing receipt, it is "fault-based."[49] Liability of a stranger for a breach of trust "depends on the basic question of

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Ltd. v. Toronto-Dominion Bank, 2015 ONSC 6900; *Jer v. Samji*, 2014 BCCA 116; *Wide v. Toronto Dominion Bank*, 2012 ONSC 4039; *Kherani v. Bank Of Montreal*, 2012 ONSC 2230; *Pardhan v. Bank of Montreal*, 2012 ONSC 2229; *Eaton v. HMS Financial Inc.*, 2010 ABQB 635; *Dynasty Furniture Manufacturing Ltd. v. Toronto Dominion Bank*, 2010 ONSC 436; *Ramias v. Johnson*, 2009 ABQB 386.

[47] *Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R. 787.

[48] *Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R. 787, pp. 810-811; *Citadel General Assurance Co. v. Lloyds Bank Canada*, [1997] 3 S.C.R. 805, para. 48.

[49] *Citadel General Assurance Co. v. Lloyds Bank Canada*, [1997] 3 S.C.R. 805, para. 46; *Gold v. Rosenberg*, [1997] 3 S.C.R. 767, para. 41.

whether the stranger's conscience is sufficiently affected to justify the imposition of personal liability."[50]

45. Culpability is established through both knowledge and participation. Where a trustee had perpetrated a dishonest and fraudulent breach of a trust, a stranger to that trust is liable for knowing assistance if (i) the defendant had actual knowledge of the trust and the dishonest breach; and (ii) the defendant participated in the breach of trust.[51] A higher level of knowledge is required for knowing assistance because unlike with receipt, the stranger to the trust has not received the trust property for his or her benefit. Therefore, a lesser standard of knowledge would be "insufficient to bind the stranger's conscience."[52]

Uncertainty on the requirements of "participation"

46. This case turns on the meaning and requirements of "participation." What does it mean to participate in a breach of trust?

47. This Court has not spoken to the issue. In *Air Canada*, the issue before the Court was the appropriate standard for knowledge of a breach of trust. In that case the question of participation was not in issue because the defendants had "directly caused" the breach.[53]

48. Lower courts, often referring to participation as assistance, have failed to create any clarity on this critical element of knowing assistance. Like *Air Canada*, the jurisprudence has largely addressed situations where the defendant had committed "specific harmful conduct,"[54] making a delineation of the element of participation unnecessary. The Ontario Court of Appeal recently held that "[w]hat amounts to assistance – or, in the words of the motions judge, 'helping' or 'taking part' – has not yet been fully explored in the jurisprudence."[55]

49. The requirements of participation matter. Before a corporation can be liable for knowing assistance as a result of the actions of its fraudster principal, it must be found to have assisted in

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[50] *Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R. 787, p. 808.
[51] *Gold v. Rosenberg*, [1997] 3 S.C.R. 767, para. 34.
[52] *Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R. 787, p. 812.
[53] *Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R. 787, p. 827.
[54] CA Reasons, para. 217, LA, Tab 2D.
[55] *Locking v. McCowan*, 2016 ONCA 88, para. 21.

the fraud. The question is therefore what level of assistance is actually required by the corporation? Does it need to be substantial assistance or more than *de minimis*?

50. An equally important question is whether an entire corporate group can all be found to have knowingly assisted on the basis of the principal's participation. And at what level of generality? Can a court conclude (as the Court of Appeal did) that *all* corporations that are under the *de facto* control of the fraudster are liable? Or does the plaintiff have to show that a specific corporation was used in a specific way to assist the breach *and* that this assistance contributed to the harm caused to the beneficiary of the fiduciary obligation? This Court should grant leave and clarify these numerous questions.

Divergence in jurisprudence in the requirements of participation

51. The majority's approach to establishing participation divergences from standards in other Canadian provinces as well as internationally.

52. Under the majority's articulation of the knowing assistance doctrine, participation plays a small role. First, participation or assistance requires no act or omission of an individual actor. There was no evidence that the individual Investor Companies assisted in misdirecting funds from the Walton-Bernstein Companies. To the contrary, with respect to two of the Investor Companies (in which the DeJongs had invested), there was no evidence of any transfer between their accounts and the Rose & Thistle account, let alone the Walton-Bernstein Companies.[56] Yet, Justice Blair found participation from the "global scheme" itself:

> [i]t is the *overall fraudulent scheme*, and the [Investor Companies'] knowing assistance in the perpetration of that 'shell game' that provides the prism through which liability for this claim must be determined [emphasis added].[57]

53. Second, according to the Court of Appeal, assistance or participation requires no act or omission of any significance or consequence. Unlike the directors who "directly caused" the breach of trust in *Air Canada*, Justice Blair described the Investor Companies as "conduits" or "pawns" in the Waltons' scheme.[58] But their incidental and interchangeable role in the fraud was

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[56] CA Reasons, para. 226, LA, Tab 2D.
[57] CA Reasons, paras. 105, 129, LA, Tab 2D.
[58] CA Reasons, para. 102, LA, Tab 2D.

ultimately ignored in his analysis. This diminished role diverges significantly from the law in the U.K., British Columbia, and the United States.

54. ***U.K. law.*** The cause of action of knowing assistance is based on U.K. law. But the Court of Appeal's decision strays from the rules imposed by English courts. In the U.K., a defendant is only liable if its assistance is meaningful; it "must not be of minimal importance."[59] Moreover, the assistance must actually facilitate the breach of trust: "if there is no causative effect and therefore no assistance given … I cannot see that the requirements of conscience require any remedy at all."[60]

55. ***British Columbia.*** The law is to the same effect in British Columbia. Drawing on English law, B.C. Courts have held that "a claimant must at least show that the defendant's actions have made the fiduciary's breach of duty easier than it would otherwise have been." In this sense, the defendant's conduct must have had "some causative impact" such that it was not merely of "minimal importance" to the fiduciary.[61]

56. ***United States.*** The U.S. parallel to knowing assistance—the tort of substantial assistance in breach of a fiduciary duty—requires an even more substantial contribution than U.K. and B.C. law. The plaintiff must allege that "the actions of the aider/abettor proximately caused the harm on which the primary liability is predicated."[62] In other words, the accessory's participation must be a "substantial factor" in bringing about the injury purportedly suffered.[63] On this basis, a court has concluded that even though a Ponzi scheme had only been possible because of a third party's actions and inaction, the third party's "conduct was not a proximate cause of the Ponzi scheme." In that case, the third-party clearing broker allegedly violated margin requirements and

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[59] *Baden v Société Générale pour Favoriser le Développement du Commerce et de l'Industrie en France SA* (1983), [1992] 4 All ER 161, p. 234 (Eng. Ch.), appeal dismissed, [1985] BCLC 258 (C.A.).
[60] *Brown v. Bennett*, [1999] 1 BCLC 649, p. 659 (Eng. C.A.). *See also* Paul S. Davies, *Accessory Liability* (Oxford: Hart Publishing, 2015), pp. 33, 37-39.
[61] *Imperial Parking Canada Corp. v. Anderson*, 2016 BCSC 468, para. 26; *Bronson v. Hewitt*, 2010 BCSC 169, paras. 498-500, var'd on other grounds, 2013 BCCA 367.
[62] *SPV Osus Ltd. v. UBS AG*, 882 F.3d 333, p. 345 (2d.C. 2018).
[63] *Neilson v. Union Bank of California*, N.A., 290 F.Supp.2d 110, pp. 1129-1130 (C.D.Cal.2003).

overextended credit to the fraudster's fund, but neither act was a proximate cause of the scheme.[64]

The requirements of participation need clarification

57. This case presents an opportunity for this Court to clarify the level of assistance or participation that is required to make a stranger to a trust liable for its breach. The Court should hear arguments on whether and how the stricter requirements of B.C., U.K. and/or U.S. law should be adopted as opposed to the minimalist approach of the majority below. This would permit the Court to articulate a single standard to be used throughout the common law provinces.

58. Articulating a participation threshold would align the doctrine of knowing assistance with the fault-based nature of liability at its core. Such a threshold would ensure that "a person [or company] does not run the risk of accessory liability for negligibly contributing to a wrong committed by another."[65]

59. The standard for participation is not simply a theoretical question in this case. Rather, Justice van Rensburg's dissent reflects how the DeJong's position would have been entirely different using a standard of meaningful participation, and requiring evidence of that participation, to establish knowing assistance. She held that the evidence did not establish that the Investor Companies themselves "participated in Ms. Walton's diversion of the [Bernstein Applicants'] funds."[66] The only transfers in evidence were between Walton Companies generally and Rose & Thistle, the Waltons' personal clearing house. Indeed, as Justice van Rensburg observed, "[t]he actions of the [Investor Companies] were the same as those of the [Walton-Bernstein Companies] – they were conduits and used as part of the Waltons' shell game."[67]

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[64] *Cromer Fin. Ltd. v. Berger*, 137 F.Supp.2d 452, pp. 470-472 (S.D.N.Y. 2001).
[65] Paul S. Davies, *Accessory Liability* (Oxford: Hart Publishing, 2015), p. 39.
[66] CA Reasons, para. 223, LA, Tab 2D.
[67] CA Reasons, para. 221, LA, Tab 2D.

Issue 2: Application of the corporate identification doctrine

60. The majority's application of the *Canadian Dredge* raises the important issue of how the corporate identification doctrine can be applied in the context of knowing assistance to maintain the necessary level of culpability.

61. The two elements of knowing assistance—knowledge and participation—are both critical in establishing the necessary fault to make a stranger to a trust liable for a breach of that trust. In *Air Canada*, this Court required a high degree of knowledge to reflect the necessary culpability: "actual knowledge" is required as constructive knowledge is "insufficient to bind the stranger's conscience so as to give rise to personal liability."[68]

62. In *Livent*, this Court affirmed that *Canadian Dredge* remains the authoritative test for the corporate identification doctrine – *i.e.*, when will an individual's actions be imputed to a corporation? Under the test, a corporation will be liable for an action taken by its directing mind when that action "(a) was within the field of operation assigned to him; (b) was not totally in fraud of the corporation; and (c) was by design or result partly for the benefit of the company."[69]

63. However, the Court recognized that "public policy and judicial necessity" do not always favour imputing a corporation with the directing mind's actions and knowledge in a civil suit:[70]

> The principles set out in *Canadian Dredge* provide a sufficient basis to find that the actions of a directing mind be attributed to a corporation, not a *necessary* one (pp. 681-82). As a principle that is grounded in policy, and which only serves as a means to hold a corporation criminally responsible or to deny civil liability, courts retain the discretion to refrain from applying it where, in the circumstances of the case, it would not be in the public interest to do so [emphasis in original].[71]

64. Relying on *Livent*, Justice Blair held that "policy considerations support a more flexible approach" to the corporate identification doctrine in complex multi-corporation fraud cases. In contrast, Justice van Rensburg applied the criteria strictly. She saw "no justification in the

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[68] *Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R. 787, p. 812.
[69] *Canadian Dredge & Dock Co. v. The Queen*, [1985] 1 S.C.R. 662, para. 66; *Deloitte & Touche v. Livent Inc. (Receiver of)*, 2017 SCC 63, para. 100.
[70] *Deloitte & Touche v. Livent Inc. (Receiver of)*, 2017 SCC 63, paras. 102-103.
[71] *Deloitte & Touche v. Livent Inc. (Receiver of)*, 2017 SCC 63, para. 104.

circumstances of this case to lessen the requirement for knowledge before one victim of a fraud is tagged with the conduct of a fraudster."[72]

65. The divergence in legal approaches raises a fundamental question: should innocent shareholders bear the responsibility of the directing mind's actions where those actions themselves defraud the company and breach the directing mind's fiduciary duties to the company? This is especially so where the innocent shareholders are being penalized at the expense of their own recovery of the remaining corporate assets. As M.H. Ogilvie notes, "[t]he *Air Canada* focus on attributing another party's breach of trust to the stranger steps back several paces from a fault-based liability and begins to confuse compensation with restitution."[73] In this case, the Investor Companies become the vehicle for compensating the Bernstein Applicants for the fraud, even though the mental "fault" of these companies is derived solely from the mental state of the fraudster.

66. This question is an issue of national importance: should corporate attribution be used as a sword, to create liability, without meeting the strict requirements of *Canadian Dredge*? The second and third criteria, which the majority below relaxed, play a crucial role: they prevent the action of the directing mind from being attributed where it was "totally in fraud of the corporation" and was "intended to and does result in benefit exclusively to" the directing mind.[74] When these criteria are applied, the fraudster "ceases to be a directing mind of the corporation" because he or she is acting solely in his or her own benefit.[75] As one commentator notes, "[i]f the mental state of an individual is to be attributed to the corporation, surely that mental state should not be one of an individual who is stealing from the corporation."[76]

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[72] CA Reasons, at paras. 73, 237, LA, Tab 2D.
[73] M.H. Ogilvie, "(Un)Knowing Assistance by the Ontario Court of Appeal," (2004) 40 Can. Bus. L.J. 399, p. 410.
[74] *Canadian Dredge & Dock Co. v. The Queen,* [1985] 1 S.C.R. 662, para. 66.
[75] *Canadian Dredge & Dock Co. v. The Queen,* [1985] 1 S.C.R. 662, para. 66.
[76] Darcy L. MacPherson, "The Civil and Criminal Applications of the Identification Doctrine: Arguments for Harmonization" (2007) 45 Alta. L. Rev. 171, p. 187.

Issue 3: In granting this equitable remedy, must the court consider its effect on third parties?

67. Courts have made the protection of third parties a key tenet of equitable remedies in contexts as divergent as *Mareva* injunctions, the rescission of a contract, to the imposition of a constructive trust for breach of fiduciary duty. [77] The doctrine of knowing assistance should be no different.

68. Knowing assistance is an equitable doctrine,[78] dependent on a classic equitable formulation of whether "the stranger's conscience is sufficiently affected."[79] The inquiry into good conscience in equity "has always taken into account" the absence of an unfair or unjust effect on third parties.[80]

69. This case provides this Court with the opportunity to consider whether a court must applying the doctrine of knowing assistance, like other equitable remedies, with consideration for the protection of innocent third parties. Justice van Rensburg emphasized that, in applying equitable doctrines, the court must avoid unjust results for innocent third parties. Even where the criteria for knowing assistance are met, she concluded that equity cannot be invoked "where one group of defrauded investors seeks to obtain judgment sounding in knowing assistance against another group that has been defrauded in a similar manner."[81]

70. The majority's approach ignored these crucial considerations. There was no dispute that all the investors were innocent and that the remedy sought by the Bernstein Applicants would effectively wipe out the claims of the third party investors.[82] However, Justice Blair did not engage the question of whether or when the Court should exercise its discretion to decline a

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[77] Robert J. Sharpe, *Injunctions and Specific Performance*, looseleaf (Toronto: Thomson Reuters, 2017), at para. 2.1030. See *also Regina v. Consolidated Fastfrate Transport Inc.* (1995), 24 O.R. (3d) 564, at para. 133 (C.A.) (WL), Weiler J.A., concurring. *Kingu v. Walmar Ventures Ltd.* (1986), 10 B.C.L.R. (2d) 15, at para. 18 (C.A.) (WL); *Soulos v. Korkontzilas*, [1997] 2 S.C.R. 217, paras. 34, 45.
[78] CA Reasons, paras. 40, 245, LA, Tab 2D.
[79] *Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R. 787, p. 808.
[80] *Soulos v. Korkontzilas,* [1997] 2 S.C.R. 217, para. 34.
[81] CA Reasons, paras. 40, 248, LA, Tab 2D.
[82] CA Reasons, paras. 120-121, LA, Tab 2D.

remedy in the interest of third parties. Instead, he held that it was "hard to conceive of a case" where this discretion would be exercised. [83]

71. The consequences are readily apparent in the outcome of this case. Dr. Bernstein, the first-moving and the best-resourced fraud victim, was able to structure the recovery efforts to favour himself and his companies. The Net Tracing Analysis was not conducted to develop a full picture of the fraudulent scheme, but to determine the losses of *his* companies. Even the defined terms were defined in relation to him: the so-called Schedule C Companies (here the Walton Companies) were defined as all companies to which he did not have an interest—despite the fact that many had innocent third party investors. The DeJongs did not even know of Dr. Bernstein's litigation against the Waltons until 20 orders had been made in the proceedings.[84]

72. In the context of large complex frauds, it is critical that the Court take the interests of *all victims* into account, not just the ones who arrive first. This Court should grant leave to consider how to properly protect innocent third parties in the aftermath of a fraud.

PART IV – SUBMISSIONS WITH RESPECT TO COSTS

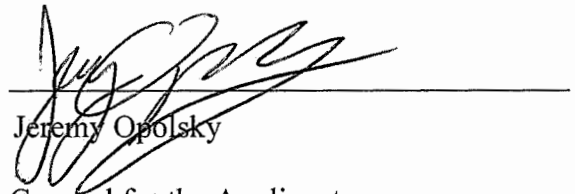
73. Given the issues of national and public importance at stake in this application, and that all parties are the victims of fraud, the applicants do not seek the costs of this application.

PART V – ORDER SOUGHT

74. The Applicant therefore seeks an order granting them leave to appeal.

March 23, 2018

ALL OF WHICH IS RESPECTFULLY SUBMITTED



Jeremy Opolsky
Counsel for the Applicant,
Christine DeJong Medicine Professional Corporation

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[83] CA Reasons, at para. 123, LA, Tab 2D.
[84] CA Reasons, at para. 169, n 18, LA, Tab 2D.

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