

**SECURITIES CLASS ACTIONS IN CANADA:
HAVEN OR HINTERLAND?**

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I. INTRODUCTION

Class actions provide a powerful tool to Plaintiffs and their counsel. Actions that would previously not have been brought suddenly make sense when many small claims can be efficiently aggregated. With the passage of class action legislation, anyone with responsibilities to a diffuse group is now at greater risk. Issuers, directors, officers and brokers are no exception.

II. THE U.S. EXPERIENCE

Actions against issuers, their officers and directors are among the most popular areas for class actions in the United States. Most common are claims of fraud under section 10(b) of the *Securities Exchange Act of 1934*.¹

If a director or officer fails to ensure that the company discloses adverse material information, they are likely to find themselves part of a class action lawsuit by shareholders who purchased in the secondary market during the period of the material non-disclosure. The action will claim the difference between the price at which the shares were purchased, and what the shares were actually worth.

These class actions are assisted by the “fraud on the market” theory, which essentially removes the necessity to establish reliance on any particular misrepresentation by the company, so long as the Plaintiff can establish that the failure to disclose had an impact on the market price.² Further, courts may be willing to certify the class action even if the claim requires an assessment of documents produced over an extended period of time, so long as the documents were part of a

¹ 15 U.S.C. 78j(b)

² *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975)

common scheme to defraud shareholders.³ Both these principles reduce the individuality associated with the claims, and keep the focus on the issuer's conduct. Certification is essentially automatic in such class actions.⁴

Defendants whose share price takes an unexpected dip will usually face a spate of actions by many different law firms. For example, Cendant Corp. alone was hit with 70 different lawsuits in 1998.

The resources required to defend the lawsuit and the negative impact on the company's ability to raise capital, coupled with certain class counsel's willingness to resolve claims for cents on the dollar, create an environment that is very conducive to settlement. Class settlements' percentage of the potential investor losses was found to range from 2-21% in one study.⁵

So many class actions were filed in the early 1990s that (Republican) legislators came to believe that remedial legislation was required. Congress passed the *Private Securities Litigation Reform Act* in 1995. This legislation:

³ *Newberg on Class Actions*, (West Publishing, 1992), para.22.19.

⁴ *Newberg on Class Actions*, *supra*, para.22.01

⁵ See Bajaj, Mazumdar, and Sarin, "Securities Class Action Settlement: An Empirical Analysis" (Nov. 16, 2000) at <http://secuties.standord.edu/report>

- a. heightened the pleading requirement - more specificity was required in relation to the fraud allegation;
- b. created a presumption that the best representative Plaintiff is the person with the largest financial interest in the case;
- c. required that each Plaintiff seeking to serve as a representative party file a sworn certification that:
 - (i) the Plaintiff did not purchase the shares at the direction of counsel or in order to participate in a lawsuit;
 - (ii) identifies any other action filed during the preceding three-year period in which the Plaintiff sought to serve as a representative Plaintiff; and
 - (iii) the Plaintiff will not accept payment for serving as a representative party on behalf of a class beyond the Plaintiff's pro rata share of any recovery, except as approved by the court;
- d. assigned joint and several liability for damages only if the trier of fact specifically determines that the Defendant knowingly violated securities laws; otherwise, damages were restricted to that portion of the judgment that corresponds to the percentage of each individual Defendant's responsibility for the Plaintiffs' losses;
- e. provided certain issuers a safe harbor from liability for forward-looking statements regarding a security's projected performance or operations, if: (1) the statement is immaterial or is identified as a forward-looking statement and accompanied by certain cautionary statements; or (2) the Plaintiff fails to prove that the statement was made with either actual knowledge of its false or misleading nature by a natural person, or actual approval by an executive officer.

The desire to shift control of securities class action litigation from alleged “straw men” to institutional investors was a driving force behind the enactment of the legislation.⁶

Did the legislation succeed in deterring securities class actions? The answer is clear from the following headline at Stanford’s *Securities Class Action Clearinghouse* website⁷:

**SECURITIES FRAUD LITIGATION SETS RECORD IN 1998 ---
Companies Sued at a Rate Close to One-A-Day**

It is generally accepted that the legislation failed to achieve the purpose of reducing the number of cases.⁸ Class actions continued unabated. While settlements slowed following the reforms, the absolute value has been larger. The settlements’ percentage of the potential loss did not change significantly.⁹

Congress responded to this failure by passing the *Securities Litigation Uniform Act of 1998*. This legislation creates further restrictions by attempting to ensure that the U.S. Federal Court is the exclusive jurisdiction for these types of actions. Evidence suggested that class counsel were seeking to circumvent the 1995 federal requirements by filing securities actions in state courts rather than federal court.

However, these changes still did not materially change the number of filings. The “Filings per Issuer Index” was 2.3 in 1998 and 2.8 in 2004.¹⁰

⁶ *Lirette v. Shiva Corp.*, 1998 U.S. Dist. LEXIS 18525 (Mass.D.C.)

⁷ <http://securities.stanford.edu>. This website is an amazingly comprehensive site of cases, statutes, and academic material.

⁸ Tamara Loomis, “Securities Reform: What Went Wrong” (October 27, 2000), found at <http://securities.stanford.edu/report>

⁹ Bajaj, *supra*

¹⁰ Indices of Securities Class Action Filings, Stanford Securities Class Action Clearinghouse, found at http://securities.stanford.edu/litigation_activity.html

III. THE CANADIAN EXPERIENCE

Has the U.S. experience been imported into Canada? Canada has seen some securities class action activity, but there are presently limitations on how far the area can expand. A review of the case law to date will show the opportunities and pitfalls associated with such litigation.

1. The Prototypes - Maxwell v. MLG Ventures and Kerr v. Danier Leather Inc.

In *Maxwell v. MLG Ventures Ltd.*, an action based on alleged misrepresentations in an offering circular was certified, and a settlement subsequently achieved on behalf of investors.¹¹ The class included all former shareholders of Maple Leaf Gardens Ltd. who had tendered their shares pursuant to the Defendant's offer. The settlement required the offeror to substantially increase its initial offer. Class certification was assisted by the fact that the Ontario *Securities Act* provides for deemed reliance on the contents of the offering circular¹². This provision removes one

¹¹[1995] O.J. No. 2698 (Gen.Div.)

¹²*Securities Act*, R.S.O. 1990, c.S.5, s.131. The same rule applies to misrepresentations in a prospectus. S.130 reads:

130 (1) Liability for misrepresentation in prospectus - Where a prospectus together with any amendment to the prospectus contains a misrepresentation, a purchaser who purchases a security offered thereby during the period of distribution or distribution to the public shall be deemed to have relied on such misrepresentation if it was a misrepresentation at the time of purchase and has a right of action for damages against,

- (a) the issuer or a selling security holder on whose behalf the distribution is made;
- (b) each underwriter of the securities who is required to sign the certificate required by section 59;
- (c) every director of the issuer at the time the prospectus or the amendment to the prospectus was filed;
- (d) every person or company whose consent has been filed pursuant to a requirement of the regulations but only with respect to reports, opinions or statements that have been made by them; and
- (e) every person or company who signed the prospectus or the amendment to the prospectus other than the persons or companies included in clauses (a) to (d)

or, where the purchaser purchased the security from a person or company referred to in clause (a) or (b) or from another underwriter of the securities, the purchaser may elect to exercise a right of rescission against such person, company or underwriter, in which case the purchaser shall have no right of action for damages against such person, company or underwriter.

otherwise difficult individual issue, and will often tip the balance in favour of certification in cases involving primary market distributions (i.e. distributions direct from the issuer or purchases pursuant to a take-over bid circular).

In *Kerr v. Danier Leather Inc*¹³ the court certified a class action alleging misrepresentation in a prospectus. Danier issued a prospectus May 6, 1998 in connection with the IPO of its shares. The public offering closed May 20, 1998. The price was \$11.25 per share.

Notably, the allegation of misrepresentation was in relation to a forecast. In the prospectus, an increase in revenue of \$5,000,000 was projected for the 1998 fourth quarter over that of the 1997 fourth quarter. Unfortunately, the actual sales in May and early June 1998 did not meet the expectations in the Forecast. This was attributed to a prolonged period of unseasonably warm weather. On June 4, 1998 Danier's Board of Directors issued a press release containing a "Revised Forecast" which anticipated that the warm weather trend would continue in June. Fourth quarter revenue projections were reduced from \$17,410,000 to approximately \$12,600,000, a decline of about 27.5%. A net loss of \$1.15 million was now projected for the fourth quarter, an increase of about 196% over the projected loss of \$384,000. The total projected net earnings of fiscal 1998 were restated and reduced from \$4,500,000 to \$3,700,000.

However, the unseasonably warm weather did not continue after the June 4, 1998 Revised Forecast. There was cooler weather for the balance of June 1998. Also, Danier made use of certain "reserves" in its manner of financial reporting. Hence, the actual results for the fourth quarter and overall fiscal 1998 were only marginally less than the projections in the Forecast. However, the share price remained depressed for some time.

The subsequent results for fiscal 1999 and 2000 for Danier demonstrated significant additional growth in sales, gross profits and net earnings, all of which were reflected favourably in the

Similar provisions are found in B.C.'s *Securities Act*.

¹³ (2001), 13 B.L.R. (3d) 248 (Ont.S.C.J.)

market price for the shares.

The case is one of the few class actions to have proceeded through a full trial.¹⁴ The class claim was successful. The court concluded that a forecast could be subject to consideration under the *Securities Act* provisions:

A forecast is not a fact in the sense that actual results are facts. Issuers cannot be liable under s. 130 for every variation from forecast results. A forecast can be a fact in that every promise includes implied assertions of fact. The factual assertions that may be derived from a forecast have been described as:

- i. the forecast represents the forecaster's best judgment of the most probable set of economic conditions and the company's planned course of action (Summary Judgment Motion, *supra*);
- ii. the forecast is sound and reliable in the sense that the forecaster made it with reasonable care and skill (Esso, *supra*); and
- iii. the forecaster generally believes the forecast, the forecaster's belief is reasonable and the forecaster is not aware of any undisclosed facts tending to seriously undermine the accuracy of the forecast (NationsMart, *supra*).

These descriptions are merely variations on a theme. Description (i) is consistent with the definition of "Forecast" in NP 48. Description (iii) provides further clarification of what is meant by "best judgment." Similarly, it would be difficult for the forecaster to maintain that his or her belief in the forecast is reasonable or that the forecast represents his or her best judgment without having used reasonable care and skill...

A forecast can be a "fact," and can also be "material." The term "material fact" is defined in s. 1(1) of the OSA as follows:

[W]here used in relation to securities issued or proposed to be issued, means a fact that significantly affects, or would reasonably be expected to have a significant effect on, the market price or value of such securities.

If a forecast has or would reasonably be expected to have such an effect, then it is material. (at paras. 64-67)

The court concluded that the forecast was not untrue as of May 6, but became untrue by the time the distribution period closed on May 20, particularly in light of poor Victoria Day sales.

¹⁴

[2004] O.J. No. 1916 (S.C.)

The court also found that the subsequent rebound did not negate liability stating:

[The] key date for the determination of liability under s. 130(1) of the OSA is the time of purchase. As such, the focus is on whether the factual assertions implied from the Forecast were true or untrue, or whether there was an omission of material facts which were necessary to make the Forecast not misleading, as of that date. Thus, it is information available as of May 20, 1998, that is critical to this analysis. It is the public information available as of that date upon which the purchasers of securities base their investment decision. It is the public and non-public information available as of that date that management must consider in determining whether or not it needs to take action to avoid breaching its obligations under s. 130(1) of the OSA. In this case, hindsight obtained from the fact that a misrepresentation at the time of purchase later becomes true because the Forecast is substantially achieved, does not make it any the less a misrepresentation at the operative date, the time of purchase.

Despite Danier's favourable year-end results, its share price did not recover. Danier's share price did not reach the IPO price of \$11.25 until August 2000, at which time the company had grown substantially. (at paras. 278-279)

One of the interesting elements of this case was the consideration of damages. The court held that the prima facie measure of damages is the depreciation in the price of the security: offering price less post-misrepresentation price. In terms of the relevant date for this calculation, the court concluded:

The defendants' argument that the only evidence of the value of the shares at the time of purchase is the trading price and the evidence of their expert indicating that the intrinsic value of the shares was at least the trading price must be rejected. In this case, the misrepresentation was made to all purchasers of the shares. The trading price was not free of the misrepresentation before June 4, 1998, the date of the disclosure. The market reaction as of this date and following is the best evidence of the consensus of buying and selling opinion as to the real value of the shares absent the misrepresentation. With respect to the defendants' expert, it would be illogical to prefer the opinion of one expert to the consensus of the market, particularly when the market consensus was that the real value of the shares was below \$11.25.

Under s. 130(7), it is open to the defendants to rebut the depreciation in value evidenced by the market reaction to the disclosure, by proving that other factors caused the depreciation in price or that the market prices on June 4, 1998, and following did not represent value because they were affected by factors unrelated to value. (at paras. 338-339)

Given the eventual rebound of the shares, the court also considered whether class members must

have sustained an actual loss; that is, must they must have sold after the misrepresentation was disclosed, and are they only entitled to recover any actual loss flowing from such sale? The court rejected this stating:

Neither s. 130 nor any of the authorities referred to suggest that the plaintiffs can recover only if they have sold and crystallized their loss. This follows from the premise that the appropriate measure of damages is the difference between the price paid and the then value of the securities. As indicated in *Pearson, supra*, if the plaintiff both buys and sells the securities when they are affected by the misrepresentation - i.e. sells before the disclosure of the misrepresentation - then he or she has not suffered any depreciation in value and cannot recover damages. Accordingly, purchasers who sold before June 4, 1998, may not recover, and, in fact, are not included in the class in this case. If a plaintiff makes a second investment decision and continues to hold the securities after the disclosure of the misrepresentation, then subsequent movements in the market price of the securities will not inure to the benefit of either the plaintiff or the defendant. This method of measuring damages does not risk awarding a windfall to the plaintiff. For example, assume Ms. X purchased shares at \$30 per share on the understanding that the company had drilled for oil and had discovered a significant oil field and expected significant increases in production and cash flow. Thirty days after this purchase, the company discloses that its claim to have discovered a significant oil field was a misrepresentation. The market reacts to this disclosure and the price of the shares declines to \$10 per share. Ms. X sues for damages, but continues to hold her shares because in her view, at \$10 per share, the company is a good investment in light of the corrected information regarding its current prospects. Subsequently, the company's shares stagnate for two years and then appreciate to \$50 per share on the basis of an even larger discovery. Ms. X sells her shares at \$50 per share. Would awarding Ms. X damages at trial represent a windfall? In my view, absolutely not. Ms. X should have realized \$40 per share based on the then value of the shares she purchased. Instead she only realized \$20 per share. Awarding Ms. X damages of \$20 per share, representing the difference between the price she paid and the then value of the shares, would only compensate Ms. X for the harm caused by the misrepresentation. (at para.345)

Finally, the court considered the precise calculation of damages:

The closing price of Danier shares on June 4, 1998, was \$10.25, which suggests damages of \$1.00 per share.

The plaintiffs do not use this price to calculate damages. Instead the plaintiffs base their measurement of \$2.40 per share on calculations performed by their expert, Professor Giammarino. Using a statistical model that he constructed, Professor Giammarino estimated the statistical relationship between the change in Danier's share price, the proportional change in the TSE 300 index, the proportional change in the TSE Consumer Discretionary Spending sub-index and the changes in the share prices of comparable companies. The plaintiffs also note that their expert, Alan Stewart, calculated damages using the ten and twenty-day average of the closing prices of Danier

shares, of \$2.28 and \$2.21 respectively, or \$2.52 and \$2.24 when the ten and twenty-day averages are calculated excluding the closing prices on June 4 and 5. Alan Stewart's approach essentially mirrors the calculation of damages under s. 134(6). As discussed above, the measure of damages under s. 134(6) may inform measurement of damages under s. 130.

There is no reason to depart from the prima facie measure and adopt either the measure of damages under s. 134(6) or Professor Giammarino's statistical model.

Professor Giammarino's evidence, however, is helpful in determining whether the market price on June 4, 1998, is the appropriate post-misrepresentation price. It is Professor Giammarino's opinion that the implications of the forecast revision were not fully absorbed by the market until June 10, 1998. Professor Giammarino supports his opinion with statistical analysis indicating that the price swings for the trading days June 4, 5, 8, and 9 were abnormal price movements and reflect a continued response to the June 4, 1998, announcement. Further, that price stabilization activities such as those undertaken by the lead underwriter, CIBC, have the effect of mitigating price movements, which means that the market price may not reflect the consensus of buying and selling opinion. Professor Giammarino indicates that CIBC was on the buying side of 60%, 97% and 39% of the total volume of shares traded on June 4, 5, and 8 respectively. It is the evidence of Earl Rotman of CIBC that they purchased, at market, \$10 million of Danier shares on June 4th and June 5th for the purposes of price stabilization.

The plaintiffs' argument on this point is persuasive. The post-misrepresentation price should be adjusted to eliminate the effects of the price stabilization and any abnormal price movements, similar to the adjustment made in *Beecher v. Able*, supra, to eliminate the effects of panic selling. In the circumstances of this case, the appropriate post-misrepresentation price is the closing price of \$8.90 on June 10, 1998, the date that the forecast revision had been fully absorbed by the market and the market price was no longer affected by price stabilization activities.

Thus, the plaintiffs are entitled to damages of \$2.35 per share (\$11.25-\$8.90) subject to any negative causation defence proven by the defendants under s. 130(7) of the Act. (at paras. 356-361)

2. The Glass is Half-Full (or All Empty) - *Carom v. Bre-X Minerals Ltd.*

This action included pleas of misrepresentation and conspiracy against Bre-X, a sister company, its insiders and engineer, and several brokers who recommended Bre-X stock. These were "secondary market" allegations, not based on a particular prospectus or circular. All Canadian

shareholders who purchased shares of Bre-X on various stock exchanges over the course of the alleged fraud were included within the proposed class.

In an earlier pleadings motion, the court specifically declined to import the U.S. “fraud on the market” concept into such secondary market claims.¹⁵ The court held that the Supreme Court of Canada’s judgment in *Hercules Management* means that reliance must be established in every case alleging negligent misrepresentation.

Without the benefit of the “fraud on the market” concept, the negligent misrepresentation tort is usually quite personal - it begins with an analysis of exactly what was said to each individual, and it ends by requiring confirmation that each person relied on the particular statement challenged.

At the certification stage, the trial court in *Carom* refused to certify the negligent misrepresentation claims, based in large measure on the complexity created by the need to establish reliance in each case.¹⁶ However, the court did certify the fraudulent misrepresentation claim against the company and its insiders given that the focus of this claim was an overarching fraud permeating every statement rather than a series of individual representations. The court also certified the conspiracy and *Competition Act* claims against the same parties. The Ontario Court of Appeal subsequently found that the negligent misrepresentation claims could proceed against the insiders and Bre-X, given that the fraudulent misrepresentation claim had already been certified against these parties, and there was insufficient legal distinction between the nature of the two claims to justify different treatment.

Therefore, in relation to secondary market claims, unless you have a strong case of fraud against the issuer itself, it will be difficult to achieve certification. The problem facing the Plaintiff in *Carom*, which will not be infrequent, is that the issuer is left with little in the way of exigible

¹⁵ (November 4, 1999) 97-GD-39574 (Ont. Ct. Gen. Div.)

¹⁶ 44 O.R. (3d) 173 (Gen. Div.), aff’d (1999), 46 O.R. (3d) 315 (Div. Ct), appeal allowed (October 31, 2000) C33905 (C.A.)

assets once a fraud is uncovered.

It may be possible to justify certification of secondary market claims if there is one press release or statement that will obviously have been heard or relied upon by all shareholders, but such situations will be rare.

3. Misrepresentation Difficulties, What Misrepresentation Difficulties? -
Menegon v. Philip Services Corp.

A settlement class was certified against the issuer in *Menegon v. Philip Services Corp.*¹⁷, in which secondary market misrepresentation claims were advanced by the shareholder class. However, there was little analysis of the concerns raised in *Carom*. The certification seemed to be driven by the particular circumstances of that case. The issuer required settlement approval in order to achieve a restructuring under the *Companies' Creditors Arrangement Act*. The court specifically held that certification against the issuer was without prejudice to any arguments the remaining Defendants might wish to make in opposition to certification at some later date.

4. Oppression Class Actions: The Form is Fine, but what about the Content? -
Stern v. Imasco Ltd. and *Joncas v. Spruce Falls Power and Paper Co.*

There is a variety of corporate activity that takes place outside the framework of prospectuses or takeover bids. The oppression remedy is meant to provide a remedy for all situations in which shareholders have been unduly prejudiced. Can the class action vehicle be used effectively to advance such claims?

In *Joncas v. Spruce Falls Power and Paper Co.*¹⁸, the court approved an oppression claim relating to a share issuance by the company to employees. Certification was not actively

¹⁷[1999] O.J. No. 4080 (S.C.)

¹⁸(April 13, 1999) No.97-CV138924 (Ont.Ct.Gen.Div.)

contested by the Defendant however, only the existence of a cause of action.

In *Stern v. Imasco Ltd.*¹⁹, the Plaintiff sought to bring an oppression-based class action alleging that the issuer, its directors, and de facto controlling shareholder were entering into an improvident transaction which had the effect of “freezing out” minority shareholders at a price that did not properly reflect the value of the shares. All shares were to be transferred to the de facto controlling shareholder, BAT plc.

The Defendants argued that an oppression-based class actions are barred through the operation of section 37(a) of the Ontario *Class Proceedings Act*.

Section 37(a) provides that the Act does not apply to a proceeding that may be brought in a representative capacity under another act. The Defendants argued that an oppression action could be brought in a representative capacity under the applicable corporate statute, and therefore certification under the Ontario Act was not appropriate. The court rejected this argument stating that although an oppression proceeding can sometimes have the characteristics of a representative action in its effect, it is not “brought in a representative capacity”. The court found that use of the class proceedings legislation can be complementary to the objectives of the oppression remedy.

When it came to assessing the merits, however²⁰, the court adopted the traditional business judgment rule and held that: “The directors of Imasco have an arguable basis for facilitating a decision by Imasco's public shareholders on BAT's proposal.”. The business judgment rule as interpreted to date by Ontario and B.C. court's have provided officers and directors with a great deal of latitude in terms of structuring transactions²¹. As a general matter, it would appear that

¹⁹(1999), 38 C.P.C. 4th 347 (Ont.S.C.J.)

²⁰The Plaintiff had asked for interim disclosure orders, which required the court to consider the merits of the Plaintiff's position generally.

²¹*Brant Investments Ltd. v. KeepRite Inc. et al.* (1991), 3 O.R.(3d) 289 (C.A.) at 320; *Brio v. Clearly Canadian Beverage Corp* (1995), 8 C.C.L.S. 1 (B.C.S.C.) at para. 17t; *CW Shareholdings Inc. v. WIC*

U.S. courts are more inclined to adopt a degree of healthy scepticism when considering the motives of a corporation's principals.

The Court in *Stern* also struck the personal claims against the directors, and those against the de facto controlling shareholders. This left only the issuer as subject to the oppression action. These findings illustrate two points: (1) the broad scope of the business judgment rule in Canada, and (2) the need to carefully assess the scope of any securities claim to ensure that only the bare minimum of parties necessary to assure full recovery at the end of the day are joined. This is particularly true in Ontario, where costs can be awarded against representative Plaintiffs within the class proceeding.

5. Undermined by an Apparent Alternative - *Millgate v. National Trust Company*

This claim concerned debentures that were issued by National Trust as corporate trustee. Other Defendants named in the action include corporations and senior executives who were alleged to have stripped a company of assets after it sold the debentures.

Class certification was refused, based on the Defendants' agreement to be bound by a resolution of certain legal issues determined in one action²². The court did allow that certification could be revisited after a resolution of these legal issues.

One may ask why, if there was a central legal issue, the case could not be certified immediately so that the class members would gain all of the associated procedural advantages under the Act.

6. Preventing Abuse - *Epstein v. First Marathon Inc.*

*Epstein v. First Marathon Inc.*²³ illustrates the care courts will take to ensure that securities class proceedings are not used improperly to prevent commercial transactions from proceeding smoothly.

In Ontario, any discontinuance of a class action must obtain court approval, whether or not the action has been certified.²⁴ In *Epstein*, the Plaintiff sought to discontinue a proposed securities class action. The action was sought in order to challenge the corporation's decision to enter into a statutory arrangement. Prior to any challenge being advanced however, the Plaintiff agreed to discontinue the action in return for a sum of money on account of fees. No funds were going to be paid to the class, and the agreement was not generally disclosed.

The court refused to approve the fee, concerned that the action had the characteristics of a "strike suit" advanced solely to obtain the payment of fees rather than in the best interest of shareholders. The court noted that the case on the merits was never advanced by the Plaintiff, and counsel was the only person benefiting from the settlement.

²²[1998] O.J. No. 4537 (Gen.Div.)

²³(2000), 41 C.P.C. (4th) 159 (Ont.S.C.)

²⁴Note: This is not the case in B.C. where approval is only required if the case reaches certification.

7. The Billing Cases – *Scott v. TD Waterhouse*

In *Scott v. TD Waterhouse*²⁵, a class action was brought against a broker challenging the means by which the broker calculated the exchange rate on trades of any foreign securities. The case was eventually settled.

IV. CROSS-BORDER ISSUES

In the case of Bre-X, class actions were brought in both the U.S. and Canada. The U.S. action purported to include Canadian shareholders. The Defendants in the U.S. action opposed the inclusion of Canadians.

The U.S. court agreed, and dismissed the Canadian claims.²⁶ The court concluded that there was no jurisdiction in the U.S. court to consider such claims. There was insufficient conduct in the United States relevant to the claims of the Canadians to allow them to rely on the provisions of the U.S. securities legislation.

Conversely, in *Paraschos v. YBM Magnex International Inc.*²⁷, a U.S. Court found that there was sufficient activity conducted by the issuer in the U.S. to allow the Canadians to pursue U.S. statutory remedies. The court did not preclude parallel litigation in Canada on any Canadian remedies might also be available.

Given the strength and advantages provided by the “fraud on the market” remedies in the U.S., it can be argued that, at the present time, it is generally be preferable to pursue claims in the U.S. whenever possible. Recently, the Ontario Court of Appeal has indicated that so long as U.S. class actions (1) properly assume jurisdiction over Canadian claims, (2) provide fair and

²⁵ (2001), 94 B.C.L.R. (3d) 320 (S.C.) (certification), (unreported April 25, 2003, Vancouver S002736, B.C.S.C.) (settlement approval)

²⁶ *McNamara v. Bre-X Minerals Ltd.* (Jan. 7, 1999. E.D. Tex., Texarcana Division)

²⁷ (May 29, 2000, E.D. Penn)

adequate notice to Canadians (including a right to opt out), they will enforce U.S. settlements or judgments against Canadians.²⁸

However, it is interesting to note that in the *YBM* case, there was also a Canadian class action commenced, and the Canadian case was eventually used to effect the settlement of the claim.²⁹

Nonetheless, in the absence of legislative reform, it is likely that most Canadian securities class actions will only involve Canadian issuers, and cases where little of the challenged conduct occurred within the U.S.

V. THE NEW WAVE OF LIABILITY ON THE HORIZON

The Canadian Securities Administrators published proposed legislative changes which would facilitate bringing class actions by adopted in a form of “fraud on the market” theory for secondary market claims. The proposed changes included the following elements:

- a. Secondary market investors will have a civil right to sue issuers, directors, responsible senior officers, auditors, “influential persons”, and other experts for withholding information or for releasing misleading information that causes losses which could have been prevented, had complete information been made available.
- b. Secondary investors would not have to prove that they had relied on any specific information. Reliance will be deemed.
- c. Defences: For some types of disclosure, defendants will have a due diligence defence. For other types, it will be necessary to show that the defendants were reckless.

²⁸ *Currie v. McDonalds*, [2005] O.J. 506 (C.A.)

- d. **Damage Limits:** Damages against an issuer are limited to 5% of market capitalization or \$1 million, whichever is greater.
- e. **Joint and Several Liability:** Liability will not be joint and several. Each person at fault will only be responsible to the extent that they were responsible for the misrepresentation, unless the misrepresentation is made knowingly.
- f. **Procedural Issues;** Leave of the court would be required to commence the action, and the court will have to approve any settlement. Given that these requirements exist in for class actions already, these requirements do not add any complexity to securities class cases.

Given the market capitalization limits, the incentive will be to pursue larger companies. It is difficult to rationalize why the issuer's exposure should be limited to 5% when the misrepresentation may have caused far greater losses. The explanation likely lies in the need for a political compromise to ensure that the legislation has a reasonable prospect of being passed.

The author has a real concern whether the limits are sufficiently high to motivate class counsel to bring such difficult and challenging secondary market claims. It may be necessary for class counsel to "double up": invoke the statutory remedies to ensure certification, while maintaining the common law claims to ensure that the company continues to face exposure for the entire loss suffered by shareholders.

Although promised for some time, none of the provinces have yet proclaimed these new measures. On November 22, 2004, the Ontario government announced its intention to implement

²⁹ *Mondor v. Fisherman*, [2002] O.J. No. 1855 (S.C.)

the new statutory regime for civil liability for secondary market disclosure. The proposed amendments were essentially identical to those introduced by the preceding government in May 2003 in Bill 41, which died on the Order Paper when the last Ontario provincial election was called.

This move forward by the Ontario government follows the announcement by the British Columbia government that it was delaying the proclamation date of similar comprehensive reform to B.C.'s *Securities Act* through its Bill 38.³⁰

VI. CONCLUSION

The *Class Proceedings Act* does partially even the playing field between issuers and wronged shareholders. Canadian class counsel are learning from their American counterparts. Canadian legislators are learning from their American counterparts.

30 Osler Hoskin Harcourt "Government Moves Towards Implementing Civil Liability for Continuous Disclosure in Ontario" (December 3, 2004) found at

<http://www.osler.com/index.asp?navid=1086&layid=1124&csid=3033&csid1=1719>

See also Osler Hoskin Harcourt "Proposed New Ontario Securities Laws to Provide Greater Investor Protection" (November 18, 2002) found at

<http://www.osler.com/index.asp?navid=1086&layid=1124&csid=3033&csid1=1252> and Blakes, "Civil Liability for Continuous Disclosure is pending" (February 5, 2005) found at

Launching a securities class action is not for the faint of heart however. Issuers will retain top-flight counsel, and will confront class counsel with a full array of procedural objections. The speed at which securities transactions and its associated litigation occur requires enormous resources and devotion. The issue of costs for cases brought in Ontario can be daunting. On the merits, the courts will generally grant the corporation a wide latitude in relation to its decision-making.

Nonetheless, at the end of the day, class actions have increased exposure for securities issuers. This should improve both the conduct of issuers, and the lot of shareholders wronged by improper activities. The level of improvement will depend on the courage (or foolhardiness) of class counsel, and the willingness of the legislature to further improve the balance between issuers and their shareholders with new legislation.