

On Dec. 31, 2005, Part XXIII.1 of the *Ontario Securities Act* (Act), which provides for a statutory right of action against reporting issuers, their officers and directors for misrepresentation in secondary markets, came into force. One of the provisions of the amendment is that plaintiffs must obtain leave of the court to proceed with a claim.

On Dec. 9, 2009, a landmark pair of decisions were handed down by Madam Justice Katherine van Rensburg of the Ontario Superior Court, who in *Silver v. IMAX* granted leave for the first action to be brought pursuant to Part XXIII.1 and certified the first class action claim involving secondary market disclosure.

In-house counsel in public companies have been watching the case with interest. In the decisions, which are currently under appeal, Justice van Rensburg not only certified the claim as a “global” class action, but also, in applying the statutory test for leave, set a low threshold for deciding that the action is brought in good faith; and that the plaintiffs have a reasonable possibility of success at trial.

In light of the *IMAX* decisions, CCCA Magazine asked three lawyers who defend securities class actions to suggest practice points for in-house counsel to consider.

### Here are their top eight suggestions:

#### **1** Correcting misrepresentations or omissions

What happens if your organization discovers that there has been a misrepresentation or an omission?

First of all, there should be a procedure in place that immediately involves in-house counsel. The way the matter is handled from the outset can have enormous implications for your organization.

# Defending

## Eight practice points to safeguard your organization

“If and when an issuer becomes aware that they may have made a misrepresentation (or an omission), they should ensure that the legal department is involved and seriously consider getting external advice,” says Andrea Laing, a partner at Osler Hoskin Harcourt LLP in Toronto, who has been active in defending public issuers pursuant to the new secondary market liability provisions.

“Procedures should be in place to ensure that any potentially material errors or omissions that are discovered are promptly reported and are raised with the legal department so that legal can be involved in the investigation and any corrective measures that are taken,” she says.

“The damages provisions of new Part XXIII.1 are set up so that damages payable by an issuer are measured in relation to the drop in the market price of its securities following a correction,” says Laing. Thus, the way an issuer handles corrections can have a serious effect on its

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# securities class actions

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potential liability and it is critical to get it right, she explains.

“For example, if the issuer “over-corrects” the misstatement, it could magnify its damages. But if it under-corrects, it could be accused of omitting to reveal the true state of affairs — effectively making a new misstatement or omission with the correction,” she says.

## 2 Handling the leave stage

When everyone read these provisions early on and were doing their best to interpret the legislation, a general consensus was that the leave stage would be the critical battleground, says Nigel Campbell, a partner with Blake, Cassels & Graydon LLP in Toronto.

In addition, “it was expected that the threshold in order to obtain leave would be quite severe, that there would be a high threshold of proof,” says Campbell, who defends class action cases across the country.

Yet, as Campbell points out, “the court explicitly says in *IMAX* that their interpretation of the language of the legislation is that it sets “a relatively low threshold.”

“A case like *IMAX* shows how high the stakes in [this type of litigation] can be,” says Campbell. “Not only the [potential] liability, but even through the leave stage. *IMAX* began in 2006 and here we are in 2010 and not done leave yet, which is under appeal,” he says.

“The potential for not only costly, but protracted litigation, which any management will tell you is disruptive and distracting — particularly if it is cross-border with large international ‘classes,’ — is a big drain on the resources and attention of the corporate counsel department and management,” continues Campbell.

“From what I’ve seen, in-house counsel might start revisiting their thinking on many of these cases. If it is quite a low threshold that the plaintiff needs to meet, then maybe you don’t want to take all the time and the energy and the resources and fight the leave stage,” he says.

“Maybe you want to get right to the merits. Strategic thinking will begin to vary now depending on the nature of the case,” he says.

## 3 Disclosing of confidential information

“I think the *IMAX* line of decisions (which now consists of three decisions, including a prior procedural ruling in which Justice [Katherine] van Rensburg ordered the defendant to make broad documentary disclosure prior to the hearing of the leave motion), turns one of the conventional defensive strategies on its head when it comes to securities class actions,” says Laing.

“Together these decisions mean that the automatic response of opposing every procedural step isn’t going to

work in every instance; in fact, there are some serious risks associated with this approach.”

In fact, points out Laing, “now that we have the super-imposition of a leave requirement before someone can even commence an action, and in opposing leave a defendant could expose itself to very invasive documentary production obligations, everyone needs to think seriously, when they are faced with one of these leave applications, as to whether they should be consenting to it.

“As the *IMAX* decision has shown us, the threshold for obtaining leave is very low for a plaintiff so there may not be a lot to be gained for a defendant in opposing leave and in fact there may be a lot to lose,” she adds.

As a result, in-house counsel should consider that “when a defendant files affidavits in opposition to the leave application, it may be opening the door to very extensive cross-examination on the merits of the claim being advanced against it,” she says.

In Laing’s view, “this is really quite extraordinary. You could have a situation where permission has not yet been obtained from the court for the action to even be commenced.

“Yet all of a sudden you can be asked for all kinds of highly sensitive, confidential documents and information that you would not otherwise have to produce until perhaps many months or even years after the litigation has actually been commenced... and not at all, if you succeed in defeating certification.”

One of the issues is that “in the normal course of a class proceeding, the discovery process occurs after certification is granted,” points out Laing. Yet in this type of proceeding, “in contrast, if the potential defendant opposes the leave application by filing an affidavit, a plaintiff may be able to demand extensive document production and come up with creative new claims that they may not have had any basis to assert until they had the opportunity to review the documents.”

“This is a legitimate concern. If in-house counsel are faced with an application for leave to commence a securities class action under Part XXIII.I, they need to resist the automatic impulse to fight it,” she says.

[In-house counsel] “need to weigh the prospect of leave being denied, which will be low in most cases, against the potential downsides of being forced to make early documentary disclosure.

“These downsides include the risk that the plaintiff will uncover ‘support’ for even more threatening claims, the associated legal costs, and the demand on internal company resources that large-scale documentary production can entail. In many cases it just won’t be worth it,” says Laing.

## 4 Forward planning for possible exposure

In-house counsel need to understand the potential exposure to a common law claim, at least a claim that has the

potential to survive the motion for certification.

“In *Bre-X*, the key issue was whether you could bring a common law fraud on the market case in Canada and the court said you could not. In *IMAX*, the judge allowed the case to proceed, but questioned whether it would ultimately succeed,” says Alan D’Silva, a partner with Stikeman Elliott LLP.

But the fact that *IMAX* “got past the first hurdle means that corporate counsel need to deal with the possibility and take this into account in dealing with the exposure,” says D’Silva, a class action defence lawyer who “has been defending eight of the 15 active secondary market class actions.”

## 5 Reviewing your insurance

“My No. 1 piece of advice for in-house counsel is to review your D&O insurance,” says D’Silva.

“In many cases where we are defending a securities class action, or even before that, one of the critical issues we are seeing is that corporations either have inadequate D&O insurance, the wrong insurance, or their insurance coverage does not go far enough,” he says.

For example, in terms of inadequate coverage, “the company may have \$100-million worth of exposure and \$10-million worth of insurance,” he says.

Or, the company “may have coverage that doesn’t go far enough in that they are missing a very important piece of coverage. This is “entity insurance” which also covers the company, and often doesn’t cost them any more money,” he adds.

D’Silva has also seen instances where the corporation “may have the wrong type of D&O insurance because, “it may be a U.S.-based insurer that has given them a policy based on U.S. law that does not cover what is required in Canada.”

Based on what he has seen, D’Silva suggests that in-house counsel “make sure their insurance broker is sophisticated enough to understand securities class actions and have your external counsel review your D&O policies.”

“When you look at the numbers and the kinds of exposures that some of these cases have — in the millions of dollars — it’s very important to have the right D&O coverage,” he points out.

## 6 Vetting ALL core documents

In-house counsel need to expand the range of documents vetted.

“Public issuers should not only be focusing on vetting and verification of core documents such as financial statements, prospectuses, or bid circulars, which I think everyone has always understood have to be absolutely accurate,” says Laing.

Now, documents that might not have been paid the same kind of attention in the past can also be the source of very threatening lawsuits, she says. Press releases, for example, are something issuers



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need to be very concerned about in terms of accuracy, says Laing.

In addition, "public oral statements can also be the source of alleged misrepresentations in a securities class action," says Laing, whose firm is defending a proposed class action where several of the alleged misrepresentations are said to have been made in conference calls to which market participants would have had access.

"If your organization's vetting and verification procedures draw a distinction between documents and oral statements, they shouldn't; both require careful attention," she asserts.

Laing suggests further that in-house counsel should make sure that procedures are in place to document the steps that are taken to verify statements that might affect the market price for a company's securities.

## Recours collectifs contre les émetteurs

### Huit conseils pour faire face au risque « IMAX »

Le 31 décembre 2005, la partie **LXXIII.1** de la Loi sur les valeurs mobilières de l'Ontario est entrée en vigueur. Cette section prévoit un droit de poursuite en responsabilité civile contre un émetteur responsable, ses administrateurs et ses dirigeants pour des fausses représentations faites sur le marché secondaire. L'une des dispositions prévoit que l'autorisation de la cour est nécessaire pour aller de l'avant avec une réclamation.

Le 9 décembre 2009, une décision importante a été rendue par la juge Katherine van Rensburg de la Cour supérieure de l'Ontario dans la cause *Silver c. IMAX*, dans laquelle elle a autorisé le premier recours collectif concernant la divulgation d'informations sur le marché secondaire. Cette décision a été portée en appel.

Les conseillers juridiques d'entreprise d'à travers le pays observent cette cause avec intérêt. Notre publication a demandé

à trois juristes, qui œuvrent en matière de recours collectif dans le domaine des valeurs mobilières, de fournir quelques conseils sur la manière de faire face à cette nouvelle réalité. Voici huit de leurs principales recommandations.

#### 1. Corrigez le tir rapidement

D'abord et avant tout, une procédure doit être mise en place pour impliquer immédiatement le conseiller juridique interne advenant un incident susceptible de déclencher le mécanisme prévu à la partie **XXIII.1** de la loi. En effet, la manière dont l'affaire est gérée dès le départ peut avoir d'énormes conséquences sur l'entreprise.

« Les dispositions de la partie **XXIII.1** portant sur les dommages prévoient que ceux qui sont dus par un émetteur sont calculés en fonction de la chute de l'action sur le marché à la suite d'une correction », explique Andrea Laing, associée chez Osler Hoskin Harcourt à Toronto.

D'où l'importance de réagir promptement et de rectifier le tir avec exactitude.

#### 2. Négociez l'étape de l'autorisation

Lorsque les amendements à la loi sont entrés en vigueur, plusieurs s'attendaient à ce que le test appliqué par les tribunaux pour autoriser le nouveau recours soit sévère. Ils avaient tort, juge Nigel Campbell, associé chez Blakes, Cassels & Graydon à Toronto. « La cour a explicitement dit dans *IMAX* que son interprétation de la loi était qu'elle établissait un seuil relativement bas », note l'avocat.

Dans ces circonstances, « les conseillers juridiques d'entreprise voudront peut-être revoir leur manière de penser », dit-il.

« Peut-être que vous ne voudrez pas accorder temps, énergie et ressources à vous battre lors de la phase de l'autorisation. Peut-être voudrez-vous plutôt vous rendre au fond de l'affaire le plus rapidement possible. La stratégie va

“When it comes to defending one of these types of actions, the better the documents you have to show that you took proper care, the better positioned you are going to be,” she says.

## 7 Educating management and the BOD

Make sure directors and officers and other senior management within the company are aware of their exposure to securities class actions, and how the legislation changed at the beginning of 2006 to allow for this type of claim, says D’Silva.

Education is a huge issue, he says. “A lot of the cases I have been involved in, the people were not aware they could be sued until after they had been sued,” he says.

## 8 Obtaining Buy-In

Buy-in from the board of directors and management is critical, says Campbell.

The clear lesson coming out of the *IMAX* decision is the old adage “an ounce of prevention is worth a pound of cure,” he says.

While corporate counsel have been alert to the risks inherent

in Bill 198, the planning and discussions have been theoretical. “Cases like *IMAX* are ready-made for senior corporate counsel to approach their management and their board,” says Campbell.

“This is very expensive time-consuming litigation; in-house counsel need to draw this to the attention of the board and get the mandate, the buy-in that, ‘I’m not speaking theoretically here, this is a risk, give me the mandate and the resources to adequately plan for this risk,’” he says.

## Further thought

What lies ahead after *IMAX*?

“In a case I’m currently defending, which is just coming to the leave stage, I expect that procedural questions will preoccupy counsel in that case too, for awhile,” says Campbell.

“Until this legislation gets more ‘field-testing’ and the law is developed, there will remain many mechanical and procedural issues to resolve.” ■

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commencer à varier en fonction de la nature du dossier.»

### 3. Jaugez le risque de l’information confidentielle

À ce seuil moins élevé qu’attendu, s’ajoutent d’autres décisions rendues par la juge Van Rensburg dans le dossier *IMAX*, et dans lequel elle a limité la possibilité pour la partie défenderesse d’invoquer des motifs de confidentialité de renseignements corporatifs pour s’opposer à certaines procédures.

Résultat : « Il n’y a peut-être pas beaucoup à gagner pour une défenderesse de s’opposer à l’autorisation; en fait, il y a peut-être beaucoup à perdre », renchérit Andrea Laing.

### 4. Préparez-vous

Le seul fait que l’affaire *IMAX* « ait passé la première étape du nouveau recours signifie que les conseillers juridiques d’entreprise doivent envisager cette possibilité et celle de devoir gérer la visibilité qu’elle engendre », croit Alan D’Silva,

associé chez Stikeman Elliott, qui a participe à « huit des quinze actuels recours collectifs sur le marché secondaire ».

### 5. Revoyez vos assurances

« Mon premier conseil pour des conseillers juridiques d’entreprise est de réviser votre assurance responsabilité pour administrateurs et dirigeants », recommande M<sup>e</sup> D’Silva. Souvent, dit-il, les entreprises qu’il représente n’avaient pas la bonne assurance ou leur couverture n’était pas suffisante.

Il suggère donc que les juristes en entreprise « s’assurent que leur courtier en assurance soit suffisamment sophistiqué pour comprendre les recours collectifs en matière de valeur mobilière et qu’ils fassent réviser la police par un leur conseiller juridique externe ».

### 6. Réviser TOUS les documents importants

Dans la même logique, les juristes qui travaillent dans un contentieux devraient élargir le nombre de documents que

d’ordinaire ils révisent et approuvent. C’est le cas des communiqués de presse, par exemple, qui dépassent le cadre traditionnel des états financiers ou des circulaires, mais qui demeurent des sources potentielles de poursuites sur la base de fausses représentations.

### 7. Éduquez les cadres

« Dans plusieurs des causes dans lesquelles j’ai été impliqué, les gens n’étaient pas au courant qu’ils pouvaient être poursuivis... jusqu’à ce qu’ils le soient », note M<sup>e</sup> D’Silva.

### 8. Ayez les moyens de prévenir

Selon Nigel Campbell, une leçon claire de l’affaire *IMAX* est : « Mieux vaut prévenir que guérir ».

« Il s’agit d’un litige très long et très coûteux, note-t-il. Les conseillers juridiques d’entreprise doivent attirer l’attention de leur conseil d’administration et obtenir le mandat, » en leur rappelant que le risque est réel. D’où la nécessité d’avoir suffisamment de ressources pour planifier adéquatement en conséquence. ■