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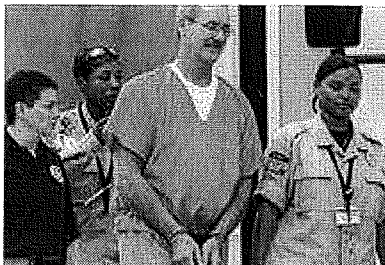
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The trouble with Ponzi class actions

Tricky to execute

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Presented by



Steve Campbell, Reuters Files

As Ponzi schemes in Canada tumble out of the sky, aided by the turbulent winds of economic collapse, investors are turning to class actions as a means to recover their lost money, suing everyone from the perpetrators to the financial institutions that handled the funds.

Unfortunately for investors, the orchestrators of Ponzi scams often ensure they either spend the bilked funds or move the money to places where it's difficult trace.

It's an expensive and lengthy endeavor to launch a class action, although some lawyers are infusing creativity in efforts to recoup losses for groups of investors.

Michael Mysak, a partner in the litigation group at Bennett Jones in Calgary, says sometimes his firm encourages investors to narrow the class down and identify a specific representative group who wants to pursue the action together, rather than simply having one person take on the case on behalf of all investors.

"When you're looking at a Ponzi scheme and you realize there may not be a lot of money there, the plaintiff who comes in has to make the decision as to whether they want to do it on behalf of everybody out there, or just band together with one group," says Mr. Mysak.

"Whether it's five or 150 plaintiffs, it's a defined group, and the idea is that if we recover something, it's going to go to the people who have signed up as plaintiffs," he says.

"When you're suing on behalf of everyone, when there's very little left at the end of the day and have to split it among 1,000 people instead of 100, it dilutes the effort."

He represented a group of 200 investors who had lost investments in an alleged Ponzi scheme that was set up as a ticket-scalping operation for concerts and sporting events in southern Alberta and northern United States.

While the group reached a confidential settlement, in similar cases, he has seen recovery of upwards of 20%, "which frankly for a Ponzi scheme, is a pretty good recovery," he says.

His firm is preparing a class action against Gary Sorenson and Milowe Brost, who through a series of businesses, including Merendon Mining, the Institute for Financial Learning and Syndicated Gold Depository S.A., were charged criminally this past fall for what RCMP allege is the largest Ponzi fraud scheme in Canadian history worth \$100-million.

Criminal proceedings are just getting underway and a trial date hasn't been set yet. The class action has not yet been certified. However, it's expected there could be as many as 3,000 potential members of the class.

Mr. Mysak says on behalf of the class, lawyers at Bennett Jones are identifying assets and requesting they be frozen to increase the chance there will be something to recover for the plaintiff group.

The process of identifying and freezing assets can be both protracted and expensive, says Toronto lawyer Kelley McKinnon, a partner in the securities litigation group at Gowling Lafleur Henderson. "The problem is in many, if not most, cases of fraud, the money is long spent and gone or if there are assets to be recovered, there may be some challenges," she says.

"With Ponzi schemes in particular, you've got somebody holding themselves out as investing your money, but what they're doing is taking investors' money and using the new money coming in to pay out earlier investors," she explains.

"Early investors do get some money back and that's why these Ponzi schemes can get so big, because early investors who do get money tell two friends who tell two friends and other people are encouraged to invest and buy in."

Ms. McKinnon says in some cases, it's possible to retain a receiver as well as a private investigator to facilitate the process of locating and freezing any assets.

But she also points out that the receiver gets paid out of the money recovered, diminishing the pot available for investors.

"It is an expensive process, but it's got to be done by someone to see if there's anything left for investors," she says.

So far, few class suits in Canada involving Ponzi schemes have gone to trial, so there's not an abundance of experience for investors to draw on quite yet, says Glenn Smith, a senior partner and commercial litigator at Lenczner Slaght in Toronto.

In the case of *Mondor v. Fisherman*, investors settled for \$85-million before going to trial, while another matter, *Carom v. Bre-X Minerals Ltd.*, a gold-salting scam, ended when the matter was settled.

American Allen Stanford, accused of running a US\$8-billion Ponzi scheme, was sued in August in a class action in Alberta, after the U.S. Securities and Exchange Commission and Antiguan regulators shut down Mr. Stanford's operations, alleging he and his associates were part of a giant US\$8-billion Ponzi that affected 27,000 investors in 113 countries.

He denies the charges. That case spurred a \$17-million negligence lawsuit by a group of investors against Toronto-Dominion Bank over its role as correspondent bank to some of the parties involved. The bank denies it's at fault for the losses.

"We haven't had a lot of Ponzi schemes that have gone the class-action route and that's probably not unusual because in Canada, we're not as aggressive with respect to prosecuting class actions as they are in the United States," says Mr. Smith.

There was also a settlement reached in the matter of Manulife Securities Investment Services Inc. v. Societe Generale (Canada) on behalf of all purchasers of investment products of Portus Alternative Asset Management Inc.

The settlement reached in 2008 enabled Manulife to recover upwards of \$600-million for its investors, a significant recovery, after the Portus founders were charged with fraud. The settlement process was recently wrapped up with investors recovering 95¢ on the dollar.

"I think there is the potential for plaintiff class-action lawyers to gain recovery in situations where there are significant investors with reputations and assets, and financial institutions are involved in a deal that goes south," says Mr. Smith.

He adds, however, that it's no easy feat initiating a class action against a financial institution that may have been caught in the Ponzi scheme cross fire.

"The structure of the lawsuit has to be very well thought out and you have to choose the right plaintiff," he says.

"And when you go after an innocent financial company, you had better make sure you know that when you're playing with fire, you might get burned."

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