

Torys on Litigation and Dispute Resolution

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Developments in Securities Class Actions in Ontario

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This bulletin discusses developments under Ontario's secondary market liability regime: the status of the claims that have commenced and two decisions that have been rendered regarding the important requirement for plaintiffs to obtain leave to proceed with a claim under this regime. Torys closely monitors developments in securities class actions and will provide updates as cases progress through our courts.

Highlights of the Secondary Market Liability Regime

Ontario's regime for secondary market liability came into effect in 2006 as a result of amendments to the *Securities Act*. The amendments created a statutory cause of action allowing shareholders to seek damages when an issuer fails to make timely disclosure of material changes or an issuer's disclosure contains a material misrepresentation.

Under the regime, a shareholder does not have to prove actual reliance on the misrepresentation or the failure to make timely disclosure. The effect of deemed reliance is to facilitate certification of secondary market claims as class actions. The regime imposes a cap on damages other than in cases where a knowing violation of disclosure obligations has been committed; the regime also requires that the plaintiff obtain leave from the court to proceed with a claim. These measures are intended to protect defendants from coercive and unmeritorious claims, known as "strike suits."

Status of Outstanding Claims

Since 2006, 11 claims have been commenced against issuers. In these claims, individual officers and directors have also been named as defendants, and allegations have been asserted against those individual defendants that, if proven, could entitle the plaintiffs to damages in excess of the damages cap. Some of these claims have, in addition, named financial advisers as defendants.

One of the 11 claims – the *Southwestern Resources* case – has been settled. The plaintiffs had sought damages of \$300 million for the proposed class of shareholders. In the settlement, approved by an Ontario court on November 3, 2008, the defendants agreed to pay \$15.5 million, which includes fees to class counsel in the amount of \$2.5 million.

None of the remaining claims has yet been granted leave by a court to proceed as a claim under the secondary market liability regime. To obtain leave, plaintiffs must show that there is a reasonable possibility that the action will be resolved at trial in the plaintiffs' favour and that the action is brought in good faith. The first leave motion was argued in December 2008. Although the courts have not yet provided any guidance on how they will apply the test for leave, two important decisions have been made on the scope of the evidence available for the leave motion and the procedures

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for that stage of the action that will likely affect the conduct of leave motions that will be litigated in the future.

Procedure on Leave Motions

Section 138.8(1) of the *Securities Act* states that on the leave motion, the plaintiffs and defendants must file affidavits setting out the material facts on which the party relies and that each affiant may be cross-examined in accordance with the rules of court. One of the reasons for including the court's gatekeeper role at the leave motion stage was to reduce the defendants' exposure to costly proceedings; plaintiffs must also obtain leave prior to the close of pleadings and the beginning of the discovery process. This procedure has now been considered by the courts in decisions in the *Imax* and *CV Technologies* litigation.

In *Silver v. Imax Corp.*,¹ the court was asked to limit the scope of cross-examination on defence affidavits filed on the leave motion and to allow the defendants to refuse to produce, among other things, materials provided to the company's auditor. The defence argument was that this limitation was consistent with the court's gatekeeper role at the leave motion stage and would prevent defendants from being exposed to unnecessary and intrusive discovery-like examinations before the close of pleadings in the matter. In rejecting the defendants' position, the Court held that the statutory procedure established for the leave motion expressly permits cross-examination in accordance with the rules of court, and therefore cross-examination is limited only by the "semblance of relevance" test.

Following the *Imax* decision, there was concern that the gatekeeper role of the leave motion may be less effective than previously anticipated. However, in the subsequent *Ainslie v. CV Technologies Inc.*² decision, the Court held that the procedure established by section 138.8(1) of the *Securities Act* must be interpreted to give effect to the intention of the section – that is, to protect defendants and to place the onus on plaintiffs to satisfy the leave test. The Court rejected the plaintiffs' motion for an order compelling each defendant to file an affidavit to allow cross-examination. The Court held that defendants are required to file affidavits only if they intend to rely on material facts in response to the motion for leave. If a defendant is content to rely on expert evidence or evidence obtained on cross-examination of the plaintiffs, then the defendant is not required to file an affidavit. The Court also rejected a motion by the plaintiffs for an order in the alternative for examination of the defendants as witnesses on a pending motion. It would be inconsistent with the gatekeeper role to expose defendants to a costly and time-consuming discovery process before the plaintiffs had satisfied their onus and obtained leave to proceed.

In light of the *Imax* and *CV Technologies* decisions, defendants responding to motions for leave to proceed under Ontario's secondary market liability regime will have to make careful strategic decisions about the evidence they choose to rely on and the extent to which they want to limit or allow potentially wide-ranging cross-examination on the merits of plaintiffs' allegations. **1**

¹ [2008] O.J. No. 1844 (S.C.J.), leave to appeal refused, [2008] O.J. No. 2751 (Div. Ct.) [*Imax*].

² [2008] O.J. No. 4891 (S.C.J.) [*CV Technologies*].