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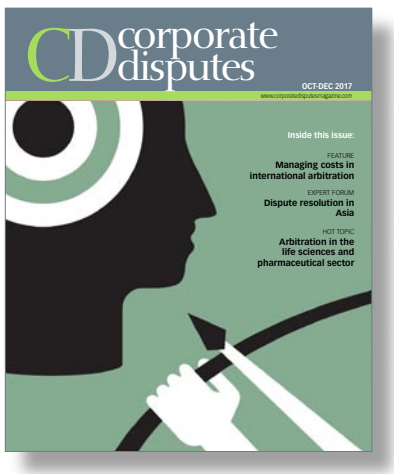
CD corporate disputes

CANADIAN SECURITIES CLASS ACTION LITIGATION

REPRINTED FROM:
CORPORATE DISPUTES MAGAZINE
OCT-DEC 2017 ISSUE



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Published by Financier Worldwide Ltd
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MINI-ROUNDTABLE

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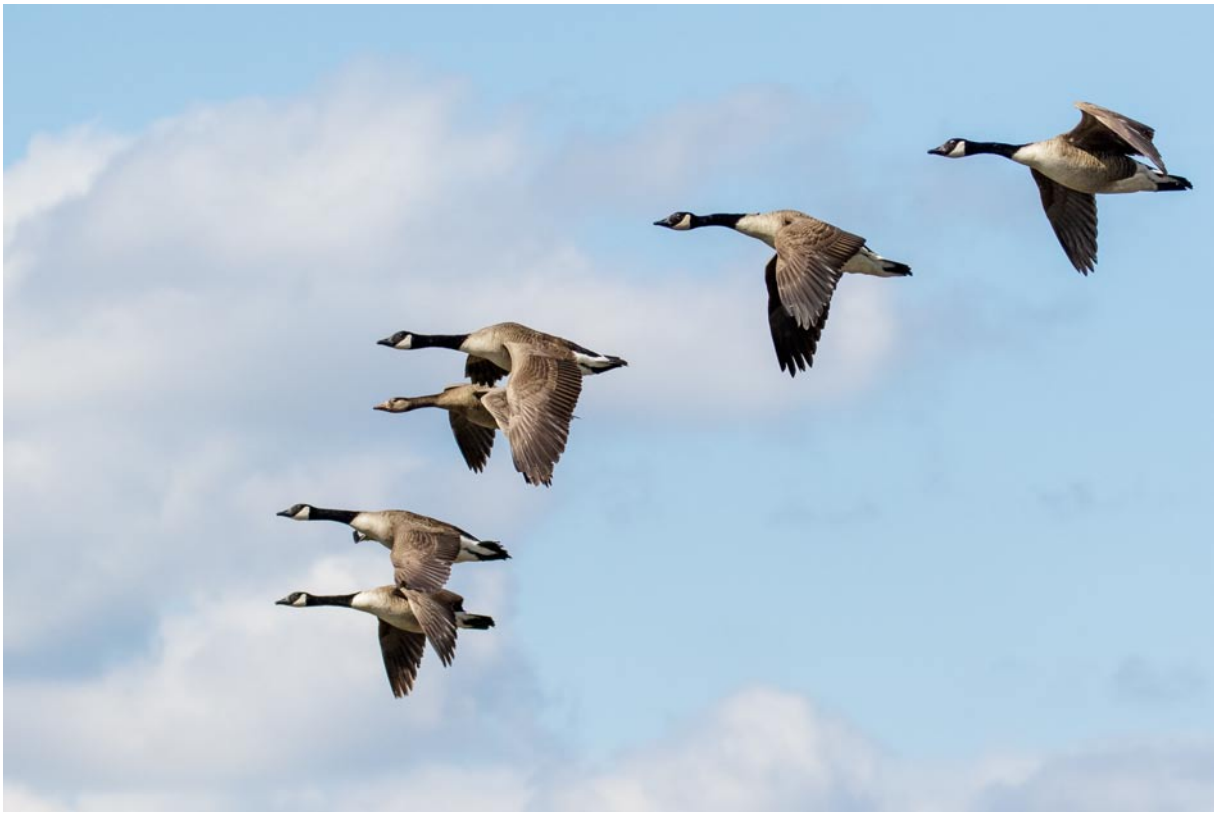

PANEL EXPERTS

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Jonathan Foreman is a partner at Harrison Pensa LLP and his practice focuses exclusively on plaintiffs' side class action work. Repeatedly recognised as a leading plaintiff-side class action litigator in Canada by Lexpert and Best Lawyers in Canada, Mr Foreman leads the plaintiff's class actions group at Harrison Pensa LLP. The class actions group overall has also been ranked as a leading plaintiff-side practice in Canada by Chambers Global.

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Michael Statham is the managing partner of WeirFoulds LLP in Toronto. His commercial litigation practice involves complex and high-profile business disputes, with a particular emphasis on class actions. Recent examples include acting for the representative plaintiff in the lengthy trial and subsequent appeal in *Trillium Motor World Ltd. v. General Motors of Canada Ltd*., and acting for a NASDAQ-listed issuer and two of the issuer's senior officers in defending an ongoing securities class action advanced on behalf of a global shareholder class.

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Dana M. Peebles is a partner in the Toronto Litigation Group at McCarthy Tétrault LLP and a past chair of the national class actions team. He is widely recognised as one of Canada's leading class action lawyers. Mr Peebles has acted for leading Canadian and international companies in complex matters in trial and appellate courts across Canada, including a number of class actions paired with ongoing US litigation.

CD: How would you describe the level of securities class action filings in Canada over the past 12 to 18 months? Are any specific Canadian provinces witnessing greater numbers of these cases?

Foreman: Filings in Canada have certainly slowed down over the past one to two years. Our provincial governments introduced new legislation in 2006 that was designed to enable securities law class actions for secondary market misrepresentations. Activity started slowly thereafter and then grew considerably. Two cases made their way to our Supreme Court of Canada for an interpretation of some of the fundamental elements of that new regime. The result was a careful and quite conservative interpretation of the statutory requirements for secondary market misrepresentation class actions. Those cases have since driven a more cautious approach to these matters on the plaintiff's side – something which has been reflected in the lower rate of new filings. That is a double edged sword – nobody wants meritless cases in the system, but it is my hope as a front line operator in this space that our system will do more than simply service the largest and most obvious securities law failures. There is a pendulum swing here and circumstances are ripe for recalibration in my view. Across Canada, Ontario is overwhelmingly the main jurisdiction in which claims are brought, although we have seen a number of cases in Quebec and in other provinces from time to time.

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> *Michael Statham, WeirFoulds LLP*

Statham: According to NERA Economic Consulting's annual update, the number of new shareholder class actions asserting the statutory cause of action under provincial securities legislation for alleged misstatements in secondary market disclosure increased in 2016 to seven as compared to four in 2015. However, the 2016 figure remains at or slightly below the levels witnessed over the period 2010 to 2014. The filing volumes have not borne out the prediction, articulated by some observers in earlier years, that Canadian courts' relatively permissive approach to global shareholder classes,

subject to *forum non conveniens* arguments, and the corresponding rejection of the exchange-based 'bright line' test set out by the US Supreme Court in *Morrison*, would prompt a surge in Canadian filings. With respect to geographical distribution, the majority of case filings are made in Ontario, home to the TSX, either exclusively or in combination with claims asserted in other provinces.

Peebles: This is a narrow field and so any small movement in the number of commenced actions can seem significant. Looking only at statutory secondary market cases, there have been only 76 commenced in Canada since 2006. Over the last five years, there have been nine in 2011, eight in 2012, 10 in 2013, 11 in 2014, four in 2015 and seven in 2016. Most cases are filed in Ontario – or prosecuted there if commenced in multiple provinces – but it seems to me that in the past year or so, plaintiffs' counsel are looking to Quebec as a venue where they can re-try some of the interlocutory battles they have already fought and lost in Ontario.

CD: Could you outline some of the common types of disputes driving securities class actions? Are a notable number of these cases cross-border in nature?

Statham: Claims concerning the accuracy of an issuer's reported financial results – with or without a subsequent revision to such results – are a common thread of shareholder class actions. Also common are claims premised on late, incomplete or non-disclosure of key operational events in the life of an issuer's business, such as product, environmental or regulatory issues. Such claims may be accompanied by allegations of misrepresentations as to the state of the issuer's internal controls over financial reporting and disclosure controls and procedures. With respect to the cross-border aspect, NERA's most recent report indicates that approximately half of the shareholder class actions pursued in Canada have involved parallel class proceedings in the US. Among other things, this reflects that many of the corporate defendants to Canadian claims are cross-listed on the TSX and on one or more of the major US exchanges.

Peebles: Unlike the US where M&A securities cases are popular, Canadian cases are generally textbook secondary market continuous disclosure actions. Mining companies and pharmaceutical companies are popular targets, given that their share prices often fluctuate based on investors' perceptions as to their future prospects, such as resources and reserves, and new drugs in development. About half of Canadian cases have had a parallel US class action. And, to add to the complexity of the cross-border issue, several current cases in Ontario have ongoing jurisdiction disputes arising out of the inclusion of purchasers

on US exchanges in the definition of the proposed Canadian action class.

Foreman: Our regime permits claims predominantly in connection with misrepresentation by public securities issuers to the securities markets. The statute establishes a constellation of related actors who can be liable, including the issuer, its directors and officers, experts such as auditors, accountants, engineers and other influential persons such as a promoter or an insider who is not a director. Our statute enables class action claims in the context of a prospectus misrepresentation, a misrepresentation in a takeover bid circular or an offering memorandum and most recently in connection with secondary market trading. A misrepresentation most generally is the making of an untrue statement of material fact or a failure to make timely disclosure of a material fact. We see misrepresentation cases in connection with a wide range of businesses. In Canada, we have a very strong focus on mining and resources and we have seen several cases where development stage or even more mature mining and resources companies were alleged to have made misrepresentations in connection with the cost of mining developments, or in respect of other material matters.

CD: Are there any recent Canadian securities class actions which showcase the intricacies of these types of disputes?

What insights can we draw from their outcome?

Foreman: A crucial case that is not to be missed is *Green v. Canadian Imperial Bank of Commerce et al*., a decision from our Supreme Court of Canada released in December of 2015.

Peebles: There has really been a lull in the development of leave to proceed case law in the last year outside of Quebec. After the motion court decision to deny leave in *Silvercorp* was upheld in the Ontario Court of Appeal in August 2016, the only decision has been *Pretium* in July 2017, in which leave to proceed was granted, with an appeal underway. The more interesting development has been in Quebec, where several recent interlocutory decisions have signalled a willingness of that court to strike a different path from the consensus view in Ontario that the statutory threshold test is meant to deny investors premature access to the confidential information of public issuers: *Derome v. Amaya and Catucii v. Valeant*. The decision of the Quebec Court of Appeal in the former matter will be a strong indicator as to whether the case law will be consistent or divergent in the two jurisdictions on access to corporate documents. Leave to proceed was granted in *Valeant* in late August, which may encourage plaintiff's counsel in that province.

Statham: To date, there are no trial decisions on claims asserting the statutory cause of action for misstatements in secondary market disclosure. Consequently, the case law interpreting and giving meaning to aspects of the statutory regime has developed through motions practice and, in particular, through judicial assessment of the screening mechanism that requires plaintiffs to first obtain judicial leave before proceeding with a statutory claim. In 2015, in widely-read decisions arising from proceedings taken in Quebec, *Theratechnologies Inc.,* and Ontario, *Green v. CIBC*, the Supreme Court of Canada clarified the threshold that a plaintiff must meet to obtain leave. Whereas some lower court decisions had characterised the threshold as a mere 'speed bump' for plaintiffs, the court has now articulated a more rigorous standard that requires motions judges to undertake "a reasoned consideration of the evidence to ensure that the action has some merit", while taking care that the leave motion not cross over into a mini-trial.

CD: What general advice can you offer to parties on preparing for class action litigation? To what extent can expert witnesses and new technologies impact the way a case is conducted, for example?

Peebles: Defendants are usually very interested in the timing of the action, which means, most importantly, the timing of the statutory leave to proceed motion. In Canada, a plaintiff must obtain a court order authorising commencement of a misrepresentation action under the provincial Securities Act. In Ontario at least, defendants can expect a case to move relatively quickly if plaintiff's counsel is efficient and motivated. A case can proceed from service of a motion record for leave to proceed and, usually, for certification as a class action, through filing of a responding record, then cross-examinations, then the exchange of written arguments, to a typically two or three day oral hearing in approximately 10 to 14 months. Expert reports, as to accounting decisions, or resource and reserve estimates, for example, are critical in many cases. The plaintiff's initial report is likely to be

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speculative, as it is based only on publicly available information. The expert report for the defendants, particularly if it is based on otherwise confidential internal corporate information, is therefore a critical turning point in the motion and, therefore, the case.

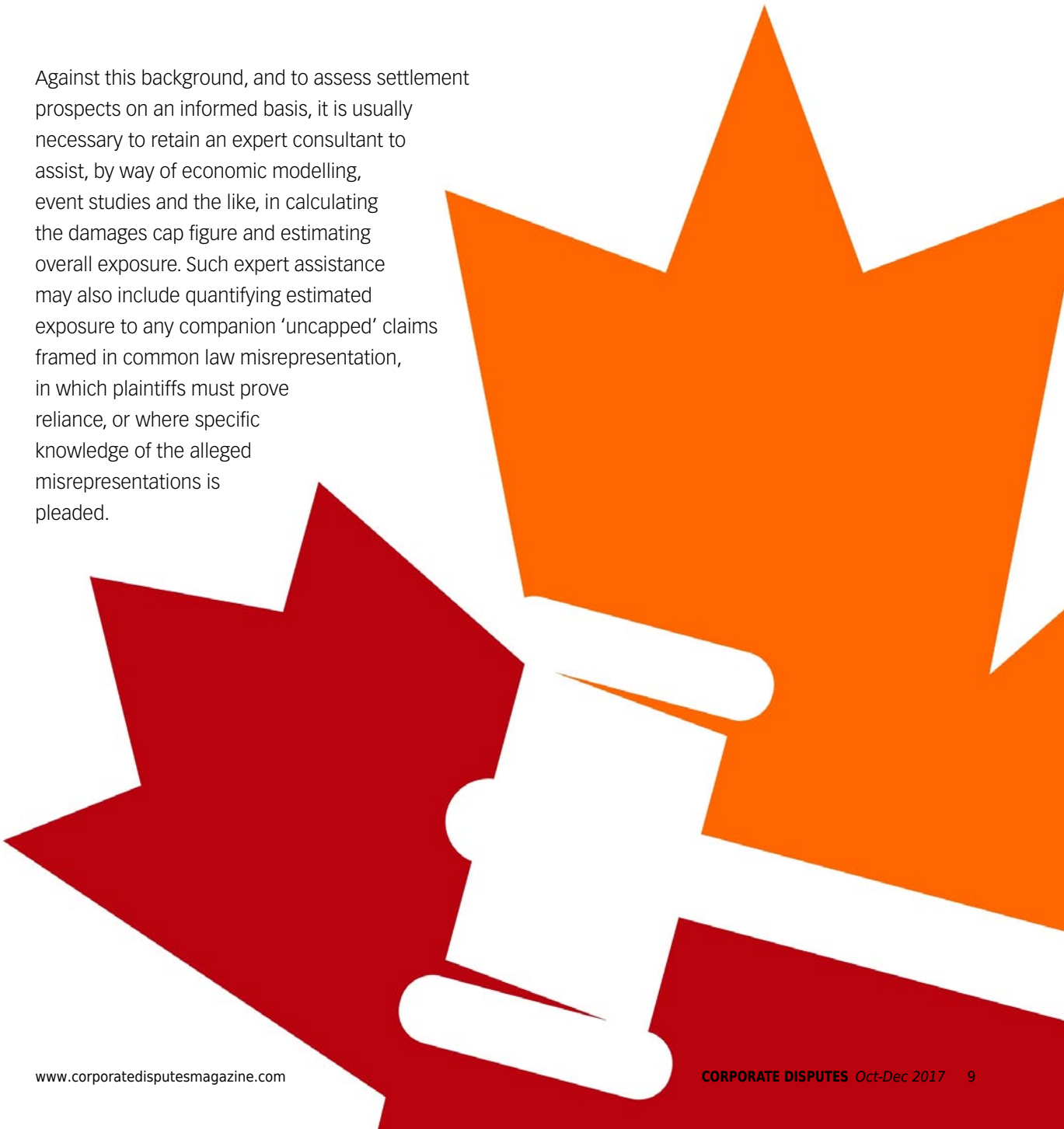
Statham: Early analysis and marshalling of the affidavit and other documentary evidence to be relied on in support of, or in response to, the leave motion is imperative. Naturally, these strategic choices are shaped by the nature and scope of the specific case. Of relevance to defendants is a line of cases in Ontario establishing that plaintiffs cannot compel testimony or documents from defendants to assist plaintiffs in meeting their burden on the leave motion; and defendants are not required to deliver affidavit, or any, evidence on such motions. As a practical matter, many cases will require defendants to provide a detailed evidentiary response, including expert evidence on relevant accounting, materiality and other issues, to have a realistic prospect of defeating the leave motion. However, there may be other cases in which the defendants' best response is to file no evidence at all but, rather, focus exclusively on the insufficiency of the plaintiff's evidence. In either event, early collection and command of the large masses of email and other electronic data that invariably pervade these cases is essential. Counsel typically agree to detailed discovery plans, including specific coding measures and search terms to be employed.

Foreman: Generally speaking, the regime is highly technical and there is a lot of room for interpretation in the statutory structure. My belief is that plaintiffs must be very selective, very organised and persistent. If a case has obvious merit, a defendant is well served to manage the problem and settle it on acceptable terms quickly in order to get on with business. I have seen some recent examples where troubled issuers handled big problems quickly and decisively. The markets rewarded them for that in the longer run. I thought those examples showed great risk management all around.

CD: In Canada, what general considerations should parties make when evaluating potential damages and settlement?

Statham: The statutory scheme set out in the various provincial Securities Acts incorporates specific damages assessment mechanisms. These mechanisms include provisions limiting the liability of defendants, commonly referred to as 'liability limits' or 'damages caps'. In effect, the caps reflect a rough balancing of interests given that the statutory scheme dispenses with any requirement that plaintiffs prove reliance as an element of the cause of action. The damages caps do not apply if the plaintiff proves that a defendant authorised or permitted the making of a misrepresentation while knowing that it was a misrepresentation, however.

Against this background, and to assess settlement prospects on an informed basis, it is usually necessary to retain an expert consultant to assist, by way of economic modelling, event studies and the like, in calculating the damages cap figure and estimating overall exposure. Such expert assistance may also include quantifying estimated exposure to any companion 'uncapped' claims framed in common law misrepresentation, in which plaintiffs must prove reliance, or where specific knowledge of the alleged misrepresentations is pleaded.



Foreman: Our statutory regime is unique in the secondary market setting in that damages are calculable under an express statutory formula. And even the results of that formula are subject to a liability cap that is related to the issuer's market value. That cap can be waived in certain circumstances – mainly if the misrepresentation was made knowingly. In other contexts, damages are determined according to quite well established economic formulae based on trading models and the like. The liability cap in the statute is somewhat controversial but it has undoubtedly played a heavy role in liability assessment and in settlement. It is important no doubt, but I have found that most cases by their nature present a strong risk that the liability cap could be waived.

Peebles: Every case is different in terms of potential damages, depending upon the class definition, the duration of the class period and the swing in the share price after the corrective disclosure. Further, there is little to be gained from looking at the pleaded damages sum in statements of claim, which are based more on counsel's optimism than any rational calculation. However, NERA shows the median settlement value in statutory secondary market cases from 2006 to 2016 to be CDN$9m across 31 court-approved settlements. Certainly the court will want to see some rationale from class counsel for an agreed settlement sum, including an assessment of the cost of prosecuting the action, the risk of failure and some understanding of the size of the class' loss.

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CD: What typical challenges can parties expect to face when involved in securities class action litigation in Canada?

Peebles: I would argue that in most instances, there is a limited public relations price when a securities class action is started. The underlying issue may be a significant one in the minds of investors, but the Canadian market may well be enured, already, to the news of a lawsuit. The critical immediate challenge for a defendant public issuer

and its directors and officers is a strategic one. That is, should the defendants use internal corporate information and documents as a foundation for their responding affidavits, or if so, in what breadth? It can be difficult to refute the usually sweeping but non-specific attack by the plaintiff investor based only on the public disclosure already filed, but opening the evidentiary door gives the investor access to the confidential records of the company which the leave to proceed motion was meant to protect. Every case raises this dilemma anew, but the trend is certainly towards a more, rather than less, detailed response. After the decisions in *Theratechnologies* and *Green v. CIBC* at the Supreme Court, each of the corporate defendants in *Silvercorp, Atlantic Power* and *Eastern Platinum* filed significant evidence on the facts of the cases, and succeeded in resisting leave to proceed.

Foreman: I think it is fair to say that all of these cases are expensive, time consuming and risky. Some are clearer than others but it seems that the regime has sufficient complexity that there is plenty of room for battle on that basis alone.

Statham: Shareholder class actions often present practical challenges of cost, time and resources. The assembly of the evidentiary record and the argument of the leave motion can effect significant erosion of defendants' insurance coverage and consume the time of individual defendants and other senior company management, all before progressing the case to discovery, let alone a trial on the merits. These realities often drive cases down a settlement path at some point along the pre-trial time horizon. Moreover, the absence, to date, of any trial decisions interpreting and applying the statutory cause of action, and the corresponding statutory defences, presents uncertainty which, in turn, may inform parties' settlement calculus. A potentially significant challenge for defendants in some cases is the existence of contemporaneous regulatory proceedings or class proceedings in the US, and the associated need to coordinate and protect the defendants' position to the greatest possible extent in different forums. Canadian courts have, from time to time, commented on and been influenced by mutually inconsistent positions advanced by the same parties in Canada and in the US, respectively.

CD: In what ways are alternative dispute resolution techniques being applied in Canadian class actions?

Foreman: Mediation is probably the leading technique for dispute resolution in Canada. We have a very strong lineup of respected retired judges and experienced senior lawyers who have a lot of success helping litigants solve problems and resolve cases. Beyond that, in my experience leading plaintiff lawyers and defence lawyers here know each other quite well and can often successfully negotiate directly as well without the assistance of a neutral.

Statham: Mediations, as agreed to by the parties and conducted before or after the leave motion and examinations for discovery, are fairly commonplace. The cost-benefit analysis in any given case normally weighs in favour of at least exploring settlement possibilities with the assistance of a skilled mediator. Settlements require court approval. This involves an assessment of whether the proposed settlement falls within a 'zone of reasonableness' from the perspective of the interests of the class members. Generally, early stage settlements attract greater judicial scrutiny than settlements arrived at after discovery. Even where no overall settlement can be achieved, it may be possible, as has transpired in some cases, for the parties to narrow the scope of the proceeding, and get on to the merits, by having the defendants consent to, or not oppose, the plaintiff's leave motion in consideration of the plaintiff's agreement to simultaneously abandon any and all companion claims framed in common law misrepresentation or other causes of action.

Peebles: It does not seem to me that there is any real difference in the use of ADR options in securities class actions as against other class actions.

CD: What is the outlook for securities class action litigation over the next 12 months or so? What trends do you expect to dominate this space?

Statham: We do not see any discrete systemic factors that point to a looming surge, or reversal of the relative lull, in shareholder class actions for misrepresentation in secondary market disclosure. With the Supreme Court of Canada having clarified the threshold test for leave, it will be interesting to evaluate how motions judges go about the task of weighing and sorting through the parties' competing and voluminous evidence, while observing and enforcing the direction that the leave motion is not the trial. Finally, one of these cases will inevitably come to a common issues trial and, when it does, we expect the decision will yield valuable guidance on a range of matters, including materiality, the contours of the reasonable investigation defence and the determination of any uncapped damages claims.

Peebles: I would be surprised to see a dramatic uptick in the pace of securities class action filings in the near future. We have enough guidance already from the courts that our small plaintiffs' bar can rationally assess their options. The case law in Ontario has set a balanced test for the leave to proceed threshold, with real cost penalties for failed motions, which presents a meaningful disincentive to frivolous cases. What we may be seeing, though, is a change in tactics by plaintiffs' counsel in terms of choosing the location to start or prosecute actions. Investors may be seeking out other jurisdictions,

primarily Montreal, to avoid Ontario precedents on access to corporate documents and costs.

Foreman: I expect that in the near term, the outlook will continue to be somewhat conservative by plaintiffs. But I also believe that there is creativity at work on the plaintiff side to make more out of these cases for injured shareholders. We have learned a lot over the last decade and I hope to see some breakthroughs that will improve the picture for shareholders who incur losses in cases of all shapes and sizes. CD