AMENDED THIS Oct 7 2021 PURSUANT TO
MODIFIÉ CE CONFORMÉMENT À
☐ RULE/LA RÈGLE 26.02 ( _____ )
☒ THE ORDER OF Justice Perell
L'ORDONNANCE DU
DATED / FAIT LE July 15th, 2021

REGISTRAR
SUPERIOR COURT OF JUSTICE
GREFFIER
POUR SUPÉRIEURE DE JUSTICE

Court File No. CV-16-565287-00CP

***ONTARIO***
**SUPERIOR COURT OF JUSTICE**

B E T W E E N :

THE ESTATE of BRYAN MADRYGA, BY HIS ESTATE ADMINISTRATOR REBECCA SHAW

Plaintiff

-and-

FORTRESS REAL CAPITAL INC., FORTRESS REAL DEVELOPMENTS INC., FORTRESS KEMPENFELT BAY DEVELOPMENTS INC., HARMONY VILLAGE-LAKE SIMCOE INC., CITY CORE DEVELOPMENTS INC., BUILDING & DEVELOPMENT MORTGAGES CANADA INC., ESTATE OF ILDINA GALATI by its Trustee in Bankruptcy CROWE SOBERMAN INC., DEREK SORRENTI, SORRENTI LAW PROFESSIONAL CORPORATION, GRANT EDWARDH APPRAISERS AND CONSULTANTS LTD. and IAN G. MCLEAN

Defendants

Proceeding under the *Class Proceeding Act, 1992*

**SECOND FRESH AS AMENDED STATEMENT OF CLAIM**

TO THE DEFENDANTS

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

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

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

Instead of serving and filing a Statement of Defence, you may serve and file a Notice of Intent to Defend in Form 18B prescribed by the *Rules of Civil Procedure*. This will entitle you to ten more days within which to serve and file your Statement of Defence.

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

Date December 2, 2016 Issued by "A. Miller"
Local Registrar

Address of court office: Superior Court of Justice
330 University Avenue, 9th Floor
Toronto, ON M5G 1R7

TO: **FORTRESS REAL CAPITAL INC./FORTRESS REAL DEVELOPMENTS INC**.
25 Brodie Drive, Unit 8
Richmond Hill, ON L4B 3K7

AND TO: **FORTRESS KEMPENFELT BAY DEVELOPMENTS INC**.
25 Brodie Drive, Unit 8
Richmond Hill, ON L4B 3K7

AND TO: **HARMONY VILLAGE-LAKE SIMCOE INC**.
2250 Bovaird Drive East, Unit 14
Brampton, ON L6R 0W3

AND TO: **CITY CORE DEVELOPMENTS INC**.
2250 Bovaird Drive East, Unit 14
Brampton, ON L6R 0W3

AND TO: **BUILDING & DEVELOPMENT MORTGAGES CANADA INC**.
25 Brodie Drive, Unit 8
Richmond Hill, ON L4B 3K7

AND TO: **ESTATE OF ILDINA GALATI BY ITS TRUSTEE IN BANKRUPTCY, CROWE SOBERMAN INC. c/o CROWE SOBERMAN INC., LICENSED INSOLVENCY TRUSTEE**
2 St. Clair Ave. E., Suite 1100
Toronto, ON M4T 2T5

AND TO: **DEREK SORRENTI**
Sorrenti Law Professional Corporation
310-3300 Highway 7

Vaughan, ON  L4K 4M3

AND TO: **SORRENTI LAW PROFESSIONAL CORPORATION**
310-3300 Highway 7
Vaughan, ON  L4K 4M3

AND TO: **GRANT EDWARDH APPRAISERS AND CONSULTANTS LTD**.
18 King St. East, Suite 301
Toronto, ON  M5C 1C4

AND TO: **IAN G. MCLEAN**
18 King St. East, Suite 301
Toronto, ON  M5C 1C4

## CLAIM

1. The Plaintiff, Rebecca Shaw, Estate Administrator for the Estate of Bryan Madryga ("Estate") ("Shaw"), claims on behalf of the Estate and on behalf of the proposed Class:

(a) an order pursuant to the *Class Proceedings Act, 1992*, S.O. 1992, c. 6 (the "*CPA*"), certifying this action as a class proceeding and appointing Shaw as the Representative Plaintiff;

(b) a declaration that Fortress Real Capital Inc. ("Fortress Capital") held its interest in an agreement with Harmony Village-Lake Simcoe Inc. dated April 18, 2012, relating to a real estate development located at 51, 53, 55 and 75 Bradford Street, Barrie, Ontario (the "Harmony Simcoe Project", or "The Kemp Project"), in trust for the benefit of the Estate and the Class, and that any proceeds it received or receives from the proceeds of sale of The Kemp Project are impressed with a constructive trust in favour of the Estate and the Class;

(c) if necessary, a declaration that all the remaining proceeds of sale of The Kemp Project held by FAAN Mortgage Administrators Inc. belong to the Class, and should be distributed to them *pari-passu* based upon the quantum of each Class member's investment in the syndicated mortgage loan or the Collateral Charges registered against the subject lands;

(d) a declaration that Fortress Capital, Fortress Real Developments Inc. ("Fortress Developments"), Building and Development Mortgages Canada Inc. ("BDMC"), Ildina Galati, Derek Sorrenti, and Sorrenti Law Professional Corporation breached their respective fiduciary duties owed to Bryan Madryga ("Madryga") and the Class (together, the "Investors");

(e) an accounting and equitable tracing of all funds received by the Defendants, Fortress Capital, Fortress Developments, Fortress Kempenfelt Bay Developments Inc., Harmony Village-Lake Simcoe Inc., BDMC, Derek Sorrenti, and Sorrenti Law Professional Corporation from the Investors;

(f) an order compelling disgorgement of all profits earned by those Defendants who are found by the Court to be fiduciaries of the Investors;

(g) in the alternative to subparagraph (b) above, rescission of all agreements between the Investors and the Defendants with respect to their investments in a syndicated mortgage loan (the "SML") that Harmony Village-Lake Simcoe Inc. granted to the Investors or Collateral Charges registered against title to the subject lands;

(h) a declaration that the Estate and the Class are creditors of Harmony Village-Lake Simcoe Inc. and City Core Developments Inc., and as such are complainants under s. 245 of the *Business Corporations Act*, R.S.O. 1990, c. B.16 (the "*OBCA*");

(i) a declaration that Harmony Village-Lake Simcoe Inc. and City Core Developments Inc. have acted in a matter that is oppressive, unfairly prejudicial to, and that unfairly disregarded the interests of the Investors contrary to the provisions of section 248 of the *OBCA*, entitling the Investors to damages from these defendants equivalent to the total investment losses that they have suffered;

(j) damages, including aggravated damages, in the amount of $25,000,000, or as otherwise fixed by the court;

(k) exemplary and punitive damages in the amount of $2,500,000;

(l) an order directing a reference or giving such other directions as may be necessary to determine issues not determined in the trial of the common issues;

(m) costs of this action on a substantial indemnity basis, plus the costs of any notice given to the Class, and of administering the plan of distribution of the recovery in this action, plus applicable taxes, pursuant to section 26(9) of the *CPA* on a full indemnity basis;

(n) pre-judgment and post-judgment interest at the rate of 8% interest per year, pursuant to the terms of the SML and pursuant to the terms of the Collateral Charge granted by Fortress Kempenfelt Bay Developments Inc. that replaced the SML;

(o) in the alternative to subparagraph (n), pre-judgment and post-judgment interest pursuant to ss. 128 and 129 of the *Courts of Justice Act*, R.S.O. 1980, c. 43, or such other rate as this Honourable Court deems just; and,

(p) such further and other relief as this Honourable Court deems just.

**DEFINITIONS**

2. In this claim, the following definitions are used:

(a) **"BDMC"** means Building & Development Mortgages Canada Inc., which was at all material times, a licensed mortgage brokerage firm;

(b) **"Class"**, **"Class Members"** and **"Investors"** means all persons in Canada who invested in a syndicated mortgage in respect of the Harmony Simcoe/The Kemp Project, registered against title to lands located at 51, 53, 55 and 75 Bradford Street, Barrie, Ontario as Instrument SC983678;

(c) **"CUSPAP"** means the Canadian Uniform Standards of Professional Appraisal Practice which are the professional standards that appraisers must meet in performing a real property valuation as established by the Appraisal Institute of Canada ("AACI");

(d) **"FAAN"** means FAAN Mortgage Administrators Inc.;

(e) **"Fortress Brokers"** means FFM Capital Inc., FMP Mortgage Investments Inc., and FDS Broker Services Inc.

(f) "**Fortress Defendants**" or **"Fortress"** means, jointly, Fortress Real Capital Inc. ("Fortress Capital") and Fortress Real Developments Inc. ("Fortress Developments");

(g) **"FKBD"** means Fortress Kempenfelt Bay Developments Inc., a single-purpose corporation incorporated under the laws of the Province of Ontario with an office in the Town of Richmond Hill, incorporated on June 1, 2016 to acquire and develop The Kemp lands;

(h) **"FSCO"** means the Financial Services Commission of Ontario, which regulated the financial services industry, including regulation and licensing of mortgage brokers, agents, brokerages and mortgage administrators with respect to dealing and trading in mortgages in Ontario, and which was replaced by FSRA in June 2019;

(i) **"FSRA"** means the Financial Services Regulatory Authority of Ontario, a regulatory commission established under the *Financial Services Regulatory Authority of Ontario Act*, *2016*, S.O. 2016, c. 37, Sched. 8 (the "*FSRA Act*"), replacing the Financial Services Commission of Ontario in June 2019;

(j) **"Harmony Simcoe"** or **"The Kemp"** or **"the subject lands"** refers to the real estate development project located at 51, 53, 55, and 75 Bradford Street in Barrie, Ontario;

(k) **"HVLS**" means Harmony Village-Lake Simcoe Inc., a corporation incorporated under the laws of the Province of Ontario in 1996 with an office in the City of Brampton;

(l) **"*MBLAA*"** means the *Mortgage Brokerages Lenders and Administrators Act, 2006*, S.O. 2006, c. 29;

(m) **"SML"** means the syndicated mortgage loan (a mortgage that secures a debt obligation in respect of which two or more persons are lenders) granted by Madryga and the Class to Harmony Village-Lake Simcoe Inc.;

(n) **"Sorrenti Defendants"** means Derek Sorrenti and Sorrenti Law Professional Corporation; and,

(o) **"Valuator Defendants"** means Grant Edwardh Appraisers and Consultants Ltd. and Ian G. McLean.

**NATURE OF THE ACTION**

3. This action concerns a syndicated mortgage loan made by Madryga and the proposed Class that was registered against the lands underlying the Harmony Simcoe/The Kemp Project. Investments in the SML were marketed and sold to the Class by Fortress, BDMC, and other mortgage brokerage firms or referring parties acting as subagents to BDMC and for which BDMC is liable in law.

4. The Harmony Simcoe Project lands are a 6.8 acre property located at 51, 53, 55 and 75 Bradford Street in Barrie, Ontario. The development was planned as a mixed-use residential condominium and commercial development. The legal description of the lands is set out at Schedule "A" to this Second Fresh as Amended Statement of Claim.

5. The SML went into default, along with the mortgage registered in priority to it, and the lands were sold under power of sale by the first-registered mortgagee to a Fortress-related entity, FKBD. There were no proceeds from the sale to repay the Investors the amounts owing under the SML. Instead, Fortress, FKBD, BDMC, HVLS and City Core conspired together to defeat the Investors' ability to claim against HVLS and City Core on the SML and the guarantee.

6. This conspiracy and the effect it would have on the Investors' ability to enforce their security was not disclosed to the Investors. Instead, Fortress, BDMC, HVLS and City Core Development Inc. conspired together and told the Investors the SML was still in good standing and secure after the purchase of the lands by FKBD, notwithstanding that the SML was extinguished and replaced with new Collateral Charges that were effectively unsecured. The extinguishment of the SML also extinguished the Investors' rights to pursue their losses against HVLS, and against City Core on its guarantee.

7. Thereafter, FKBD defaulted on the new first mortgage and the Collateral Charges. The subject lands were sold under power of sale. $2.2 million was payable to the Investors from the sale of The Kemp Project, and the Investors lost the balance of their capital in the amount of approximately $15,723,838, and the accrued and unpaid interest.

8. Fortress has wrongfully claimed $572,000 of the power of sale proceeds, which belong to the Investors, resulting in a delay in repayment of $700,000 by FAAN, and additional expenses being incurred to the detriment of the Investors.

9. The Defendants were negligent and made negligent misrepresentations about the value of the lands, and the nature and risks associated with investment in the SML, which induced the Investors to enter into the SML and the Collateral Charges, thereafter, to the detriment of the Investors.

10. Alternatively, the representations made by Fortress and BDMC were fraudulent in respect of the value of the subject lands, and the nature and risks associated with investment in the SML, and these fraudulent representations induced Madryga and the Class to enter into the SML.

11. Further, the Defendants, other than Sorrenti and the Valuator Defendants, conspired to, and did, cause injury to the Investors.

12. The outstanding principal owing on the SML in respect of the Harmony Simcoe/The Kemp Project is approximately $15,723,838. Interest is also outstanding and continues to accrue.

13. The Plaintiff therefore claims, on behalf of the Estate and the Class, damages equivalent to the total losses of capital that they have sustained, including interest at the rate of 8% per year.

**THE PARTIES**

14. The Plaintiff, Rebecca Shaw, Estate Administrator for the Estate of Bryan Madryga, resides in the town of Whitchurch-Stouffville, Ontario. She was Madryga's wife. Madryga died on February 8, 2021.

15. Madryga and the Class invested in a SML granted by HVLS, which was secured against a development known as the Harmony Village Simcoe Project (later, renamed "The Kemp").

16. Shaw brings this action on behalf of the Estate, and on behalf of a proposed Class defined as:

> *All persons in Canada who invested in a syndicated mortgage in respect of the Harmony Village Simcoe Project/The Kemp, registered against title to lands located at 51, 53, 55 and 75 Bradford Street, Barrie, Ontario as Instrument SC983678.*

17. Fortress Developments is an Ontario corporation incorporated on July 9, 2012, with an office in Richmond Hill, Ontario. It carried on the business of real estate development, and as a development consultant including assisting other developers in obtaining financing for their developments. Its officers and directors are Vince Petrozza and Jawad Rathore (the "Fortress Principals").

18. Fortress Capital is a federal corporation incorporated in 2009, carrying on substantially the same business as Fortress Developments, and sharing office space with it. Its sole director is Vince Petrozza.

19. Together, the Fortress Defendants facilitated providing development loans to real estate developers through syndicated mortgages sold to unsophisticated retail investors.

20. FKBD is an Ontario corporation with its head office in Richmond Hill. FKBD was incorporated on June 1, 2016, by the Fortress Principals to acquire the Harmony Simcoe Project lands under power of sale, and to continue the development of the Harmony Simcoe Project.

21. HVLS is an Ontario corporation with its head office in Brampton. HVLS was the corporate vehicle originally used to develop the Harmony Simcoe Project lands, and is an affiliate of City Core Developments Inc. ("City Core").

22. City Core is an Ontario corporation with an office in Brampton, Ontario, at the same location as HVLS. It was the guarantor of the SML. The officers and directors of City Core are the same as the officers and directors of HVLS.

23. BDMC, (formerly carrying on business as Centro Mortgage Inc. until in or about January 2016), is an Ontario corporation, which at all materials times operated from an office at the same location as Fortress in Richmond Hill. At all relevant times, BDMC was a licensed mortgage brokerage and a licensed mortgage administrator.

24. BDMC was the main mortgage broker Fortress used to raise initial financing from the investing public through syndicated mortgage loans to cover the "soft costs" of real estate developments in the early stages of development, including the Harmony Simcoe Project. In many Fortress projects, it also held the syndicated mortgage loans as a trustee for the syndicated investors, and acted as the mortgage administrator in respect of the syndicated mortgage loans, including, starting in 2016, with respect to the SML.

25. Until early 2013, BDMC acted as the mortgage broker for both Fortress and for the investors in Fortress syndicated mortgage loans. Thereafter, BDMC was not the broker of record

for the investors, but it continued to perform many functions of the mortgage broker for the investors, including conducting project due diligence reviews and drafting written disclosures for the investors - including the statutorily mandated FSCO disclosure forms - and obtaining valuations or opinions of value for the properties securing the syndicated mortgage loans, which were intended to be disclosed to the investors as part of the disclosure package. In carrying out these functions, BDMC was in a conflict of interest with respect to its duties to investors and its own financial interests.

26. As the mortgage broker and mortgage administrator for the SML, BDMC owed the Investors a duty of care to act as a reasonably prudent mortgage administrator to protect their interests under the SML, as well as fiduciary duties, and statutory duties imposed by the *MBLAA*.

27. On February 1, 2018, FSCO issued an order, on consent, revoking BDMC's mortgage brokerage license pursuant to section 19 of the *MBLAA*. BDMC was ordered to pay an administrative penalty of $400,000 pursuant to section 39 of the *MBLAA*. The license of Vince Petrozza, who was a broker with BDMC, was revoked.

28. On April 20, 2018, the Ontario Superior Court of Justice appointed FAAN Mortgage Administrators Inc. ("FAAN") as Trustee of all of the assets, undertakings and properties of BDMC, including all of the assets in the possession of or under the control of BDMC, including lenders under any syndicated mortgage, and all real property charges in favour of BDMC, until all assets under all syndicated mortgage loans have been realized and all property has been distributed to those entitled to it.

29. The Investors have been paid $1,476,162 from the proceeds of the power of sale of the subject property. FAAN continues to be the Trustee of BDMC's assets in respect of the balance of

the proceeds from the sale of The Kemp Project in the amount of $700,000. These funds belong to the Investors. FAAN agrees.

30. At all material times, Ildina Galati-Ferrante ("Galati") resided in Vaughan, Ontario and was the sole owner, and a director and officer of BDMC. Galati was a licensed mortgage broker and was the principal mortgage broker of BDMC at all material times. On or about February 1, 2018, as part of BDMC's settlement with FSCO, Galati surrendered her broker license, and was required to cease all mortgage brokering activities effective February 5, 2018.

31. Galati died on September 26, 2020. On March 17, 2021, the Galati Estate made an assignment into bankruptcy. By order of the Bankruptcy Court dated September 13, 2021, the statutory stay of proceedings as against the Galati Estate in respect of this action was lifted.

32. Derek Sorrenti ("**Sorrenti**") is a lawyer licensed to practice law in Ontario. He practices through his professional corporation, Sorrenti Law Professional Corporation ("**Sorrenti Law**"), from offices in Vaughan, Ontario. From time to time, the Sorrenti Defendants employed other lawyers, who assisted the Sorrenti Defendants in providing the services set out herein with respect to Madryga's and the Class' investments in the SML. The Sorrenti Defendants are vicariously liable for the acts or omissions of their employees.

33. The Sorrenti Defendants provided ostensibly "independent" legal advice ("ILA") to the Investors about their proposed investments in the SML, then Sorrenti acted as bare trustee to hold the Class' interests in the SML until 2016. The legal advice was not independent, and the Sorrenti Defendants breached the duty of care and fiduciary duty they owed to the Investors by providing negligent advice. Sorrenti also was negligent in fulfilling his role as the Investors' trustee.

34. Sorrenti Law also acted as the SML mortgage administrator for the Investors until 2016. Sorrenti Law was able to administer mortgages as part of a law practice, and without a licence, pursuant to an exemption in s. 5(6) *MBLAA*, and ss. 3-5 of O. Reg. 407/07 thereunder.

35. As the SML mortgage administrator, Sorrenti Law owed to the Investors, and breached:

(a) a duty of care to act as a reasonably prudent mortgage administrator to protect their interests under the SML;

(b) a fiduciary duty, and

(c) statutory duties imposed by the *MBLAA*.

36. On September 30, 2019, on the application of the Law Society of Ontario, FAAN was appointed as trustee of all of the assets, undertakings and properties of the Sorrenti Defendants relating to their professional business of trusteeship and administration of syndicated mortgage loans in Fortress projects, including all of the assets in the possession or under the control of the Sorrenti Defendants relating to their syndicated mortgage loan administration business.

37. Grant Edwardh Appraisers and Consultants Ltd. is an Ontario corporation, with its registered office in Pickering, Ontario. It carries on business as a real estate and consultancy business under the registered business name of MacKenzie Ray Heron & Edwardh ("MRHE").

38. Ian G. McLean ("McLean") was a licensed real estate appraiser, and a member of the AACI, a self-regulated body that has established professional standards for appraisers known as the CUSPAP. McLean was, at all material times, either a partner in, or an employee of, or an independent contractor of MRHE.

39. McLean prepared and signed a Current Appraisal Report (the "Appraisal") opining on the current market value of the fee simple of the Harmony Simcoe Project effective as of March 31, 2012, and dated April 12, 2012, which he signed on behalf of MRHE. The Appraisal was an update of a market value report prepared by MRHE and dated January 10, 2011. Neither report accurately provided an opinion on the current, as is, value of the subject lands in compliance with CUSPAP.

40. At all times, the Valuator Defendants knew that the primary purpose of the Appraisal was not for HVLS to secure a first mortgage to purchase the subject property, but rather, to be used for the purposes of obtaining syndicated mortgage financing through Fortress' services. It was for this reason that the appraisal was stated to be a current value report but was in fact a report on future value. This resulted in the Appraisal being for a significantly higher amount than the current value of the subject lands, which was a pre-requisite for HVLS and Fortress obtaining the syndicated mortgage financing that HVLS required.

41. At all times, the Valuator Defendants knew that the mortgage brokers who would be assisting HVLS in financing the development of the Harmony Simcoe Project were required by FSCO to produce to all syndicated mortgage lenders a copy of any existing appraisal of the property completed within the prior 12 month period, with the intent that the lender could rely upon the appraisal in making their investment decision. Hence, the Valuator Defendants knew that the Appraisal would be produced to the Investors, and relied upon by the Investors in making their investment decisions.

42. The CUSPAP standards for appraisals effective in 2012 state that appraisers must identify in their report whether the appraisal is current, retrospective, prospective or an update to a previous appraisal (Section 6.2.5). Notwithstanding this statutory obligation, the Valuator Defendants

prepared the Appraisal representing that it was a current value for the Harmony Simcoe lands, but based their conclusions on future events that had not transpired – in other words, it was a prospective valuation, not a current valuation. This was not in conformity with CUSPAP.

**MORTGAGE LAW IN ONTARIO**

43. In Ontario, the mortgage brokerage industry is governed by the *MBLAA* and its regulations. The *MBLAA* and its regulations set out standards of practice for mortgage brokerages, principal brokers, brokers, agents, mortgage administrators and brokerage officers and directors.

44. At the relevant times, the mortgage brokerage industry was regulated by FSCO and then FSRA, under the *Financial Services Commission of Ontario Act, 1997*, S.O. 1997, c. 28, and the *FSRA Act*, respectively.

45. A license is required for anyone who:

(a) solicits a person or entity to borrow or lend money on the security of real property;

(b) negotiates or arranges a mortgage on behalf of another person or entity;

(c) carries on the business of dealing and trading in mortgages;

(d) solicits a person or entity to buy or sell mortgages;

(e) buy or sells mortgages on behalf of another person or entity;

(f) lends money on the security of real property; or

(g) holds themselves out as lending money on the security of real property.

46. The *MBLAA* codifies much of the previous common law with respect to the duties of mortgage brokerages, principal brokers, brokers, agents, mortgage administrators and brokerage officers and directors. Its regulations set out high standards of practice for mortgage brokerages, principal brokers, brokers, agents, mortgage administrators and brokerage officers and directors.

47. At all times, Fortress was acting as an unlicensed mortgage broker, and in breach of the statutory duties established under the *MBLAA*. At all times, BDMC and the Sorrenti Defendants knew or ought to have known that Fortress was acting as an unlicensed mortgage broker, but they turned a blind eye to Fortress' misconduct because they wished to enrich themselves through their roles in supporting Fortress' syndicated mortgage business.

48. FSCO requires that investors receive a copy of an appraisal of the investment property based on its "as is" value, if one has been prepared within the preceding 12 months. Appraisals are to be prepared in accordance with the CUSPAP standards established by the AACI. This requirement was known to the Valuator Defendants, BDMC, Fortress, the Fortress Brokers, Galati, and the Sorrenti Defendants, but they ignored this requirement, and proceeded to provide advice to the Investors based on as-built valuations or opinions of value, which resulted in the Investors bring duped into believing their investments were fully secured on the subject lands.

**FORTRESS' BUSINESS MODEL**

49. The Fortress Defendants and BDMC followed the same business model for each of the developments in which they raised capital for developers and builders through the vehicle of syndicated mortgages sold to individual retail investors, including with respect to the Harmony Simcoe Project.

50. The Fortress Defendants acted as one corporate enterprise. Fortress Developments was primarily the entity that entered into development consulting agreements with third party developers/builders, while Fortress Capital was primarily responsible for raising investment capital through the syndicated mortgages, which would be used to fulfill Fortress' obligations under the development consulting agreements. Both companies acted in concert, shared office space, shared management and staff, and pooled their financial resources.

51. Prior to the popularization of syndicated mortgage financing in Ontario by Fortress and other companies, the financing for the soft costs of a development was usually obtained through "mezzanine" financing, which is typically only available to a developer at higher interest rates than that charged on mortgages for the acquisition of the development lands or for construction costs, both of which are registered in priority to mezzanine financing. Because of its subordinate position, mezzanine financing is risky and the interest rates are commonly as high as 30%, reflective of the degree of risk involved in the investment. The SML was equally risky.

52. Fortress followed a business model whereby it would enter into development consulting agreements with developers/builders whereby Fortress promised to provide real estate financing for the "soft costs" of the developments in return for 50% of the profits to be generated by the development. In some cases, the developer/builder would be a single purpose entity incorporated wholly or partially by the Fortress Principals, in which case, the single purpose entity would be the borrower in respect of the syndicated mortgage loan.

53. In the present case, circumstances caused Fortress and the Fortress Principals to deviate from their usual business model when the original developer, HVLS, defaulted on its mortgages. The Fortress Principals then incorporated FKBD to purchase the subject lands through a power of

sale proceeding after the development had floundered in late 2015. Instead of FKBD being the borrower for the SML, *per se*, it became the borrower in respect of a Collateral Charge that replaced the SML, as particularized below.

54. Fortress' agreements with developers/builders called for advance payments to Fortress of "anticipated profits" at the time the financing was raised. This resulted in a substantial portion of investors' money (approximately 35%) being retained by Fortress years before any profits were actually earned, if at all, diverting the loan money away from the developer or builder. Fortress used the funds that it retained to pay mortgage brokers and agents' commissions at inflated rates of 15% in total, as well as to pay the Sorrenti Defendants for the allegedly "independent" legal advice that they provided to investors (discussed further below). The rest it kept as its own profits. The fact that Fortress held back approximately 35% of the investors' funds to pay these Fortress-related fees and commissions was not disclosed to the investors, and was intentionally withheld from the investors, including the Investors, by Fortress, BDMC and the Fortress Brokers.

55. BDMC or Sorrenti Law, as the mortgage administrators, also retained another 16% of investors' capital in an "interest reserve", which was used by the mortgage administrator to pay investors the interest payable under the syndicated mortgage loans over the first two years of the mortgage's term. Effectively, this was a return of capital, as the interest paid to the investors was actually part of the capital they invested. The result was that Investors paid taxes on ostensible income that was actually a return of capital.

56. Additionally, if the "interest reserve" was depleted, then the interest was paid to the investors from the investment funds of subsequent investors, effectively operating like a "Ponzi" scheme. The payment of interest from the capital advanced is contrary to s. 23 of the *MBLAA*

Regulation 189/08, which states that a mortgage administrator shall not make a payment to a lender or investor in connection with the administration of a mortgage unless the payment is made from the funds paid under the mortgage by a borrower.

57. Fortress, BDMC, Galati and the Sorrenti Defendants knew, or ought to have known, that the structure of holding back part of the capital of the syndicated mortgage investment to pay future interest obligations on behalf of the borrower was a breach of s. 23 of the *MBLAA* Regulation 189/08, and that this information ought to have been disclosed to the Investors before they entered into the syndicated mortgage, but no such disclosure was made to the Investors.

58. The result was that the developer or builder received less than 50% of the funds raised from investors for use in the development of the project itself. This fact was not disclosed to the investors, including Madryga and the Class, was intentionally withheld from the investors, including Madryga and the Class, by Fortress, BDMC and the Fortress Brokers, and was negligently withheld by the Sorrenti Defendants.

59. Fortress raised the capital to finance the developments predominantly from small and unsophisticated investors. Syndicated mortgage loans aggregate the small investors' loans, which are held in the name of a trustee. The trustee then lends the aggregate amount of the syndicated mortgage loan capital to the developer through a loan agreement executed by the trustee acting on behalf of investors, and the loan is secured by way of a mortgage registered on title to the project lands, often listing the names of all the investors as a schedule.

60. Approximately 80 – 85% of the investors in Fortress syndicated mortgage loans held their investments in registered accounts such as registered retirement savings plans, registered education savings plans, or registered retirement income funds. The fact that the syndicated mortgage loans

were allegedly eligible to be held in a registered account was a key representation and selling feature of the Fortress syndicated mortgage loans, including the SML.

61. The Fortress syndicated mortgage loans were administered on behalf of the investors by either BDMC or by Sorrenti Law. In this case, Sorrenti Law was the administrator originally but was replaced by BDMC in 2016, at about the time that the first mortgagee began power of sale proceedings.

62. While Fortress actively marketed the syndicated mortgage loans to potential investors, including Madryga and the Class, Fortress could not sell the syndicated mortgage loans to investors directly because the Fortress Defendants were not licensed mortgage brokers. Instead, Fortress arranged for BDMC to be their front, to sell the syndicated mortgage loans.

63. BDMC both solicited investors and sold the syndicated mortgage investments to investors. It acted as the agent for both the investor and for Fortress or the developer. By acting for both the investors and the lender on the sale of the syndicated mortgage loans, BDMC acted in an undisclosed conflict of interest.

64. In 2013, Fortress entered into agreements with the Fortress Brokers to have these mortgage brokers market the mortgage investments widely to members of the public, as well as to other mortgage brokers and agents who, in turn, would act as their agents to solicit investments in the Fortress syndicated mortgage loans from members of the public.

65. Despite the interposition of the Fortress Brokers as the selling brokers, BDMC continued to perform duties that were the responsibility of a selling mortgage brokerage, and continued to provide mortgage brokerage services to the syndicated mortgage loan investors, including to those

members of the Class who invested in the SML after the Fortress Brokers commenced carrying on business. Thus, BDMC continued to act in an undisclosed conflict of interest.

66. Although Fortress was not a direct party to the sale of the syndicated mortgage loans to investors, it was actively involved in marketing the syndicated mortgage loans. Fortress developed professional sales and marketing packages in respect of the developments in which it was involved, which were disseminated widely to its network of mortgage brokers and agents. The marketing packages were also circulated directly to members of the public, and Fortress held in-person sales events or "seminars" to promote investments in its syndicated mortgage loan products.

67. Fortress prepared the marketing packages and held the marketing seminars to solicit and induce investors such as Madryga and the Class to invest in the development projects through the syndicated mortgage loans. The marketing materials represented the real estate projects as large-scale developments with blue-chip, established, and reputable builders with decades of experience. The sales pitches did not disclose that even the established builders typically used a single purpose corporation for each development to avoid liability if the development failed.

68. Particularly, and consistent with its marketing representations for all of the developments that it was financing, Fortress represented to Madryga and to the Class that the syndicated mortgage loans, including the subject SML:

(a) were fully secured against the development property;

(b) were a safe investment, providing a high (8%) rate of return, and the potential to obtain an even higher investment return through "profit participation" upon completion of the project "while still maintaining solid security and collateral on [the] principal investment";

(c) were safe, low risk, and secure investments, including that Fortress "chooses projects that have minimal zoning risk and strong sales objectives to protect the investor from any sort of protracted delays";

(d) were eligible to be held in registered accounts, which requires that the loan to value ratio be less than 100%;

(e) would pay interest at the rate of 8% per year, distributed quarterly, which would be income earned by the investor (and not a return of capital);

(f) were for a short term, of a few years, and at the end of the term, the principal would be repaid in full;

(g) in the unlikely event of default of the syndicated mortgage, the trustee would be able to take immediate steps to act upon the investors' security and would take such steps; and,

(h) appraisals of the property are provided by Appraisal Institute of Canada designated members to provide "hard, reliable valuations" which are used to assess the "loan to value" ratio of the syndicated mortgage loan.

(Together, the "Core Misrepresentations".)

69. Fortress, BDMC, Galati, and the Fortress Brokers all knew that the Core Misrepresentations were made to potential investors, including Madryga and Class, to induce them to enter into the syndicated mortgage loans, including the SML. These Defendants knew, or ought reasonably to have known that the representations were false, or they were reckless in respect of determining the veracity of the representations. These Defendants knew, or ought reasonably to have known, that the investors relied upon the Core Misrepresentations in making their decisions to invest in the syndicated mortgage loans, including the SML.

70. Fortress, BDMC, Galati, and the Fortress Brokers intended that investors, including Madryga and the Class, would rely upon the Core Misrepresentations when making their decisions to invest in the Fortress syndicated mortgage loans. The Investors did rely upon the Core Misrepresentations set out in the marketing materials and provided to them at Fortress seminars and by representatives of Fortress, BDMC, and the Fortress Brokers when the Investors decided to invest in the SML.

71. Fortress arranged for a trust company, Olympia Trust Company ("Olympia"), to act as the trustee to facilitate investors' Fortress syndicated mortgage loan investments to be held in registered accounts. To the knowledge of Fortress, BDMC, Galati, the Fortress Brokers, and the Sorrenti Defendants, Olympia was never licensed to act as a trust company in Ontario, but Olympia proceeded to carry on business in Ontario acting as trustee for the investments held in registered plans. No other trust companies or financial institutions licensed to do business in Ontario would permit registered account clients to invest in Fortress syndicated mortgages through their registered accounts. These facts were not disclosed to the Investors until August 2017, when FSCO required that Olympia cease doing business in Ontario, and long after the Investors had made their SML investments.

72. Fortress and BMDC knew that they needed evidence that the syndicated mortgage loans would qualify to be held in registered accounts, which meant proof that the loan to land ratio was less than 100%. However, these defendants did not obtain appraisals for the developments based on the actual "as is" value of the properties. Instead, they obtained either appraisals or "opinions of value" based upon a hypothetical future value calculated as if the project was completed. The appraisals or opinions of value were not compliant with CUSPAP, including the appraisals or

opinions of value prepared in respect of the Harmony Simcoe Project (the "Misrepresentation of Value").

73. As part of Fortress' marketing scheme, it conspired with BDMC, and the Fortress Brokers to, and did, misrepresent to investors, including the Investors, that the valuations on the properties were compliant with FSCO's requirements, including that the current "as-is" value of the developments were sufficiently high so that the syndicated mortgage loans were eligible to be held in registered accounts, and therefore that the loan to value ratio was less than 100%.

74. Like Fortress, BDMC, Galati, and the Fortress Brokers made the Core Misrepresentations and Misrepresentation of Value to induce investors to invest in the Fortress syndicated mortgage loans, and these defendants knew that investors, including the Investors, would rely upon these misrepresentations in making their decisions to invest in the Fortress syndicated mortgage loans. The Investors did, in fact, rely upon the Core Misrepresentations and Misrepresentations of Value of the Harmony Simcoe lands made by these defendants in deciding to invest in the SML, including the decision to hold the investments in registered accounts.

75. Had Fortress, BDMC, Galati, and the Fortress Brokers disclosed the true value of the development properties rather than grossly inflated values, none of the syndicated mortgage loans would have been registered-plan-eligible according to regulations set out by the Canada Revenue Agency, the Fortress syndicated mortgage lending scheme would never have succeeded, and the Investors would not have invested in the SML.

76. Fortress also intentionally omitted material information about the development projects it was financing in both the marketing materials and in the disclosure materials that it produced for the mortgage brokers to provide to the investors in the Fortress syndicated mortgage loans,

including the terms of its agreements with the developers or builders whereby Fortress kept a secret profit of approximately 35% of the investment funds. These misrepresentations and omissions went to the core of the investments, and were essential to determining the real risk involved in investing in the syndicated mortgage loans and to knowing the true nature of the syndicated mortgage loan investments. The omissions were made intentionally to induce the Investors to invest in the SML and are part of the Core Misrepresentations.

77. In September 2020, FRSA found that Fortress had been dealing in syndicated mortgages without a brokerage licence, and had violated s. 2(2) of the *MBLAA* twelve times. FSRA imposed a $250,000 penalty against Fortress for its violations of the *MBLAA*.

**THE HARMONY SIMCOE/KEMP PROJECT**

78. On March 20, 2012, HVLS and BDMC signed a loan commitment whereby BDMC agreed to provide HVLS with loan facilities totalling $23,210,000 to be secured by the SML against the Harmony Simcoe Project lands, "for the purposes of financing the development and the construction of residential homes on [the subject lands]".

79. Subsequently, Fortress Capital entered into an agreement dated April 18, 2012, with HVLS and City Core to provide capital for pre-construction (mezzanine-like) financing of up to $23,210,000 for the Harmony Simcoe Project, in return for Fortress receiving a 50% profit participation interest in the Project (the "Fortress Agreement"). The key provisions of the Fortress Agreement were:

(a) the terms of the Fortress Agreement were confidential to the Fortress Principals, and that confidentiality was "elemental to the business of Fortress";

(b) the maximum amount of the syndicated mortgage loan would be $23,210,000, securing two tranches of loans ("Facilities");

(i) Facility 1: $15,846,000 gross to net $10,300,000, of which Fortress would be paid Project Profits of $5,546,000; and

(ii) Facility 2: $7,363,000 gross to net $4,786,000, of which Fortress would be paid Project Profits of $2,577,000;

(c) 50% of the Project Profits were payable to Fortress as the fee for obtaining the syndicated mortgage loan, and from which Fortress would pay the deductions listed below;

(d) Fortress retained at least 35% of all amounts raised from the Investors;

(e) Fortress' Project Profits were fixed and non-refundable based upon the amount of each Facility it advanced to HVLS;

(f) the set-up costs for the syndicated mortgage loan, and a $2,500 monitoring fee would be paid to Fortress from the loan proceeds, including a $5,000 charitable donation for which City Core would receive the tax benefit;

(g) the term of the syndicated mortgage loan would be 36 months with the ability for HVLS to extend for a further 12 months;

(h) interest to be paid on the syndicated mortgage loan would be 8% per year;

(i) City Core was to pay the first year's interest, and the interest for years 2 through 4 would be paid from the funds raised in the SML; and,

(j) Fortress would pay from the Project Profits the interest payable to Investors, the Deferred Lender Fee, sales agents' fees to BDMC and Fortress Capital, the fees disclosed in Investors' Form 9d, and any Shortfall Costs.

80. The result of the Fortress Agreement was that HVLS received less than 50% of the amounts raised from the Investors. This material fact was not disclosed to the Investors by any of the Defendants.

81. HVLS retained the Valuator Defendants to provide a current value appraisal of the Harmony Simcoe Project lands.

82. On April 12, 2012, Ian McLean, on behalf of MacKenzie Ray Heron & Edwardh delivered to HVLS c/o City Core its Current Appraisal Report for the Harmony Simcoe lands effective as of March 31, 2012 (the "Appraisal"). The Appraisal was stated to have been produced in conformity with CUSPAP, but it was not. . In the Appraisal, Mr. McLean opined that the current market value of the lands was either $13,900,000 or $19,500,000 depending on the gross buildable floor area for the Project. Neither value ($13,900,000 or $19,500,000) was the current market value of the subject lands.

83. The Valuator Defendants authorized BDMC and the Sorrenti Defendants to disclose the Appraisal to Investors in Fortress' syndicated mortgage loan for the Harmony Simcoe Project, or they knew that the Appraisal was required by FSCO to be disclosed to the Investors, and acquiesced in its disclosure to the Investors.

84. The Valuator Defendants knew that the Appraisal was the *sine qua non* for the syndicated mortgage that HVLS needed to proceed with the development. Without an appraisal for the subject lands that showed a value many times the true as-is value of the Project, the loan to value ratio of the intended syndicated mortgage would not qualify for it to be held in a registered account, and no investors would participate in the syndicated mortgage. The Valuators were negligent in preparing the Appraisal when they knew it would be used for this purpose. But for the negligently prepared Appraisal, the SML would never have been granted.

85. On May 25, 2012, six weeks after the Appraisal was delivered, HVLS purchased the subject lands for $6,750,000. A first mortgage in the amount of $4,750,000 was registered against the property by the first mortgagees. The current market value of the subject property was the amount that HVLS paid for it: $6,750,000.

86. The zoning for the Harmony Simcoe Project lands had been set by the City of Barrie in 2009. In order to build the Project, HVLS needed zoning approval to increase the buildable area of the intended development significantly. HVLS planned to seek a zoning amendment, but its efforts to obtain a rezoning for the Harmony Simcoe Project ultimately failed, and it never proceeded with the development of the Project.

87. On May 25, 2012, HVLS granted the first tranche of the SML, in the amount of $4,177,000, which was registered in second priority, naming Sorrenti as the mortgagee. On May 28, 2012, the name of the mortgagee was changed to both Sorrenti (for non-registered account investors) and Olympia (for registered account investors). On June 14, 2012, the amount of the SML was increased to $7,621,000. From time to time thereafter the amount of the SML was further increased, ultimately to $19,830,000 on June 3, 2015. The subject lands were never worth the amount of the SML.

88. The firm of Legacy Global Mercantile Partners Ltd. was retained by Fortress, BDMC or Sorrenti to provide an Opinion of Market Value with respect to the Harmony Simcoe Project lands (the "Opinion"), to justify the increased amounts to be advanced under the SML.

89. The Opinion is dated February 1, 2013. The Opinion arrived at a market value for the Harmony Simcoe Project of $20 million. This was an increase in value of 44% or $6.1 million from the $13.9 million value set out in the Appraisal only ten months earlier, even though no

material change in the development had transpired. The Harmony Simcoe Project was not worth $20 million. It continued to be worth no more than approximately $6 million to $7 million.

90. Like the Appraisal, the Opinion purported to arrive at a current value for the Harmony Simcoe Project, but its analysis was based upon a future event – namely, the construction of the Project.

91. After the Opinion was obtained, BDMC and the Fortress Brokers misrepresented the current market value of the land to be $20 million in their Disclosure Statements.

92. Fortress, BDMC, and the Fortress Brokers marketed and sold the SML for the Harmony Simcoe Project to the Investors in a manner consistent with Fortress' usual business model, set out above. The marketing and sale of the SML was predominantly to unsophisticated retail investors, the vast majority of whom invested through registered plans, such as their retirement savings plans. The fact that the SML qualified to be held in a registered account was a key selling feature, emphasizing the security of the investment.

93. Madryga and the Class relied heavily upon Fortress' marketing materials, and the advice given to them by BDMC, its sales agents, or the other Fortress Brokers, all of which included the Core Misrepresentations and the Misrepresentation of Value, in making their investment decisions.

94. Fortress arranged for Sorrenti (or members of Sorrenti Law) to provide the Investors with ILA, which was paid for by Fortress, on behalf of HVLS, from the proceeds of the SML. The advice provided to the Investors was the same in each instance. A pre-set speech was delivered, often over the telephone, to the Investors, in which the Investors were assured that the SML was a low-risk, safe investment that qualified to be held in a registered account.

95. In providing its purported ILA, the Sorrenti Defendants repeated the Core Misrepresentations and Misrepresentation of Value. The Sorrenti Defendants' advice was not independent, it was misleading, and it was negligent. They provided a boilerplate promotion of the SML investment without providing a reasonable discussion of the risks associated with the SML investment, and without tailoring the advice to the client's individual circumstances, comprehension levels, or risk profile.

96. In particular, Fortress, BDMC, the Fortress Brokers, and the Sorrenti Defendants falsely represented to the Investors that:

(a) the investment was safe, and would be fully secured against the property, which was worth substantially more than the sum of the first mortgage and the total to be advanced under the SML;

(b) the appraised "as is" value of the lands was either $13,900,000, as determined by the Valuator Defendants in accordance with CUSPAP, or $20 million based on the Opinion;

(c) the investment would be for a defined term of 4 years;

(d) there would be a "steady" annual fixed distribution of 8% paid quarterly;

(e) there was a potential profit sharing of 16% at the end of the fourth year;

(f) the investment would qualify to be held in a registered account;

(g) the proceeds of the SML would be used to repay vendor take back mortgages and bridge loans, initial planning consents, attending to zoning changes, funding various consultants involved in conceiving and commencing the development, and other "soft costs" associated with the development; and,

(h) in the unlikely event of default of the syndicated mortgage, the trustee would be able to take immediate steps to act upon the Investors' security and would take such steps.

97. Fortress, BDMC, the Fortress Brokers, and the Sorrenti Defendants made these misrepresentations to induce the Investors to enter into the SML. The Investors relied upon these misrepresentations when making their investments in the SML, and they relied upon the ILA that they received from the Sorrenti Defendants to reassure them that investment in the SML was safe, secure, and appropriate based upon their investment objectives.

98. In marketing and selling the SML to Investors, Fortress was acting as an unlicensed mortgage brokerage. None of Fortress, the Sorrenti Defendants, BDMC or the Fortress Brokers disclosed this fact to the Investors.

99. Fortress, BDMC, the Fortress Brokers, and the Sorrenti Defendants failed to explain to the Investors that part of their own investments, and the investments of future Investors in the SML, would be used to pay the interest due to them under the SML – effectively that the structure for payment of the interest under the SML was tantamount to a "Ponzi" scheme.

100. Fortress, BDMC, the Fortress Brokers, and the Sorrenti Defendants failed to disclose that HVLS had no revenue sources from which to pay the interest payments due under the SML, and had no prospect of obtaining such a revenue source, since it did not even have zoning approval to proceed with the development of the planned Harmony Simcoe Project. Therefore, there was always a genuine risk that the Project would fail. It was the opposite of the safe, low-risk investment that it was represented to be. To obfuscate this reality, these Defendants misrepresented that HVLS and City Core were one and the same – that this was a "City Core development".

101. Fortress, BDMC, the Fortress Brokers, and the Sorrenti Defendants failed to disclose to the Investors what the *real* "as is" value of the subject property was (*i.e.* the then-current value of the land only, without consideration of the future planned development and construction). Nor did they disclose the true nature of the investment the Investors were making – which was in fact very risky mezzanine-like financing that would be subordinated to other mortgages to be registered on title to the Harmony Simcoe Project lands.

102. The misrepresentations set out above, at paragraphs 70, 78, 79, 81, 88 – 91, 93, 95, 97 – 100 are the "Harmony Simcoe Misrepresentations".

103. Had the true facts about the SML been disclosed to the Investors, rather than the Core Misrepresentations, the Misrepresentation of Value and the Harmony Simcoe Misrepresentations, the Investors would not have invested in the SML.

104. The ILA included the Core Misrepresentations, the Misrepresentation of Value and the Harmony Simcoe Misrepresentations, and failed to disclose many material facts about the SML, including:

(a) the SML was a high-risk investment;

(b) the actual current "as is" market value of the subject lands;

(c) the Appraisal and the Opinion were not current value appraisals, prepared in compliance with CUSPAP standards;

(d) the SML was not fully secured against the subject lands;

(e) the fact that the true loan to value ratio for the SML was well in excess of 100%, *i.e.* the amount of the SML and other debt registered against the subject lands exceeded 100% of the as is value of the land, which meant that the SMLs were not

registered- plan eligible pursuant to s. 204 of the *Income Tax Act* and s. 4900(1) of the *Income Tax Regulations*, C.R.C., c. 945, because they were not "fully secured";

(f) holding the investment in a registered plan could have adverse tax consequences for the Investor;

(g) no trust company registered to carry on business in Ontario was prepared to allow its registered account holders to hold the SML in their registered account;

(h) Olympia was not authorized to carry on business in Ontario;

(i) the fact that 16% of the capital advances would be used to pay the first two years of interest under the SMLs and future Investors' capital advances would fund the interest payments thereafter, which was a breach of *MBLAA*;

(j) the developer, HVLS, had no revenue sources from which to pay the interest payments due under the SML, and no prospect of obtaining such a revenue source, since it did not even have zoning approval to proceed with the development of the planned Harmony Simcoe Project. Therefore, there was a genuine risk that the Harmony Simcoe Project would fail;

(k) the fact that approximately 35% of the capital advances would be kept by Fortress as an unearned "profit participation" payment and that the mortgage brokers were paid a commission at a highly inflated rate;

(l) the fact that Fortress was not a registered mortgage broker, but was receiving a substantial fee for facilitating the SML for HVLS;

(m) the fact that there was no guarantee of the high rate of return set out in the SML, or any return at all;

(n) the SML would rank below other mortgages in priority of repayment, the amount of those prior ranking mortgages, and the fact that the Investors were agreeing to subordinate their position to prior encumbrances substantially greater than even the inflated values set out in the Appraisal and Opinion;

(o) HVLS had no revenue source from which to pay the interest payments due under the SML;

(p) zoning approvals were not yet in place for the proposed development upon which the Appraisal and the Opinion's assumptions were based, and therefore neither the Appraisal nor the Opinion was a hard, reliable valuation of even the projected market value of the subject lands;

(q) the borrower would have the unilateral authority to further subordinate the priority of the SML when new financing was procured, thereby increasing the risks associated with the investment;

(r) the SML Agreement contained postponement and standstill provisions which would limit the Investors' ability to enforce the SML in the event of default, and no advice was provided to the Investors as to what the terms of any such postponement and standstill would include or how that might affect the Investors' ability to enforce the SML if it went into default;

(s) the registered charge terms of the SML included a term about "Priority, Standstill, Forbearance and Postponement" that differed substantially from the disclosure about the standstill agreement in the Form 9D and the SML Agreement, and purported to prevent the Investors from acting upon their security in the event of

default or when it came due, unless the "Senior Security" lender(s) consented to such action or until all Senior Security had been repaid;

(t) while the SML would be registered on title to the property, this "security" did not guarantee repayment of the principal, as the property value might not be adequate to pay back the principal after repayment of higher-ranking lenders and it was not adequate at the time that the SML was granted; and

(u) there was no established retail market for resale of the SML, therefore it lacked liquidity.

105. The Sorrenti Defendants also failed to disclose that they were acting in a conflict of interest, because they were also acting for Fortress and BDMC, they were paid by Fortress for the service of providing the ILA, and Sorrenti and Sorrenti Law would be paid from the mortgage proceeds for acting as the bare trustee and mortgage administrator, respectively, for each person who entered into the SML. Therefore, the Sorrenti Defendants had a financial interest in ensuring that the Investors completed the SML investment.

106. The Sorrenti Defendants also failed to disclose to the Investors that they were acting for both the Investors as lenders, and HVLS as borrower in registering the mortgage, all at the expense of the Investors and not HVLS, which was negligent and a breach of fiduciary duty.

107. As Trustee, Sorrenti held title to the mortgages underlying the SML on behalf of the Investors. As mortgage administrator, Sorrenti Law was required to act in a fiduciary capacity to administer and enforce the SML. However, in both capacities, the Sorrenti Defendants failed to take any steps to protect the Investors' interests, to enforce the terms of the SML in favour of the Investors when the SML fell into default, or to advise the Investors that they could take such

actions on their own. Instead, Sorrenti quit as Trustee, and Sorrenti Law resigned as mortgage administrator when HVLS went into default, and a plan was hatched to restructure the SML to eliminate the Investors' right to enforce the debt. By abdicating these roles at the crucial time when the SML was in default, without notifying the Investors of their rights, the Sorrenti Defendants were negligent and breached their fiduciary duties owed to the Investors.

108. Sorrenti has admitted that he lacked the capacity to competently act as the SML mortgage administrator. He was, in fact incompetent and negligent in administering the SML mortgage. As mortgage administrator, Sorrenti Law owed a fiduciary duty to act only in the best interests of Madryga and the Class, which it failed to meet, as it was acting in both Sorrenti's own self-interest and in the interests of Fortress and the developer/borrower at the same time.

109. Despite Fortress and BDMC's representation that Fortress chose only projects with "minimal zoning risk", the Harmony Simcoe Project had substantial zoning risk and failed, in part, because HVLS was not able to secure the necessary approvals to construct the planned development.

110. Despite all the Defendants' assurances that the SML was a safe and secure investment, HVLS defaulted on paying the quarterly interest payments when due. The SML thereby went into default on or about October 15, 2015. No steps were taken by Sorrenti Law, the mortgage administrator, to enforce the SML, including making a demand to City Core on its guarantee.

111. In failing to protect the interests of the Investors once the SML was in default, Sorrenti Law breached its statutory and fiduciary duties as mortgage administrator and breached the duty of care that it owed to the Investors. The Investors suffered damages as a result thereof.

112. Neither the Sorrenti Defendants nor BDMC advised the Investors of their enforcement rights once the SML went into default. They were negligent in failing to do so.

113. On April 4, 2016, the first mortgagee commenced power of sale proceedings, as that mortgage was also in arrears.

114. On or about August 24, 2016, the mortgage administrator was changed from Sorrenti Law to BDMC, without the knowledge or consent of the Investors. The trustee of the SML changed from Sorrenti to BDMC for those Investors who held the SML in a cash account, and to Olympia for those who held the investment in a registered account. The Sorrenti Defendants did not explain to the Investors the reason for their departure as trustee or mortgage administrator, including Sorrenti Law's inability to perform the mortgage administration job adequately. Before leaving, the Sorrenti Defendants did not warn the Investors about their rights to enforce the SML, which was in default and was largely unsecured against the subject lands, or if he had executed a standstill agreement that might prevent the Investors from enforcing their security. This was negligent, and caused harm to the Investors.

115. By agreement dated September 28, 2016, the first mortgagee agreed to sell the Harmony Simcoe Project under the power of sale to FKBD for $22,837,989 - the amount of the outstanding mortgage debt. This amount vastly exceeded the true fair market value of the subject lands and was a fabricated purchase price as part of a conspiracy to defraud the Investors of their enforcement rights against HVLS and City Core under the SML by giving the Investors the false impression that the Harmony Simcoe lands were worth almost $23 million.

116. The sole purpose for establishing the inflated "sale price" for the Harmony Simcoe Project was to deceive the Investors into believing the Harmony Simcoe Project was worth more than the inflated amounts set out in the Appraisal and the Opinion and to hide the fact that the SML had no value from the Investors.

117. The purchase price was paid by FKBD obtaining a new first mortgage for $7 million from Vector Financial Services Limited, which was used to pay out the first mortgagee. The balance of the purchase price would be "paid" by FKBD granting a new collateral charge for the total capital owing to Investors under the SML in the amount of $17,165,713, which would be held 47.34% by BDMC (for the non-registered account holders) and 52.66% by Olympia (for the registered account holders) as the trustees. The original SML would be discharged from title. Additionally, the outstanding SML interest of $784,269 would be "secured" against the subject land as another collateral charge that would be non-interest-bearing, even though unpaid interest was to be compounded under the SML.

118. On or about November 7, 2016, BDMC notified the Investors that FKBD would be purchasing the subject property, and a new project design would be submitted for approval. BDMC advised that, as part of the purchase, FKBD agreed to take title to the project subject to a "Collateral Charge", which was a new mortgage on the same terms as the SML, and also subject to a second charge capitalizing the unpaid interest owed to the Investors. Both Collateral Charges would be administered by BDMC. The term of these Charges was also extended from the SML due date.

119. Counsel for Madryga wrote to Galati and BDMC on behalf of Investors on November 14, 2016. In the letter, counsel advised that the development loan and SML were in default (a fact not disclosed in BDMC's November 7 letter). Counsel wrote that, as trustees, Sorrenti and Olympia

had an obligation to take reasonable steps on behalf of all Investors to enforce Investors' security and had failed to do so. At this time, the Investors had not been notified that BDMC had assumed the duties of Sorrenti as a trustee.

120. The letter put BDMC, the Sorrenti Defendants, Olympia, and the other Defendants on notice that Sorrenti and Olympia no longer had the authority to act on behalf of Investors with respect to the SML. Counsel advised that their clients did not agree to any transfer of title of the Harmony Simcoe Project lands to FKBD, nor to capitalization of principal and past due interest.

121. No reply was received to the letter, and BDMC acted without the Investors' authority thereafter.

122. BDMC agreed to grant the new Collateral Charges on behalf of the Investors even though there was no value in the subject lands to support the charges, and contrary to the letter from Madryga's Counsel.

123. BDMC agreed to grant the new Collateral Charges on behalf of the Investors without first advising the Investors of their options following HVLS's default, including their right to make demand for immediate payment from the guarantor, City Core. Nor were the terms of the new Collateral Charges explained to the Investors, including that the new first-ranking mortgage was for a greater amount than the prior first mortgage, and that these Collateral Charges would be subordinated to new financing required to continue the development. BDMC did not advise the Investors that City Core was not providing a guarantee of the Collateral Charges, and that, by the granting of the Collateral Charges, the Investors would be losing the right to pursue their losses against City Core under its guarantee, which would be extinguished through the power of sale.

There were material omissions which BDMC, as mortgage administrator, was duty bound to disclose to the Investors before taking actions on their behalf.

124. On November 28, 2016, BDMC sent a letter to the Investors stating that, under the terms of the power of sale:

(a) FKBD would be assuming the mortgage debt of HVLS. The letter did not disclose that the Investors' security would be subordinate to a new first-priority mortgage of $7 million instead of the previous first mortgage of $4.75 million;

(b) the administrator of the mortgage would be BDMC, replacing Sorrenti Law;

(c) BDMC would replace Sorrenti as trustee for the Investors – which in fact had occurred months earlier without notice to the Investors;

(d) BDMC would presume that Investors agreed with BDMC's decisions relating to the Project, if the investor did not object within 10 business days of being provided with notice of its recommendations;

(e) only a majority vote of Investors in the SML would be required for BDMC to proceed with investment decisions for all Investors;

(f) BDMC had authority to postpone or "pause" future interest payments owing to Investors in favour of construction financing, which would rank ahead of the SML;

(g) the Collateral Charges could be postponed to any "non-financial charge";

(h) Investors would be prevented from taking civil action against BDMC with respect to "any losses suffered due to the negligence" of HVLS (but not with respect to BDMC's own negligence in administering the mortgage); and,

(i) if an Investor did not execute the documents, then the Investor's position in the SML would not be transferred to the new Collateral Charge mortgage to be granted

by FKBD, meaning "that [the Investor would] have to work directly" with HVLS and City Core to "recover [their] original investment and any outstanding interest they may be owed".

125. The November 28, 2016, letter did not address the following key information that the Investors required to understand the status of their investment:

(a) the SML was, and continued to be in default, therefore the Investors could start power of sale proceedings or other legal action to enforce their security, including bringing a claim against City Core on its guarantee;

(b) neither BDMC nor the trustees would take any steps on behalf of the Investors to recover on the defaulted SML;

(c) if the trustees had entered into a standstill agreement on behalf of the Investors, and if so, whether that prevented them from enforcing their security in the event of default;

(d) an accounting of how the funds that they had invested had been used by HVLS, and how much, if any, remained unspent;

(e) HVLS and City Core would have no ongoing liability to the Investors and the ability to sue on the guarantee would be lost;

(f) whether the trustees would continue to act on behalf of the Investors, if they did not sign onto the Collateral Charges;

(g) if a current appraisal of the lands was obtained to ensure FKBD purchased the lands at full market value, and, if so, what the appraised value was; and

(h) why BDMC was recommending this approach as opposed to advising the Investors to simply enforce their security.

126. On November 30, 2016, title to the Harmony Simcoe Project lands was transferred by power of sale by the holders of the first mortgage to FKBD. The SML was deleted from title.

127. On the same day, FKBD gave a mortgage to Vector Financial Services Inc. in the amount of $7 million. This mortgage amount exceeded the $5,677,025.56 in cash paid by FKBD, meaning FKBD did not put any equity into its purchase of the Harmony Simcoe Project lands.

128. The excess amount raised by FKBD, about $1.3 million, was put into an interest reserve used to pay the high rate of interest due to Vector under its mortgage. This money was improperly retained by FKBD and ought to have been used by FKBD to pay down the amounts owing to the Investors under the SML.

129. On December 1, 2016, the holders of the Collateral Charge mortgage transferred it to BDMC and Olympia. The transfer lists all 360 Investors in the SML in a schedule and confirms the total amount of their investments was $17,165,713.

130. BDMC circulated a "Memo" to Investors dated December 6, 2016, that disclosed the purchase of the Harmony Simcoe Project lands by FKBD on November 30, 2016, via power of sale, and that it had renamed the project The Kemp. This was the first time Investors were advised that a power of sale had been issued on the Harmony Simcoe Project.

131. The Memo stated falsely that the transactions "[preserved Investors'] mortgage and security under the new purchaser and borrower".

132. Fortress, BDMC and FKBD conspired with HVLS and City Core to intentionally omit the material facts about the true value of the Harmony Simcoe lands to give the illusion that there was

still value in the SML investments, to encourage the Investors to participate in the Collateral Charges, and to thereby shelter HVLS and City Core from claims by the Investors in respect of HVLS's default under the SML.

133. In fact, the subject lands were only worth the cash paid by FKBD. The original first mortgagee had attempted to sell the property under its power of sale for $8 million, which was the approximate appraised value of the subject lands based upon appraisals obtained by the first mortgagee, and had received no offers. This material fact was also omitted by BDMC and FKBD when they were encouraging the SML Investors to participate in the Collateral Charges.

134. the Investors were not advised the Notice of Power of Sale was issued, or that the appraised value of the Harmony Simcoe Project lands was no more than $8 million. This material information was intentionally withheld from the Investors as part of the conspiracy between BDMC, Fortress, FKBD, HVLS and City Core. Alternatively, BDMC was negligent and made a negligent omission of material fact in failing to disclose this material information to the Investors.

135. Fortress, BDMC, HVLS, City Core, and FKDB all knew that the Investors would not be repaid their investments, or the amounts that were secured by the Collateral Charges. This was intentionally not disclosed to the Investors. These defendants knew their actions in November and December 2016 would cause damage to Investors, and would enrich BDMC, HVLS, City Core and FKDB.

136. Thereafter, additional mortgages were granted by FKBD and the Collateral Charges were postponed in favour of these mortgages, with the Collateral Charges ultimately ending up as 4$^{th}$ and 5$^{th}$ placed charges.

137. The Kemp Project was a disaster. It was never built out by FKBD. It was sold on September 10, 2019, under power of sale by the new first priority mortgagee. After repayment of amounts owing to the first, second and third priority mortgagees, approximately $2.2M remained as residual proceeds, which are payable in full to the Investors.

138. Fortress and a third party have submitted a claim to approximately $572,000 of the residual proceeds in priority to the Investors. The current mortgage administrator, FAAN disagrees with Fortress' claim, but has held back $700,000 from distribution to the Investors pending resolution of the Fortress claim. Fortress' claim to these funds is without merit. All the remaining proceeds of sale of the Harmony Simcoe Project belong to the Investors as the holders of the Collateral Charges.

139. Fortress' false claim to the sale proceeds has caused FAAN to incur costs needlessly, which will be charged against the remaining proceeds of sale. Fortress is liable to the Investors for all such costs charged or incurred by FAAN.

**FSRA AND RCMP INVESTIGATIONS**

140. In or around December 2015, FSCO, which, at the time, had regulatory authority over the mortgage industry, commenced an investigation into Fortress, BDMC, and the Fortress Brokers arising from concerns about the conduct and administration of syndicated mortgage loans arranged by Fortress with the aid of BDMC, the Fortress Brokers, and the Sorrenti Defendants.

141. In 2016, FSRA began issuing consumer communications to the investing public stating that it considers syndicated mortgage loan investments to be "high risk" investments that were often marketed to the investing public using techniques that belie the true risks of the mortgages.

That was, in fact, the case with respect to the marketing and sale of Fortress' syndicated mortgage loans including with respect to the Harmony Simcoe Project.

142. The regulators' investigation culminated in settlement agreements between FSRA and each of BDMC and the Fortress Brokers, executed on January 31, 2018, which, amongst other things resulted in orders that:

(a) revoked the mortgage broker licenses for:

(i) BDMC;

(ii) Vincent Petrozza;

(iii) each of the principal brokers of the three Fortress Brokers;

(b) required BDMC to pay administrative penalties of $400,000; and

(c) required each of the Fortress Brokers to pay administrative penalties of $235,000.

143. BDMC agreed that FAAN would assume the mortgage administration for all Fortress-related syndicated mortgages that BDMC had been administering. Additionally, Galati surrendered her license, thereby ceasing all mortgage brokering activities.

144. In or around March 2018, BDMC (through its newly-formed alter ego corporation Canadian Development Capital & Mortgage Services Inc., which was run by Galati's mother, Giuliana Galati) engaged in various acts in breach of the FSCO settlement, including acting to frustrate FAAN's ability to carry out its role as administrator of the syndicated mortgages.

145. To prevent further harm to investors, including to Madryga and the Class, which would have been caused by continued breaches and obstruction of FAAN's operations, on April 20, 2018, on the application of the Superintendent of Financial Services, FAAN was appointed as trustee, without security, of all the assets, undertakings and properties of BDMC. Since that date, FAAN

has been the mortgage administrator with respect to the Investors' investment through the Collateral Charges.

146. At the time of FAAN's court appointment, BDMC was administering forty-five Fortress syndicate mortgage loan projects, including The Kemp.

147. On September 9, 2020, FSRA entered into a settlement with Fortress Developments, pursuant to which it imposed administrative penalties against Fortress Developments in the amount of $250,000 for 12 contraventions of s. 2(2) of the *MBLAA*, related to Fortress Developments providing services to borrowers for the purpose of financing property developments when it was not licensed to do so.

148. On April 13, 2018, the RCMP's Integrated Market Enforcement Team obtained a search warrant for Fortress, BDMC and the Fortress Brokers in connection with a fraud investigation into Fortress's syndicated mortgage businesses. In the search warrant, the investigators asserted their belief that the key aspects of this fraud occurred from 2012 to 2017 and include:

(a) investors were presented with inflated "as is" property values for the lands securing their syndicated mortgage loans, which misrepresented the true risk of the investments and their ineligibility for investment through a registered plan;

(b) the actual loan to property value ratios in respect of the syndicated mortgage loans exceeded 100%;

(c) the syndicated mortgages were promoted as being registered plan eligible, when they were not, and therefore that investors who invested through registered plans could be subject to adverse taxation by the Canadian Revenue Agency; and

(d) investment funds were used for purposes other than what was disclosed to investors. A portion of the investors' funds were not directed to the development project and instead were retained by Fortress at the time of placement of the loan.

149. These allegations were true with respect to the Harmony Simcoe Project and the SML. Fortress was engaged in a fraudulent scheme. BDMC, Galati, and the Fortress Brokers were either complicit in the fraud, or they were reckless, or negligent with respect to their role in the scheme. The Sorrenti Defendants were at least grossly negligent with respect to their role in the scheme, if they were not complicit in the fraud.

150. In sum, the actions of Fortress, BDMC, Galati, and the Fortress Brokers in facilitating the SML exposed the Investors to tremendous risk due to its financing structure, which included high professional fees, advance profit sharing, lack of proper appraisal, and automatic subordination of creditor priority. The real risks of the SML were intentionally not disclosed to Investors at the time they invested, to induce them to invest so that Fortress could take excessive and unearned profits, and so these other defendants would also profit at the expense of the Investors.

**MADRYGA'S INVESTMENT IN THE KEMP PROJECT**

151. Madryga's investment in the SML is representative of the investments made by all of the Investors. The Defendants engaged in the same misconduct with all the Investors as they engaged in with Madryga.

152. In or about April 2012, Madryga met Graham McWaters ("**McWaters**"), a registered mortgage agent with Centro Mortgage Inc. ("Centro", now known as BDMC) who was soliciting investments in Fortress syndicated mortgages at an investor forum. McWaters recommended that Madryga make an investment in a Fortress syndicated mortgage.

153. McWaters invited Madryga to a Fortress seminar on May 10, 2012, where Madryga heard a presentation by Rathore, and at which he obtained Fortress' marketing material about the Harmony Simcoe Project. Fortress representatives stated during the seminar that the Harmony Simcoe Project, with its retirement focus, was in high demand because of the aging baby boomer population. The Core Misrepresentations, the Harmony Simcoe Misrepresentations, and the Misrepresentation of Value were made to Madryga by BDMC and Fortress representatives during the seminar.

154. At no time was Madryga told that the developer did not have the necessary zoning approvals for the project to move forward, that there were significant concerns being expressed about the density of the Project, or that the Project was nowhere near ready to commence construction. These facts were material and were omitted from all the disclosures that Madryga received about the Harmony Simcoe Project from any of Fortress, BDMC or Sorrenti.

155. McWaters recommended to Madryga that he set up an RRSP account with Olympia, so that he could hold the SML investment as an RSP investment. Madryga did so.

156. Centro (BDMC) was Madryga's mortgage broker with respect to his investment in the SML.

157. In reliance upon (i) the oral and written representations made to him by McWaters, (ii) the oral and written representations by Fortress at the investment seminar and in its marketing materials (including the Core Misrepresentations, the Harmony Simcoe Misrepresentations, and the Misrepresentation of Value), including that the developer was associated with City Core, and that City Core was providing a guarantee of the SML, and (iii) from the purportedly "independent" legal advice later provided to him by Sorrenti Law, Madryga decided to proceed with an

investment in the SML in the principal amount of $25,000, which represented 0.33% of the total SML of $7,621,000 to be granted to HVLS. The SML was for a four-year term, and the interest rate was fixed at 8% per year, compounding annually. Madryga was to receive quarterly payments of $500 until maturity.

158. Had any of the material omissions set out above been disclosed to Madryga, or had any of the misrepresentations set out above not been made by Fortress and BDMC to Madryga, he would not have invested in the SML. In particular, Madryga would not have made this investment if he been advised of any of:

(a) the true as-is value of the lands;

(b) that the zoning for the Harmony Simcoe Project had not been approved, and might never be, and that the opinion of value in the Appraisal was dependant upon the zoning being changed;

(c) the fact that the SML would not qualify as an investment in a registered account;

(d) the terms of Fortress' agreement with HVLS; and,

(e) the actual risks associated with the SML investment.

159. On June 15, 2012, BDMC wrote to Madryga enclosing documents for him to review and to execute before completing the investment in the SML. The documents sent to Madryga were:

(a) Investor/Lender Disclosure Statement ("Disclosure Statement") for brokered transactions, which included a copy of the appraisal of the property prepared by the Valuator Defendants;

(b) Attestation (proof of identity);

(c) Investment Authority – Form 9D, in favour of Sorrenti;

(d) Mortgage Commitment from Derek Sorrenti, in trust (as bare trustee) on behalf of Madryga as lender/mortgagee to BDMC on behalf of HVLS as borrower/mortgagor and City Core as guarantor;

(e) the SML Agreement;

(f) Memorandum of Understanding from Madryga to BDMC that included confirmation of BDMC's duties to him as the mortgage broker, and that McWaters was only making a referral, and was not acting as Madryga's mortgage broker;

(g) Authorization;

(h) Mortgage investment direction and indemnity agreement; and

(i) Solicitor's certificate of disclosure and undertaking regarding arms-length mortgages from Sorrenti.

160. The letter included a "Project Fact Sheet" provided jointly by BDMC and Fortress Capital. The Project Fact Sheet included the following representations:

(a) a valuation of the lands had been provided by Ian G. McLean, AACI, of MacKenzie, Ray Heron & Edwardh;

(b) there was a first mortgage of $4,750,000;

(c) the loan to value ratio was 89% based on the first mortgage and the SML, which was the second mortgage;

(d) the purposes for the monies raised in the SML were first to meet the funding requirements of the development, and second to create an "interest reserve";

(e) if interest was not paid when due, it would continue to accrue, and would be paid out at the time of maturity of the SML;

(f) Fortress Capital and licensed parties at BDMC would receive additional remuneration based upon the profitability and successful completion of the development, which would be calculated as a percentage of profits in the Project;

(g) the preliminary development *pro formas* indicated that Harmony Simcoe would have sales revenues in excess of $155.8 million, and net profits of over $16.8 million.

161. McWaters purportedly reviewed Madryga's investment objectives and risk tolerance with him and negligently advised Madryga that the investment in the SML was appropriate for him. BDMC did not conduct any Know Your Client ("KYC") review with Madryga.

162. McWaters conveyed to Madryga the information which had been provided to him by BDMC and Fortress, including advising Madryga that the SML was a secure second mortgage with little or no risk, in keeping with Madryga's risk tolerance and investment objectives. None of McWaters, BDMC, nor Sorrenti reviewed the true risks associated with the SML investment in Harmony Simcoe with Madryga. No one advised Madryga that the SML was a high-risk investment that did not qualify to be held in a registered account, and that the true current value of the land was less than $7 million. If this information had been disclosed to Madryga, he would not have invested in the SML.

163. The Disclosure Statement confirmed that it had been completed by Ildina Galati on behalf of BDMC. In this statement, Galati, on behalf of BDMC, falsely represented to Madryga that the "as is" value of the land to be secured by the SML was $13,900,000, and that the loan to "as is" value of the land was 89%. It disclosed one prior encumbrance in the amount of $4,750,000. The Disclosure Statement did not disclose the purchase price paid by HVLS for the subject lands, nor

did it include HVLS's agreement of purchase and sale for the subject lands, although this, too, was required by FSCO to be included in the disclosure package.

164. The Disclosure Statement did not include:

(a) documentary evidence of HVLS's ability to meet the mortgage payments;

(b) a detailed description of the Project;

(c) a schedule of the funds that had been advanced or were to be advanced to the borrower; or

(d) the identity of the person who was supposed to monitor the disbursement of funds to the borrower,

all of which was also disclosure required by FSCO.

165. The Disclosure Statement falsely represented to Madryga that the only fees and costs to be paid by HVLS with respect to the loan were: (i) a legal fee of $2,500 to Derek Sorrenti, (ii) a broker fee of $750 to Centro (BDMC), and (iii) a "referral fee" of $1,250 to BDMC (Altaview LK). The Disclosure Statement did not disclose the 35% in fees HVLS had committed to pay to Fortress with respect to this financing. This omission was a material omission about which all of BDMC, Galati and the Sorrenti Defendants were aware, and which they intentionally or negligently failed to disclose to Madryga.

166. The Disclosure Statements delivered to each of the Class Members was in the same form, and also made the same material omissions, of which BDMC, Galati, the Fortress Brokers and the Sorrenti Defendants were aware, and intentionally or negligently failed to disclose to the Class.

167. Madryga signed the Disclosure Statement on June 20, 2012, in compliance with the instructions from BDMC that it had to be signed and dated two days before the rest of the documentation.

168. The Memorandum of Understanding confirmed that BDMC, as the licensed mortgage broker, owed duties to Madryga, including the duty to ensure that the SML was a suitable investment for him based upon his knowledge, risk tolerance and investment objectives, to investigate the merits of the development project and disclose all relevant information and risks about the project to Madryga, and to disclose any conflicts of interest to Madryga. BDMC did none of these things.

169. On June 25, 2012, Madryga attended a meeting with McWaters to sign the balance of the documents sent to him by BDMC. Another individual was at the meeting to commission or notarize certain documents.

170. At the meeting on June 25, 2012, Madryga executed a Declaration of Bare Trust in respect of the SML, which confirmed that Derek Sorrenti, as bare trustee, would be holding Madryga's interest in the SML in trust for him.

171. On June 25, 2012, Madryga, as lender/mortgagee, executed the SML Agreement with HVLS as the borrower/mortgagor, and City Core as guarantor. The key provisions of the SML Agreement are as follows:

(a) HVLS was the borrower, and City Core was the guarantor to a maximum of $23,210,000;

(b) Madryga agreed to lend $25,000 to HVLS through the SML;

(c) the SML was to be registered against the Harmony Simcoe Project lands as a second mortgage, and would be registered in the name of Derek Sorrenti, as bare trustee;

(d) Derek Sorrenti would act as trustee for all non-registered Investors and Olympia would be the trustee for the registered Investors;

(e) the total amount of the SML was $7,621,000, but could be amended to a maximum of $23,210,000;

(f) the SML was for a 48-month fixed-rate open term, scheduled to mature on April 26, 2016, but with an option by HVLS to extend for an additional 6 months to October 26, 2016;

(g) HVLS agreed to pay interest at 8% annually, payable quarterly in the amount of $500.00;

(h) the SML could be subordinated to construction financing or replacement land acquisition financing to a maximum of $140 million; and

(i) in the event of default by HVLS, the unpaid balance of the SML and all accrued interest would become immediately due and payable.

172. The terms of the mortgage were supposed to be attached to the SML Agreement, but were not included. Madryga did not receive a copy of the charge terms until he received Sorrenti's reporting letter on or about September 7, 2012. The charge terms were never reviewed with Madryga by the Sorrenti Defendants.

173. The SML Agreement stated that there was to be an "interest reserve" held by Sorrenti Law, as mortgage administrator. The Agreement did not disclose that the "interest reserve" was to be made up of part of the funds advanced by the SML Investors. Rather it implied that the reserve would be funded by the borrower. Nor was the true nature of the "interest reserve" explained to

Madryga (or the Class) by the Sorrenti Defendants or BDMC. This was a material omission. If this fact had been disclosed to Madryga or the Class, neither he nor the Class would have invested in the SML.

174. The SML Agreement provides that Sorrenti, as trustee, was not to advance the loan funds to the borrower until certain conditions were met, including receipt of an AACI Appraisal reflecting a value of $13,900,000 authored by the Valuator Defendants. No such AACI Appraisal was received by Sorrenti, so advancing the funds to HVLS was in breach of trust and breach of contract.

175. At the June 25, 2012, meeting, Madryga executed the documents necessary for the $25,000 SML investment and the fees to be paid to Sorrenti, in trust.

176. During the meeting to sign documents, Madryga had a telephone call with Derek Sorrenti (or a Sorrenti Law lawyer acting under Sorrenti's direction) during which Madryga was provided with allegedly ILA about the SML. The call lasted approximately 30 minutes, during which Madryga was given a *pro forma* review of the documentation to be signed, but was not provided with any ILA about the investment.

177. During the call, the documents to be signed were described briefly to Madryga, and the structure of the investment was discussed. Madryga was told that the structure of the Harmony Simcoe Project was similar to that of other Fortress projects.

178. None of the significant risks associated with investing in the SML were reviewed with Madryga. None of the Core Misrepresentations, Misrepresentation of Value, or the Harmony Simcoe Misrepresentations were identified as misrepresentations. None of the Sorrenti

Defendants' multiple and conflicting roles, nor Olympia's role, were explained to Madryga. Madryga received no explanation about how the SML might be enforced if it went into default, or the effects of the anticipated standstill agreement in the SML Agreement.

179. Madryga signed the documents as he was directed, and $25,000 was transferred from his Olympia RRSP to Sorrenti, in trust.

180. As the mortgage administrator, Sorrenti Law also had an obligation to advise Madryga of the real risks associated with the SML, including the actual value and loan to equity ratio of the subject property. Sorrenti ignored his legal obligations under the *Rules of Professional Conduct* to disclose conflicts of interest, including that he was paid by Fortress to provide ILA to Madryga about the Fortress investment.

181. Fortress, BDMC and the Sorrenti Defendants knew or ought to have known that this SML was inconsistent with Madryga's risk profile, and that selling the investment to him was contrary to Fortress and BDMC's obligations under ss. 43 and 45 of the *MBLAA* and ss. 4, 12, 18, 24, 25, 26 and 27 of Regulation 188/08 and s. 10.1 of Regulation 189/08. Fortress and BDMC, nonetheless, sold him the SML. All these defendants failed to provide proper advice to Madryga, in breach of their duties owed to him. In the result, Madryga has suffered the loss of his investment, including interest at the rate of 8% per year.

**THE CAUSES OF ACTION**

182. The Plaintiff's claims asserted against some or all of the Defendants are:

(a) Conspiracy;

(b) Oppression;

(c) Fraudulent misrepresentation/deceit;

(d) Negligent misrepresentation;

(e) Negligence;

(f) Breach of fiduciary duty; and

(g) Breach of Contract.

## A. CONSPIRACY

183. Fortress, BDMC, FKBD, HVLS and City Core conspired with each other with the intent to cause injury to the Investors. The particulars are set out in the facts above and summarized here.

184. Fortress, BDMC, HVLS and City Core conspired together to obtain a grossly inflated "current value" valuation from the Valuator Defendants in the Appraisal, and then later with respect to the Opinion. These Defendants used the Appraisal and then later the Opinion as the valuation that they were required to disclose to the Investors, and to give the appearance that the subject lands had a much greater value than they were actually worth, and thereby to make it appear that the SML qualified as an investment that could be held in a registered account. These defendants also used the Appraisal to assure the Investors that the SML was a low-risk investment, fully secured against the subject property, when they knew that it was not a low-risk or secured investment.

185. Fortress, BDMC, HVLS and City Core conspired together to make the Harmony Simcoe Misrepresentations and the Misrepresentation of Value to the Investors, including omitting to disclose the material facts about the actual risks associated with the SML, all as set out above. These defendants knew that they were misrepresenting the true state of affairs to the Investors. These defendants knew, that Madryga and the Class relied upon these misrepresentations and omissions of material fact in making their SML investment decisions, and they knew that the Investors would suffer losses with respect to their investments in the SML. These defendants made

the misrepresentations with the intent to cause harm to Madryga and the Class, which is what transpired.

186. Further particulars of the conspiracy among Fortress, BDMC, HVLS and City Core are:

(a) Fortress arranged to have Olympia act as the trustee for Investors who wished to hold the SML in a registered account, when Olympia could not lawfully fulfill that role in Ontario, after Fortress found that no qualified trustee was prepared to act as such in respect of any Fortress syndicated mortgage loan;

(b) BDMC, Galati, and HVLS knew that Olympia could not legally act as a trustee in Ontario and that no qualified trustee would act;

(c) Fortress, BDMC, Galati, and HVLS agreed not to disclose this fact to the Investors because it was integral to their marketing plan for the SML that it qualify as an investment in a registered account, and that, if the SML was not registered-account-qualified, then Fortress and BDMC would be unable to raise the funds that HVLS required, and none of these defendants would profit from the investment.

187. HVLS, City Core, Fortress, FKBD, and BDMC conspired to facilitate the sale of the Harmony Simcoe Project property to FKBD, structured in a way that: concealed the true value of the subject property from the Investors; concealed that, at the time of the sale, the SML was wholly or largely unsecured; and concealed that the value of the subject property did not secure the Collateral Charges which replaced the SML.

188. When FKBD took title to The Kemp Project, each of HVLS, City Core, Fortress, FKBD, and BDMC knew that the lands were worth $8 million or less, that the prospects of the planned development obtaining the requisite zoning approvals to proceed had become remote, and that it

was unlikely that the SML Investors would ever recover the full amount of their investments, even if the project did proceed to be built out.

189. Fortress, FKBD, BDMC, HVLS and City Core conspired each with the other to misrepresent to Madryga and the Class that the Collateral Charges would be fully secured against the subject property, and that the Investors were receiving a charge of equal value in exchange for the SML, when in fact the Collateral Charges had little or no value, and, by putting the Investors into the Collateral Charges, the Investors lost the ability to pursue claims against HVLS and City Core with respect to their defaults under the SML. In doing so, FKBD, BDMC, HVLS and City Core were enriched and the Investors were injured.

190. Fortress, BDMC, FKBD, HVLS and City Core agreed among themselves that they would not disclose to, and would actively hide from, the Investors that the Collateral Charges were effectively worthless. Instead, they agreed that BDMC and FKBD would assure the Investors that the Collateral Charges were fully secured against the subject lands, and that the Investors would have the same rights and entitlements as they had had under the SML, which was false.

191. Fortress, BDMC, FKBD, HVLS and City Core agreed among themselves that these material facts would not be disclosed to the Investors. Rather, these defendants agreed that, instead of taking title to the lands under the normal power of sale process—which would have extinguished the SML, and which would have allowed the Investors to pursue HVLS under the terms of the SML Agreement and to pursue City Core on its guarantee—FKBD would agree to provide the Collateral Charges, into which BDMC placed the Investors, and then have the SML extinguished through the power of sale proceeding. Based upon the current value of the subject lands, the prior

registered mortgage, the subordination terms in the Collateral Charges, these charges were effectively unsecured.

192. The result was, as Fortress, BDMC, FKBD, HVLS and City Core intended, that the Investors lost their right to claim for their SML investment losses against HVLS and City Core, and were placed into new charges that had virtually no security, were not qualified to be held in a registered account, and for which the Investors had no recourse in the event of default. The conspiracy between these defendants was intended to, and did, cause injury to the Investors.

193. Fortress, FKBD, BDMC, HVLS and City Core further agreed and conspired together that BDMC would not take any steps on behalf of the Investors to enforce their security under the SML, and would, instead, put the Investors into the Collateral Charges. In doing so, BDMC, FKBD, HVLS and City Core were enriched and the Investors were injured.

194. The actions of BDMC, HVLS, City Core, and FKBD were unlawful. They conspired to, and did, cause harm to the Investors equal to the total of their lost investments in the SML and interest at the rate of 8% per year.

## B. OPPRESSION

195. The Investors were creditors of HVLS and City Core, and as such they assert that they are complainants under s. 245 of the *OBCA*, and therefore are proper persons to assert claims for relief from oppression under s. 248 of the *OBCA*.

196. By engaging in the conspiracy set out above, including allowing BDMC to misrepresent the nature and effect of the Collateral Charges, and not disclosing that this would preclude the Investors from pursuing claims against HVLS and City Core under the terms of the SML and the

guarantee, HVLS and City Core engaged in conduct that was oppressive, unfairly prejudicial to, or that unfairly disregarded, the interests of Madryga and the Class.

197. The Estate therefore claims against HVLS and City Core for all of its and the Class' losses arising from the extinguishment of their rights under the SML, equal to all lost capital and interest thereunder.

## C. FRAUDULENT MISREPRESENTATION/DECEIT

198. Fortress, BDMC, Galati, and the Fortress Brokers made fraudulent misrepresentations to Madryga and the Class.

199. By soliciting investments in the SML, and acting as mortgage brokers for the Investors in respect of their SML investments, Fortress and BDMC were in a direct and proximate relationship with the Investors, and owed them the duty of care of a reasonably competent mortgage broker, which these defendants breached by making fraudulent misrepresentations about the SML investments.

200. These defendants knowingly made the Core Misrepresentations, the Harmony Simcoe Misrepresentations, and the Misrepresentation of Value to the Investors as set out herein, which they knew the Investors would rely upon in making their investment decisions, and which included:

(a) misrepresenting that the SML was a safe and secure investment, fully secured on the Harmony Simcoe lands, and omitting to disclose the material risks associated with the development and the investment;

(b) misrepresenting that the SML qualified as an investment that could be held in registered accounts and that the loan-to-value ratio of the Harmony Simcoe project was 89%;

(c) misrepresenting that the then-current "as is" value of the Harmony Simcoe lands was as set out in the Appraisal and Opinion, and intentionally concealing that the valuations in the Appraisal and Opinion were not prepared in compliance with CUSPAP standards, and were not current value valuations;

(d) omitting to tell the Investors that HVLS would receive no more than 50% of the funds raised in the SML and that Fortress would retain approximately 35% of the funds, including to pay Fortress for an unearned profit participation;

(e) failing to disclose that 16% of the funds paid by the Investors would be used to fund an "interest reserve" and would be used to pay the first two years of interest payments due under the SML, and that the funds of future Investors in the SML would be used to pay the interest thereafter, and therefore the payment of interest under the SML was actually a return of capital, not profits, and was structured effectively as a Ponzi scheme, and in breach of s. 23 of Regulation 189/08 of the *MBLAA*;

(f) failing to disclose that brokerage commissions amounting to 15% of the funds raised would be paid to various brokers, agents and referring parties, which was substantially higher than typical commissions in the mortgage industry, and much greater than the brokerage fees which were disclosed to the ;

(g) misrepresenting to Investors that they would receive ILA from the Sorrenti Defendants, when, in fact, Fortress retained the Sorrenti Defendants, and paid for

this legal advice on behalf of the borrower, and the Sorrenti Defendants were in a position of conflict, given that they would earn income as the trustee and mortgage administrator;

(h) misrepresenting that advances made under the SML would be based upon the "achievement and completion of certain development and construction milestones" based on reports from the cost consultant retained to work on the Harmony Simcoe Project, when in fact the funds were immediately disbursed by Sorrenti Law;

(i) misrepresenting that the SML would not be subordinated to any other mortgage, other than construction financing;

(j) omitting to disclose to the Investors that Olympia was not authorized to carry on business in Ontario as trustee for the registered plan SML investments, and that no trust companies or financial institutions licensed to do business in Ontario would permit registered plan clients to invest in Fortress syndicated mortgages through registered accounts that they administered;

(k) omitting to disclose material facts about HVLS's inability to meet project development milestones and to obtain zoning approvals for the Harmony Simcoe lands, and, in fact, misrepresenting that zoning approvals had already been obtained for the Harmony Simcoe lands;

(l) concealing from Investors the fact that HVLS had no intention to proceed with the Harmony Simcoe Project if the significant zoning changes needed for the project were not approved by the City of Barrie, yet still marketing and selling the SML to Class members after this fact were known;

(m) misrepresenting that the SML would be repaid when it came due when these defendants knew or were reckless in failing to confirm that zoning approval and construction could not be completed by the date that the SML came due, and still selling the SML to Class members after these facts were known;

(n) omitting to disclose that the registered terms of the SML included a term about "Priority, Standstill, Forbearance and Postponement" that differed substantially from the disclosure about the standstill agreement in the Form 9D and the SML Agreement, which purported to prevent the Investors from acting upon their security in the event of default or when it came due, unless the "Senior Security" lender(s) consented to such action or until all Senior Security had been repaid;

(o) misrepresenting that HVLS and FKBD had injected capital into the Harmony Simcoe Project, when it was 100% debt financed; and,

(p) misrepresenting the nature and effect of the Collateral Charges and omitting to disclose that, by taking the Collateral Charges, the Investors would lose the ability to bring proceedings against HVLS and City Core under the terms of the SML Agreement. These misrepresentations were made, *inter alia*, in the November 28, 2016, letter sent to Investors.

201. In making their decisions to invest in the SML, the Investors each relied on the fraudulent misrepresentations by Fortress and BDMC (and the Fortress Brokers) to their detriment. They relied upon the further fraudulent misrepresentations in allowing BDMC to transfer their security from the SML to the Collateral Charges. Madryga and the Class have suffered the loss of their capital and interest at the rate of 8% per year because of these defendants' fraudulent misrepresentations.

## D. NEGLIGENT MISREPRESENTATION

202. In deciding to invest in the SML, Madryga and the Class each relied to their detriment on the negligent misrepresentations made by Fortress, BDMC, Galati, the Sorrenti Defendants and the Valuator Defendants. They have suffered the loss of their capital and interest at the rate of 8% per year as a result thereof.

### a. The Mortgage Brokers

203. By soliciting investments in the SML, making representations upon which they knew the Investors would reasonably rely, and acting as mortgage brokers for the Investors in respect of their SML investments, Fortress, BDMC, Galati, and the Fortress Brokers were in a direct and proximate relationship with the Investors, and owed them the duty of care of a reasonably competent mortgage broker (and, in the case of Galati, a reasonably competent principal broker of a mortgage broker), which these defendants breached by making the Core Misrepresentations, the Harmony Simcoe Misrepresentations, and the Misrepresentation of Value negligently.

204. In the alternative to paragraphs 198 – 201, above, if the representations set out in those paragraphs were not made to the Investors by Fortress, BDMC, Galati, and the Fortress Brokers fraudulently, then they were made negligently by all of Fortress, BDMC, Galati, and the Fortress Brokers.

205. These defendants knew, or ought reasonably to have known that these misrepresentations were untrue when they were made. These defendants knew, or ought reasonably to have known, that the Investors would rely upon the misrepresentations in making their decisions to invest in the SML, and the Investors did so rely, to their detriment.

**b. Sorrenti Defendants**

206. The Sorrenti Defendants were in a direct and proximate relationship with the Investors in respect of each of the four separate roles that the Sorrenti Defendants held with respect to the Harmony Simcoe Project, *i.e.* (i) as solicitor providing legal advice; (ii) as lawyer representing the Investors in completing and registering their investment in the SML; (iii) as trustee holding title to the SML on behalf of the Investors, and subject to the terms of the Memorandum of Understanding; and (iv) as mortgage administrator. The Sorrenti Defendants were negligent in performing their duties in each such role.

207. The Sorrenti Defendants negligently made the Core Misrepresentations, the Harmony Simcoe Misrepresentations, and the Misrepresentation of Value to the Investors at the time that Sorrenti or Sorrenti Law employees provided the ILA.

208. The Sorrenti Defendants knew, or ought reasonably to have known that these misrepresentations were untrue when they were made. These defendants knew, or ought reasonably to have known, that the Investors would rely upon the misrepresentations in making their decision to invest in the SML, and the Investors did so rely, to their detriment.

**c. HVLS, City Core and FKBD**

209. BDMC acted as the agent for each of HVLS, City Core and FKBD in making the misrepresentations to the Investors about the true state of affairs at the time of the purchase of the Harmony Simcoe Project under power of sale by FKBD as set out above. HVLS, City Core and FKBD are liable for the injuries caused to the Investors as a result of the misrepresentations of their agent.

210. These defendants knew, or ought reasonably to have known, that these misrepresentations were untrue when they were made. These defendants knew, or ought reasonably to have known, that the Investors would rely upon the misrepresentations in making their decision to invest in the SML, and the Investors did so rely, to their detriment.

## E. NEGLIGENCE

211. Each of the defendants was in a proximate relationship with the Investors, giving rise to a duty of care.

212. Fortress, BDMC, and Galati owed the Investors a duty of care based on the special relationships between them, as set out above in the sections addressing fraudulent and negligent misrepresentation.

213. BDMC, HVLS, City Core and FKBD owed the Investors a duty of care arising from their representations to the Investors about the nature of the Collateral Charges that they proposed that the Investors agree to enter into to replace the SML, and which induced the Investors to agree to the Collateral Charges, rather than enforcing their rights under the SML.

214. The Sorrenti Defendants were in a direct and proximate relationship with the Investors in respect of each of the four separate roles that they held with respect to the Harmony Simcoe Project, *i.e.* (i) as solicitor providing legal advice; (ii) as lawyer representing the Investors in completing and registering their investment in the SLM; (iii) as trustee holding title to the SML on behalf of the Investors, and subject to the terms of the Memorandum of Understanding; and (iv) as mortgage administrator. The Sorrenti Defendants were negligent in performing their duties in each such role, and as a result of this negligence, the Investors were injured.

215. The Valuator Defendants were in a proximate relationship with the Investors because these defendants knew and consented to, or acquiesced in, the Appraisal being provided to the Investors as part of the disclosure package regarding the SML, and as proof of the then-current as is value of the Harmony Simcoe lands. The Valuator Defendants also knew and consented to, or acquiesced in, the valuation of the Harmony Simcoe lands from the Appraisal being reported to the Investors as the current, as is, value of the lands based upon CUSPAP standards, as part of BDMC's disclosure package regarding the SML. The Valuator Defendants knew the Investors would rely upon the Appraisal and the report of the current value of the Harmony Simcoe lands in the Disclosure Statement in making the decision to invest in the SML.

216. Each of the defendants, other than HVLS and FKBD, was in a proximate relationship with the Investors such that they knew, or ought reasonably to have known that their acts or omissions in respect of their roles in the SML investments could cause injury to or damage to the Investors if they failed to take reasonable care. Their negligence did cause harm to the Investors, and was the proximate cause, or contributed to the investment losses that the Investors have suffered.

217. The particulars of these defendants' negligence is set out above, and includes the following.

**a. Negligence of all Defendants**

218. The defendants failed to disclose the actual as-is value of the Harmony Simcoe lands to the Investors at the time that they invested in the SML and/or at the time of the conversion of the SML to the Collateral Charges.

219. They knew, or ought to have known, that the actual as-is value of the subject lands rendered the SML and the Collateral Charges ineligible for investment in registered plans, and they did not disclose this to the Investors.

220. They preferred their own interests and those of their co-defendants to those of the Class Members and failed to advise the Investors that they were making this preference.

**b. Negligence of Fortress, BDMC and Galati**

221. These defendants failed to ensure that the SML complied with all legal requirements and that proper disclosure of all material risks was made to the Investors.

222. These defendants created and disseminated the promotional materials which were inaccurate, false, deceptive, misleading, and failed to contain material information, and which were designed to convince the Investors of the safety and high return of the SML investment, which these defendants knew or ought to have known was untrue, the particulars of which are set out above.

223. These defendants marketed the SML to the Investors in a manner that was inaccurate, false, deceptive, misleading, and failed to contain material information, and which was designed to convince the Class Members of the safety and high return of the SML investment, which these defendants knew or ought to have known was untrue.

224. These defendants marketed the SML to the Investors as safe and secure investments when they knew the SML was a risky investment, and that because there was no or insufficient security for the SML, it was not suitable for any retail investors.

225. BDMC and Galati worked intimately with Fortress to market and solicit Investors for the SML when they knew that Fortress was dealing in mortgages without a licence under the *MBLAA*.

226. Fortress undertook the duties of a mortgage brokerage under the *MBLAA* when these defendants knew that neither Fortress entity was licensed as a mortgage brokerage, and BDMC and Galati allowed Fortress to fulfil mortgage broker functions, including selling investments in the SML, that ought to have been performed by them.

227. Fortress introduced the Harmony Simcoe Project investment to the Investors when only a licensed mortgage brokerage was entitled to make such introductions and BDMC (and the Fortress Brokers) allowed Fortress to do so.

228. These defendants failed to ensure that the investments in the SML were appropriate investments for each investor based on the investor's sophistication, investment objectives, and risk profile, and in fact, they failed to fulfill any of the KYC functions required of a mortgage broker before placing the Investors into the SML.

229. These defendants withheld from the Investors the fact that approximately 35% of the principal amount advanced under the SML was used to pay for "development consultant fees", all of which were paid to Fortress and not to actual consultants with respect to the development of the Harmony Simcoe Project.

230. These defendants withheld the fact that 50% of the development consultant fee would be paid to brokers, BDMC (in its capacity as borrower's broker), and Fortress.

231. These defendants failed to fulfill the obligations of a mortgage brokerage (and, in the case of Galati, the obligations of a principal broker of a brokerage) to ensure that the SML complied

with all legal requirements and that complete and accurate disclosure of all material risks was made to the Investors. This included failing to provide Investors with all of the accurate and true information and documents required by FSCO to be produced, and as enumerated in the Disclosure Statement.

232. These defendants failed to ensure that the Investors obtained genuine ILA, and instead they arranged ILA for the Investors that was designed to promote the SML as a safe investment, and to encourage the Investors to invest in the SML.

233. These defendants withheld from the Investors that the ILA from the Sorrenti Defendants was paid for by Fortress, and that Sorrenti Law would be paid fees to act as the mortgage administrator – and therefore the ILA was not truly independent.

234. These defendants failed to disclose to the Investors that Olympia was not authorized to carry on business in Ontario as trustee for the Fortress registered plan SML investments, and that no trust companies or financial institutions licensed to do business in Ontario would permit registered plan clients to invest in Fortress syndicated mortgages through registered accounts that they administered.

235. These defendants knew or ought to have known HVLS had not disclosed information which adversely affected or would be reasonably be seen as adversely affecting the Harmony Simcoe Project lands or HVLS' ability to perform its obligations, as HVLS was obligated to do under the provisions of the SML Agreement (Article 6.01(h)).

236. These defendants failed to ensure that the SML was not subordinated to any other mortgage other than construction financing.

237. These defendants failed to warn or inaccurately explain that "construction financing" references in the SML documents included all the funds needed to complete the Project that were not financed by the SML, including further "mezzanine" debt.

238. These defendants facilitated the events of November and December 2016 and then the events from December 2016 to May 2018 without the consent or approval of the Investors.

239. When the FKBD / Vector mortgage was arranged, these defendants failed to ensure that the excess of mortgage funds over the amount paid to the holder of the prior first-priority mortgage was paid out to the Investors.

240. These defendants failed to provide the Investors with truthful, clear and transparent information about the material facts, risks and fees payable related to SML.

241. These defendants withheld and/or concealed the potential and actual conflicts of interest amongst the entities involved in the SML, specifically the relationships between Fortress, BDMC, and the Sorrenti Defendants.

242. These defendants marketed and recommended the SML to the Investors when it was not an appropriate investment for any investor, as it was neither safe nor secure and, in fact, was a fraudulent scam.

243. These defendants failed to recommend products and/or services that were suitable for the Investors based on their specific circumstances.

244. These defendants failed to provide competent mortgage broker services to the Investors.

### c. Negligence of the Valuator Defendants

245. The Valuator Defendants knew that Fortress was a syndicator of mortgages, and they provided the Appraisal to Fortress and BDMC, or consented to HVLS providing the Appraisal to Fortress and BDMC, knowing that, once in BDMC's possession, BDMC would be obliged to produce it to the Investors pursuant to the *MBLAA*.

246. The Valuator Defendants acquiesced in, or consented to, the Appraisal being used by HVLS and by Fortress, BDMC and any other mortgage brokers selling the SML to raise money from Investors through a syndicated mortgage loan.

247. The Valuator Defendants knew that if they delivered an Appraisal that was based upon the true as-is market value of the subject lands, then HVLS, Fortress and BDMC would be unable to secure syndicated mortgage financing. The Valuator Defendants negligently prepared the Appraisal for HVLS and Fortress showing an inflated current value for the subject lands so that HVLS, Fortress and BDMC would be able to secure investors in the SML. But for the Appraisal, there would have been no SML, and the Investors would have suffered no loss.

248. The Valuators acquiesced in or consented to the Appraisal being provided to the Investors by BDMC, the Fortress Brokers and/or the Sorrenti Defendants, and knowing that the opinion on value stated therein would be relied upon by the Investors.

249. The Valuator Defendants knew that the Sorrenti Defendants would use the Appraisal in providing ILA to the Investors, and that both BDMC and the Sorrenti Defendants would produce the Appraisal to the Investors as part of meeting the disclosure obligations of mortgage brokers

under *MBLAA* and as set by FSCO. The Valuator Defendants acquiesced in or consented to the Appraisal being used for this purpose.

250. The Valuator Defendants' undertaking specifically contemplated that: the Appraisal would be used by Fortress and BDMC to induce investments in the SML; BDMC would use the quantum of the appraised value of the subject lands in its disclosure statement, as well as to confirm that the SML qualified as a registered account investment; it would be used by the Sorrenti Defendants in providing ILA to the Investors; and it would be relied upon by the Investors for these purposes.

251. The Valuator Defendants consented to each such use of the Appraisal. Any limiting language in the Appraisal with respect to the use that could be made of the Appraisal was waived by them either expressly or implicitly.

252. The Valuators were therefore in a proximate relationship with the Investors and owed them the duty of care of a reasonably competent real property valuator to provide an opinion on the current value of the Harmony Simcoe lands that was CUSPAP compliant, and that accurately reflected the current, as is, value of the subject lands.

253. The Valuator Defendants knew that the Investors would reasonably rely upon the Appraisal and the representation of current value from the Appraisal which was included in BDMC's disclosure package in making their decisions to invest in the SML. It was reasonably foreseeable that the Investors would suffer injury by relying on these representations, because the Appraisal was not prepared to CUSPAP standards, was negligently prepared, and provided an opinion that purported to be a current value report but was in fact a report on future value, and which was therefore grossly inflated from the actual as-is value of the subject lands.

254. The Investors did rely upon the Appraisal and the representation of current value from the Appraisal in BDMC's disclosure package in making their decisions to invest in the SML. But for the stated current value of the subject lands in the Appraisal, the Investors would not have entered into the SML. The losses that they have suffered of their capital and interest at the rate of 8% per year were direct and foreseeable, and the Valuator Defendants are liable therefor.

**d. Negligence of the Sorrenti Defendants**

255. The Sorrenti Defendants were in a direct and proximate relationship with the Investors in respect of each of the four separate roles that they held with respect to the Harmony Simcoe Project, *i.e.* (i) as solicitor providing legal advice; (ii) as lawyer representing the Investors in completing their investment in the SLM; (iii) as trustee holding title to the SML on behalf of the Investors, and subject to the terms of the Memorandum of Understanding (Sorrenti, only); and (iv) as mortgage administrator (Sorrenti Law).

256. The Sorrenti Defendants owed the Investors a duty of care to act as reasonably prudent real estate solicitors in providing them with ILA and in acting on their behalf in completing their investment in the SML.

257. Sorrenti owed the Investors a duty of care to act as a reasonably prudent trustee in fulfilling his role as the SML trustee, including compliance with the contractual provisions with respect to that role.

258. Sorrenti Law owed the Investors a duty of care to act as a reasonably prudent mortgage administrator in performing that role with respect to the SML.

259. The Sorrenti Defendants were negligent in performing their duties in each such role, as particularized above at paragraphs 70, 78, 79, 81, 88 – 91, 93, 95, 97 – 100, 103 – 111, 174 - 179 and below with respect to breach of fiduciary duties. The breaches of fiduciary duty were also acts of negligence by the Sorrenti Defendants.

## F. BREACH OF FIDUCIARY DUTY

260. The Investors were in a fiduciary relationship of trust and confidence with the Sorrenti Defendants and BDMC. These defendants had the ability to exercise discretion or power to affect the interests of the Investors, making them vulnerable to these defendants' actions. As such, these defendants were required to act honestly, in good faith, and strictly in the best interests of the Investors.

261. The Sorrenti Defendants and BDMC owed fiduciary duties to the Investors to:

(a) act honestly, in good faith and in their best interests;

(b) exercise the care, skill, diligence and judgment that a prudent investor would exercise in investing their funds (BDMC);

(c) exercise the care, skill, diligence and judgment of a reasonable solicitor in providing ILA and in representing them with respect to their investment in the SLM, including registration of the SML charge on title (the Sorrenti Defendants);

(d) exercise the care, skill, diligence and judgment of a reasonable trustee (Sorrenti, and then BDMC);

(e) consider all relevant criteria about the Harmony Simcoe Project before recommending an investment in the SML;

(f) determine the true current value of the Harmony Simcoe lands, and advise the Investors accordingly;

(g) ensure that documentation provided to them sufficiently established the current value of the Harmony Simcoe lands;

(h) disseminate accurate and truthful information about the Harmony Simcoe Project; and,

(i) warn Investors, before creating and administering the trust, that the SML was high-risk, unsecured, and a grossly improvident bargain.

262. The Sorrenti Defendants and BDMC both breached the fiduciary duties that they each owed to the Investors, as particularized above with respect to the allegations of negligent misrepresentation and negligence. These defendants both acted in their own self-interest, to the detriment of the Investors in the SML. They misrepresented material facts about the SML and omitted to disclose other material facts. Their negligence, negligent misrepresentations and breach of contract were also breaches of their fiduciary duties owed to the Investors.

263. With respect to Sorrenti and then BDMC's role as a trustee on behalf of SML Investors, Sorrenti and/or BDMC breached their fiduciary duties in the following respects:

(a) BDMC was in a conflict of interest as a result of the conflicting roles of a trustee for the Investors in addition to its role as the selling brokerage;

(b) they acted as a co-trustee with Olympia when they knew that Olympia was carrying on business unlawfully in Ontario;

(c) they knew the SML investment funds were not being used for "land acquisition costs and initial soft costs, and the costs incidental thereto" as represented, yet they took no steps to prevent such unauthorized use being made of the funds, and

allowed the SML funds to be disbursed to the borrower, when the conditions to do so had not been met;

(d) they failed to obtain the necessary information and ensure that the conditions precedent were met prior to making advances to HVLS and FKBD;

(e) Sorrenti failed to register the SML charge on title in a form that was consistent with the SML Agreement, but rather included terms that were more onerous than those to which the Investors agreed;

(f) Sorrenti failed to ensure the SML was only subordinated to other mortgages as agreed upon in the investment documentation;

(g) they used a portion of the Investors' own funds, which they held in the Interest Reserve Account, to pay the interest owing on the SML, rather than requiring the borrower to fund the Interest Reserve Account from its own sources;

(h) they failed to disclose to the Investors that the interest payments were actually a return of capital and not interest;

(i) once the SML went into default, they failed to take steps to enforce the Investors' security as they were obligated to do under the SML Agreement's terms;

(j) once the SML went into default, they failed to properly inform Investors of the default and obtain their instructions as to what steps should be taken to enforce their rights;

(k) BDMC sent out incorrect and misleading information in the memos sent to Investors in November and December of 2016;

(l) BDMC facilitated the events of November and December 2016 and then the events from December 2016 to May 2018 without the consent or approval of Investors; and

(m) BDMC failed to meet its obligations with respect to the interests of the Investors when the Harmony Simcoe lands was sold under power of sale.

264. Insofar as Fortress was acting as an unlicensed mortgage broker, it, too, owed the Investors all the duties of a mortgage broker at common law and under the *MBLAA*.

265. Fortress breached its fiduciary duties, as particularized above, including:

(a) it assumed the duties of a mortgage brokerage under the *MBLAA* when it knew it was not licensed by FSCO as a mortgage brokerage;

(b) it introduced the Harmony Simcoe investment to the Investors when only a licensed mortgage brokerage was entitled to make such introductions;

(c) it failed to take the steps required of a mortgage brokerage to ensure that the SML complied with all legal requirements and that proper disclosure of all material risks were made to the Investors;

(d) it failed to ensure the investments in the SML were appropriate investments for each Investor based on the Investor's background and risk profile, and based upon client suitability forms accurately completed following a KYC interview with each Investor;

(e) it marketed and recommended the SML as a safe and secure investment when it knew it was a risky investment not suitable for any Investors;

(f) it made the misrepresentations particularized above in marketing and selling the SML investments to the Investors;

(g) it failed to ensure the Investors obtained genuine ILA, and instead arranged for ILA that was not truly independent, as it was prepackaged and paid for by Fortress, and was delivered by the Sorrenti Defendants, who were in an undisclosed conflict of interest, and it did not warn the Investors of the risks associated with investment in the SML or the true nature of the Harmony Simcoe Project;

(h) it utilized the services of Olympia to hold the SML investments in the Investors' registered plan accounts, when it knew Olympia had been turned down for a license to carry on business by FSCO but had unlawfully decided to carry on business in Ontario as the trustee of Fortress syndicated mortgage loans;

(i) it did not disclose to the Investors that no trust company or financial institution authorized to carry on business in Ontario was prepared to hold Fortress syndicated mortgage loans in registered accounts;

(j) it knew HVLS had not disclosed information which adversely affected or would be reasonably seen as adversely affecting the Harmony Simcoe Project lands or HVLS' ability to perform its obligations, as HVLS was obligated to do under the provisions of the SML Agreement, Article 6.01(h), but nevertheless continued to solicit Investors in the SML and induce them to enter into the SML while HVLS was in default under the Agreement;

(k) it facilitated the events of November and December 2016, leading to the creation of the Collateral Charges and the discharge of the SML, and the loss of the Investors' right to pursue HVLS and City Core's debt obligations under the SML; and,

(l) it has asserted that it has a priority claim to the balance of the proceeds of sale of the subject lands, although the Investors are secured lenders and any debt owed to Fortress or other third parties is unsecured.

266. The Investors were entirely reliant on the skill and expertise of Fortress, BDMC and the Sorrenti Defendants. The Investors were in a wholly vulnerable position relative to these defendants.

267. Fortress, BDMC and the Sorrenti Defendants breached their fiduciary duties owed to the Investors, resulting in the Investors sustaining the loss of their investments.

## G. BREACH OF CONTRACT

### a. HVLS and City Core

268. The Investors entered into the SML Agreement with HVLS and City Core. HVLS defaulted on the SML, and thereby breached its contract with the Investors.

269. For the duration of the SML, HVLS failed to notify the Investors about any information adversely affecting the Harmony Simcoe Project and HVLS' assets, liabilities, affairs, business, operations or conditions, financial or otherwise, or its ability to perform its obligations under the SML. It did not disclose the fact that it could not obtain the zoning approvals necessary for the Project to proceed. It did not disclose that it paid funds from the SML to Fortress for "anticipated profits", when no profits had been earned by the Project, thereby diverting the funds from their intended use for the Project's development. These failures to disclose were all in breach of Article 6.01(h) of the SML Agreement.

270. HVLS's failure to disclose these facts to the Investors, and its intentional misrepresentations, were in breach of HVLS's duty to act honestly and in good faith with respect to its obligations under the SML.

271. HVLS's misrepresentations and omissions were a breach of contract that prevented the Investors from being able to take timely action to enforce their mortgage security and City Core's guarantee.

272. HVLS paid Fortress "advances on profits" before any profits had been earned in respect of the Harmony Simcoe Project, in breach of the purposes for which the SML funds were advanced by the Investors, which was bad faith performance of the SML Agreement, and caused damage to the Investors, as the funds advanced were not used for their stated and intended purpose.

273. HVLS and City Core acted in bad faith by allowing BDMC to misrepresent to the Investors the nature and effect of the proposed new Collateral Charges to be granted by FKBD on the sale of the subject lands and by conspiring with BDMC, Galati and FKBD to extinguish their debt obligations owed to the Investors and to replace their security with the effectively unsecured Collateral Charges, as set out above. HVLS and City Core had a positive duty to the Investors in performing their obligations under the SML to correct the misrepresentations and they failed to do so, in breach of their duty of good faith and honest performance of the contract.

274. Accordingly, all principal and all interest accrued before and after default of the SML, and all costs of recovering the debt is now due and owing to the Investors by HVLS and City Core.

**b. BDMC and Galati**

275. The Investors signed a Memorandum of Understanding ("MOU") with BDMC and retained BDMC as their mortgage broker. Where an Investor retained one of the Fortress Brokers, BDMC acted as agent for the Fortress Broker in fulfilling the role of mortgage broker for that Investors.

276. In the Memorandum of Understanding provided to Madryga, BDMC set out its duties to him as including the following:

(a) Suitability of the lender

(b) Know Your Client (KYC);

(c) Documentation Completion;

(d) Merits of the Project;

(e) Risk Disclosure; and

(f) Conflict of interest disclosure.

277. BDMC failed to meet its contractual and fiduciary obligations owed to Madryga and the Class under the MOU and as their mortgage broker. As set out above in detail, it:

(a) failed to make any effort to meet its KYC obligations with respect to any of the Investors;

(b) failed to disclose the risks associated with the SML investment;

(c) failed to ensure that an investment in the SML was an appropriate investment for each of the Investors based upon their investment objectives, sophistication, and risk tolerance;

(d) failed to ensure that the valuation of the Harmony Simcoe lands was a current value valuation prepared in compliance with CUSPAP standards; and

(e) failed to provide the Investors with a current value valuation prepared in compliance with CUSPAP standards.

278. As the principal broker of BDMC, Galati had a statutory duty under the *MBLAA* and its regulations to ensure that BDMC and its brokers and agents complied with the *MBLAA*'s provisions. She knew of these obligations but failed to meet them.

279. Galati knew BDMC's breach of contract would cause harm to the Investors. As principal broker, she did nothing to prevent those breaches from happening, contrary to her statutory obligations under the *MBLAA.* As principal broker, she did nothing to develop policies for BDMC that would prevent those breaches from happening or recurring, contrary to her statutory obligations.

280. These breaches were all a breach of BDMC's duty to act honestly and in good faith with respect to its obligations as principal broker and under the MOU.

281. Had BDMC met its contractual obligations to them, the Investors never would have invested in the SML, and they would not have suffered any loss.

282. After BDMC assumed the role of trustee and mortgage administrator, it breached the express or implied terms of its contract with the Investors by failing to take any steps to enforce the SML once it fell into default.

283. BDMC failed to fulfil its duties as mortgage administrator honestly and in good faith by:

(a) causing the Investors to give up their rights of enforcement under the SML and putting them into the Collateral Charges without instructions to do so;

(b) misrepresenting to the Investors the purpose and effect of the Collateral Charges; and

(c) failing to take any steps to enforce the Collateral Charges when they also fell into default.

284. Because of BDMC and Galati's breach of their contractual obligations to the Investors, the Investors lost the opportunity to enforce the SML against HVLS and City Core, and the Investors have suffered the loss of their capital and interest at the rate of 8% per year. BDMC is therefore liable to the Investors for the whole of their investment losses.

**c. The Sorrenti Defendants**

285. Madryga and the Class retained the Sorrenti Defendants to provide them with competent ILA, and to act on their behalf on the closing of their SML investment transactions. The Sorrenti Defendants breached their duty to act honestly and in good faith with respect to their contractual obligations to the Investors as particularized herein.

286. As set out above, the Sorrenti Defendants breached these retainers by failing to provide Madryga and the Class with genuine ILA, because they were acting in a position of conflict.

287. The Sorrenti Defendants also breached these retainers by providing negligent ILA to the Investors, as particularized above. The advice was prepackaged and was identical for all Investors.

288. The Sorrenti Defendants breached their retainers by registering the charge on title to the subject property evidencing the SML that deviated substantially from the terms of the SML Agreement, including the Priority, Standstill, Forbearance and Postponement terms.

289. Had the Sorrenti Defendants met their contractual obligations to the Investors, Madryga and the Class never would have invested in the SML, and would not have suffered any loss.

290. As a result of the Sorrenti Defendants' breach of their contractual obligations to the Investors, the Investors have suffered the loss of their capital and interest at the rate of 8% per year. The Sorrenti Defendants are therefore liable to the Investors for the whole of their investment losses.

291. Madryga and the Class also retained Sorrenti to act as trustee with respect to the SML and retained Sorrenti Law to act as their mortgage administrator.

292. Sorrenti, as trustee, breached his contracts with the Investors.

293. Pursuant to s. 12 of the SML Agreement, Sorrenti was required to satisfy himself with respect to certain conditions precedent before making advances to HVLS, which he failed to do. The conditions were not met, and the funds ought never to have been advances to HVLS.

294. Additionally, under the terms of the Acknowledgement, Sorrenti, as trustee, was obligated to obtain up-to-date valuations prior to making advances to HVLS. Sorrenti knew that the Appraisal and the Opinion were not current value valuations, and that no true current value opinion was ever received. Since the conditions for advancing funds to HVLS were never met, the funds ought never to have been advanced to HVLS and were advanced in breach of Sorrenti's contract with the Investors.

295. Sorrenti failed to fulfill his duties as trustee honestly and in good faith.

296. But for Sorrenti's breaches of contract in performing his role as trustee, none of the Investors' investment funds would have been advanced to HVLS, and they would have suffered no loss. Because of Sorrenti's breaches of contract in performing his role as trustee, the Investors lost their capital and interest at the rate of 8% per year.

297. Sorrenti Law also breached its contracts with the Investors by performing its duties as mortgage administrator negligently, including by failing to properly advise the Investors when HVLS failed to meet its contractual obligations and went into default under the terms of the SML Agreement, and by failing to take any steps to enforce the SML and the guarantee from City Core once the SML was in default.

298. Sorrenti Law failed to fulfill its duties as mortgage administrator honestly and in good faith.

299. Had Sorrenti Law fulfilled its duties honestly and in good faith, and properly advised the Investors about their rights when the SML went into default, or taken action on behalf of the Investors to enforce the SML when it went into default, then the Investors would have recovered the full amount of their capital investment and all accrued interest from HVLS and City Core, and would have suffered no loss. Sorrenti Law is therefore liable to the Investors for the whole of their investment losses arising from this breach of contract.

300. As a result of Sorrenti Law's failure to act and failure to advise the Investors of their rights when the SML went into default, the Investors lost the opportunity to bring enforcement proceedings against HVLS and City Core. If the Investors had been able to enforce the guarantee, they would have suffered no loss. Sorrenti Law is therefore liable for all damages arising from this lost opportunity.

**RELEVANT LEGISLATION**

301. The Plaintiff pleads and relies upon the provisions of the following acts and the regulations passed thereunder:

(a) *Mortgage Brokerages, Lenders and Administrators Act*, 2006, S.O. 2006, c. 29;

(b) *Financial Services Commission of Ontario Act, 1997*, S.O. 1997, c. 28;

(c) *Loan and Trust Corporations Act*, R.S.O. 1990, c. L-25;

(d) *Business Corporations Act*, R.S.O. 1990, c. B-16;

(e) *Trustee Act*, R.S.O. 1990, c. T-23; and

(f) *Negligence Act*, R.S.O. 1990, c. N-1.

**PLACE OF TRIAL**

302. The Plaintiff proposes that this action be tried at Toronto, Ontario.

DATE: December 2, 2016

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|---|---|---|---|
| REBECCA SHAW, LITIGATION ADMINISTRATOR of the ESTATE of BRYAN MADRYGA<br>Plaintiff | -and- | FORTRESS REAL CAPITAL INC. et al.<br><br>Defendants | Court File No.: CV-16-565287-00CP |

***ONTARIO***
**SUPERIOR COURT OF JUSTICE**
PROCEEDING COMMENCED AT TORONTO

# SECOND FRESH AMENDED STATEMENT OF CLAIM


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