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The Emergence of a New Battleground: Liability for Secondary Market Violations in Ontario

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I. Introduction

During the past decade, Canada has seen a dramatic rise in securities class action lawsuits.[1] The vast majority of these lawsuits have been filed in Ontario,[2] the location of Canada's principal public securities market, the Toronto Stock Exchange (TSX).[3] The most likely explanation for this development is the enactment of section 138 of the Ontario Securities Act in 2005, otherwise known as Bill 198.[4]

Section 138 (entitled "Civil Liability for Secondary Market Disclosure") amended the Ontario Securities Act by providing aggrieved investors who purchased or sold securities in the secondary trading market an avenue to sue companies and others responsible, including directors and officers, for alleged materially false or misleading statements.[5] The section 138 amendments thus "established a statutory civil liability regime for misrepresentation and omission in a public company's *continuous* disclosure."[6] The amendments, which provide a number of advantages for investor-plaintiffs to recover damages, have generated a significant rise in the number of securities class actions.[7]

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1. BRADLEY A. HEYS, MARK L. BERENBLUT & JACOB DWHYTIE, TRENDS IN CANADIAN SECURITIES CLASS ACTIONS: 2013 UPDATE; FILING STEADY, LAW IN FLUX, AND SETTLEMENTS ON THE RISE, 2 (2014) [hereinafter NERA 2013]. For example, in 2011, a record fifteen securities class actions were filed. *Id. See generally Marc I. Steinberg, International Securities Law–A Contemporary and Comparative Perspective* (1999).
2. NERA 2013, *supra* note 1, at 4. As in previous years, the large majority of cases (eight out of ten) were filed in Ontario.
3. MARC I. STEINBERG, FRANKLIN A. GEVURTZ & ERIC C. CHAFFEE, GLOBAL ISSUES IN SECURITIES LAW 38 (2013); *Contact Us*, TORONTO STOCK EXCHANGE, (Sept. 30, 2014), http://www.tmx.com/en/about_tsx/contact_us.html.
4. *See generally* Province of Ontario Securities Act, R.S.O. 1990, c. S.5 (Can.); BRADLEY A. HEYS & MARK L. BERENBLUT. TRENDS IN CANADIAN CLASS ACTIONS: 2011 UPDATE; PACE OF FILINGS GROWS, PACE OF SETTLEMENT SLOWS (2012) [hereinafter NERA 2011].
5. *See generally* Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.3 (Can.).
6. Mark Gelowitz, *Court Certifies Class Action Against Imax*, THE LAWYER'S WEEKLY (Feb. 19, 2010), http://www.lawyersweekly.ca/index.php?section=article&articleid=1103.
7. NERA 2011, *supra* note 4, at 6.

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The impact of the Section 138 amendments thus largely explains the rise in class actions, enabling investors in Ontario's secondary capital market to recover damages from corporations and other responsible persons who engage in deficient disclosure.[8] In Canada, over ninety percent of capital market activity occurs in the secondary market;[9] therefore, the ability of investors to seek recompense is dramatically more significant under the secondary market than under the primary market civil liability provisions.[10]

Included in the section 138 amendments are key provisions that facilitate recovery in securities class actions.[11] Key investor-friendly aspects of the amendments, for example, include: the elements of reliance and loss causation need not be proven by the plaintiff; in "core" documents,[12] no scienter need be shown; in "core" documents, where there is a material misrepresentation, the burden is placed on the responsible person(s) to establish the conducting of a reasonable investigation and having a reasonable belief; the absence of onerous pleading requirements; and the lifting of the ceiling on damages if the directors, officers, and others responsible (except for the subject issuer) engage in knowing misconduct.[13]

The investor-friendly provisions of section 138 of the Ontario Securities Act seem to best explain why the number of securities class actions filed in that Province have significantly increased. Recent case law has also contributed to the growing number of such lawsuits. For example, in *Silver v. Imax Corp.*,[14] the court set forth a flexible standard for class certification, thus facilitating the initiation of such actions.[15] In this regard, the following section of this article provides illustrative data from Ontario to evidence the recent growth of securities class action filings.

Thereafter, the article focuses on the section 138 amendments, including such provisions as secondary market liability, certification of class status, and the monetary ceiling on liability. Also, the article examines some key differences between the Ontario Securities Act and the United States Securities Exchange Act. Several of these differences explain why Section 138 may be viewed as providing investor-plaintiffs with a more attractive framework, even for U.S. investors who may be able to invoke the Canadian remedial framework.[16]

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8. *See generally* Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.3 (Can.).

9. *See* A.C. Pritchard & Janis P. Sarra, *Securities Class Actions Move North: A Doctrinal and Empirical Analysis of Securities Class Actions in Canada*, 47 ALBERTA L. REV. 881, 882 (2010).

10. Steinberg et al., *supra* note 3, at 139.

11. *Id.* at 138-139; Gelowitz, *supra* note 6.

12. Province of Ontario Securities Act, R.S.O. 1990, c. S.5., § 138.1 (Can.); "'Core documents' include a prospectus, various circulars (such as a take-over bid circular), "management's discussion and analysis . . . annual financial statements and an interim financial report [of the responsible issuer], [and] . . . such other documents as may be prescribed by regulation for the purposes of this definition . . . ." *Id.*

13. *See* Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.3 (Can.); *Court Certifies Class Action Against Imax*, *supra* note 6, at 2; Berenblut *see infra* notes 69-73 and accompanying text.

14. Silver v. Imax Corp. (2009), 105 O.R. 3d 212 (Can. Ont. Sup. Ct.).

15. *Id.* The Court in *Imax* held that the Ontario Securities Act set a relatively low threshold for plaintiffs seeking leave to proceed with an action in court. Silver v. Imax Corp. (2009), 184 A.C.W.S. (3d) 259 (Can. Ont. Sup. Ct. J.) (Leave to Appeal Decision), at ¶ 25.

16. *See, e.g.*, Abdula v. Canadian Solar Inc. (2012) 110 O.R. 3d 256 (Can. Ont. C.A.) (U.S. investors members of securities class action instituted in Ontario).

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II. NERA Statistics

According to studies compiled by National Economic Research Associates (NERA), the number of securities class action lawsuits filed in Canada has steadily increased since 2005. Dozens of new securities class actions have been filed, many of which have been settled.[17] From 1997 to 2007, there were between one and five class actions filed each year, far less than the average of 9.5 claims filed in 2008 and 2009.[18] As of year-end 2013, there are a total of fifty-four active Canadian securities class actions, collectively making claims for more than $19 billion (U.S.).[19]

According to a study compiled by NERA, eight new securities class action lawsuits were filed in 2010, including six cases in Ontario.[20] As of 2010, there were twenty-eight active Canadian securities class actions, representing more than $15.9 billion in total claims.[21] Twenty-five of these cases were instituted under the secondary market liability framework of the Ontario Securities Act.[22]

In 2011, plaintiff-investors filed fifteen new securities class actions, twelve in Ontario, including nine section 138 cases.[23] As of 2011, NERA reported that, out of the thirty-five Ontario Bill 198 cases commenced, thirty-three were filed in Ontario.[24] Within the 2011 report, NERA stated, "[i]n each of the last four years, we have seen at least nine new cases filed–more than in any prior year. Not surprisingly, this trend has been driven by filings of Section 138 cases, which account for more than two-thirds of the forty-six new cases filed between 2008 and 2011."[25]

In 2012, Canadian plaintiff-investors filed a total of nine new securities class actions, including eight class actions involving section 138 cases; each section 138 case was filed in Ontario.[26] Although the total number of securities class actions filed in Canada decreased from 2011 to 2012, the number of section 138 class actions filed in Ontario remained similar to previous years, significantly higher than for years prior to the enactment of the section 138 amendments.[27] As of year-end 2012, there were a total of forty-three section 138 class actions filed since the introduction of the amendments in 2005, including

17. *See* NERA 2013, *supra* note 1; NERA 2011, *supra* note 4; Steve Tenai and Nicholas Saint-Martin, *Recent Developments in Securities Class Actions in Ontario*, 2010 OBA Class Action Colloquium (December 1, 2010), http://nortonrosefulbright.com/files/recent-developments-in-securities-class-actions-in-Ontario-pdf-272kg-52205.pdf.

18. Gilles Cuniberti, *Securities Class Actions and Extra-territoriality: A View from Canada*, CONFLICT OF LAWS (June 30, 2010), http://conflictoflaws.net/2010/securities-class-actions-and-extra-territoriality-a-view-from-canada/.

19. NERA 2013, *supra* note 1, at 1.

20. MARK L. BERENBLUT, BRADLEY A. HEYS & TARA K. SINGH, TRENDS IN CANADIAN CLASS ACTIONS: 2010 UPDATE: CLIMBING TO NEW HEIGHTS–THE NUMBER OF ACTIVE CASES IS AT ITS HIGHEST (2011) [hereinafter NERA 2010].

21. *Id.* at 9.

22. *Id.* at 1.

23. NERA 2011, *supra* note 4, at 5.

24. *Id.*

25. *Id.* at 25.

26. *See* NERA 2010, *supra* note 20.

27. In 2012, there were nine new securities class actions filed in Canada, less than the fifteen new cases filed in 2011. However, eight of these class actions were Bill 198 cases, similar to the nine new cases filed in 2011 and eight new cases in 2010. *Id.*

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twenty-eight class actions that, as of that date, remained pending.[28] As reflected by the NERA statistics, the rising trend in Ontario securities class action filings is largely a result of the section 138 amendments.[29]

In 2013, plaintiff-investors filed ten new securities class actions, nine of which involved section 138 cases with eight of these cases filed in Ontario.[30] The 2013 NERA report states that these new filings are "generally in line with the pace of such filings since 2008 [hence continuing] the trend of a higher volume of cases following the coming into force of the new secondary market civil liability provisions of the provincial securities act since the end of 2005."[31] As of 2013, there have been a total of fifty-two secondary market civil liability class actions filed, with seventeen cases fully settled and four dismissed.[32]

III. Ontario Securities Act

A. Ontario Securities Act Amendments

In 2002, consistent with a more proactive approach taken by other governments towards restoring investor confidence in their capital markets (such as the Sarbanes-Oxley Act of 2002 enacted in the United States),[33] the Ontario government introduced Bill 198, otherwise known as "An Act to Implement Budget Measures and Other Initiatives of the Government."[34] Bill 198 made significant amendments to the Ontario Securities Act, including Section 126.2, which states:

> A person or company shall not make a statement that the person or company knows or reasonably ought to know, (a) in a material respect and at the time and in the light of the circumstances under which it is made, is misleading or untrue or does not state a fact that is required to be stated or that is necessary to make the statement not misleading; and (b) would reasonably be expected to have a significant effect on the market price or value of a security, derivative or underlying interest of a derivative.[35]

Additionally, section 126.1 prohibits any company or person from engaging in conduct that such company or person knows or reasonably should know is fraudulent or manipulative.[36]

28. *Id.*
29. *See generally* NERA 2011, *supra* note 4.
30. NERA 2013, *supra* note 1.
31. *Id.*
32. *Id.*
33. Sarbanes-Oxley Act, Pub. L. 107-204, 116 Stat. 745 (2002); *See* Marc I. Steinberg, Securities Regulation 281-301 (6th ed. 2013).
34. H. Garfield Emerson & Geoff A. Clarke, *Bill 198 and Ontario's Securities Act: Giving Investors and the OSC , Added Muscle*, Fasken Martineau, (Nov. 17, 18, 19, 2003), http://www.fasken.com/files/Publication/4348346f-28f6-4007-b37f-6fe91ca7ff38/Presentation/PublicationAttachment/28e70b5f-89f3-4684-a7ba-7e08688cd5c0/BILL198.PDF.
35. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 126.2 (Can.). To be actionable, any such misstatement or omission must be made material. *Id.* § 126.2. *See infra* note 42.
36. *Id.* § 126.1.

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1. *Liability*

Included in the section 138 amendments are provisions that impose civil liability for deficient secondary market disclosures. Many of these provisions are investor-friendly.[37] The secondary market liability provisions authorize investors to bring a right of action for damages if they purchase or sell securities of a publicly-traded issuer in the time frame during which there is an uncorrected material statement made by such issuer or other responsible person.[38] Liability also may be levied where a subject issuer fails to timely disclose a material change.[39]

Accordingly, sections 138.3(1) and 138.3(3) provide that where a responsible issuer,[40] or person or company acting with the requisite authority on its behalf,[41] "releases a document that contains a [material] misrepresentation, a person or company who acquires or disposes of the issuer's security during the period between the time when the document was released and the time when the misrepresentation contained in the document was publicly corrected,"[42] has a right of action for damages against the issuer and other responsible persons, including its directors, certain officers, influential persons, and experts.[43] Likewise, sections 138.3(2) and 138.4(1) state that liability may be imposed based on a materially misleading "public oral statement",[44] irrespective of the plaintiff's reliance on such statement, against the issuer and specified other responsible parties who acted with knowing or gross misconduct when that statement related to "the business or affairs of the responsible issuer . . . ."[45]

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37. Emerson & Clarke, *supra* note 34; *see* STEINBERG ET AL., *supra* note 3, at 138-39. As discussed earlier, for example, neither reliance nor loss causation need be proven; in "core" documents, the responsible person has the burden to establish the conducting of a reasonable investigation and having a reasonable belief; and the pleading requirements are relatively favorable to plaintiffs. *See supra* notes 11-13 and accompanying text.

38. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 126.2 (Can.); Emerson & Clarke, *supra* note 34.

39. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 126.2 (Can.); Emerson & Clarke, *supra* note 34.

40. Province of Ontario Securities Act, R.S.O. 1990, c. S.5. As defined in Section 138.1, a responsible issuer is defined as: "a reporting issuer, or any other issuer with a real and substantial connection to Ontario, any securities of which are publicly traded." *See infra* note 41.

41. As defined in section 138.1, an influential person, in the context of a responsible issuer, means: "a control person; a promoter; an insider who is not a director or officer of the responsible issuer; or an investment fund manager, if the responsible issuer is an investment fund." *See id.*

42. The term materiality encompasses information that "would reasonably be expected to have a significant effect on the market price or value of a security. . . ." *See id.* § 126.2(1)(b).

43. *Id.* Section 138.3(1) refers to "each director of the responsible issuer at the time the document was released"; and "each officer of the responsible issuer who authorized, permitted or acquiesced in the release of the document . . . ." *Id.* For the definition of influential person, *see supra* note 41.

44. *Id.* § 138.3(2).

45. *Id.* at §§ 138.3(2), 138.4(1). The specified other responsible parties include:

> [i] [T]he person who made the public oral statement; [ii] each director and officer of the responsible issuer who authorized, permitted or acquiesced in the making of the public oral statement; [iii] each influential person, and each director and officer of the influential person, who knowingly influenced, [a] the person who made the public oral statement to make the public oral statement or [b] a director or officer of the responsible issuer to authorized, permit or acquiesce in the making of the public oral statement; and [iv] each expert where, [a] the misrepresentation is also contained in a report, statement or opinion made by the expert, [b] the person making the public oral statement includes, summarizes or quotes from the report, statement or opinion of the ex-

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Section 138.1 of the Ontario Securities Act sets forth the definition of "responsible issuer"; Canadian courts have had occasion to interpret this term. Recently, the Ontario Court of Appeal, in *Abdula v. Canadian Solar Inc.*,[46] focused on whether Canadian Solar qualified as a "responsible issuer" under the statute. Canadian Solar's shares do not trade on any Canadian Stock Exchange. Therefore, Canadian Solar is not a reporting issuer under the Ontario Securities Act, the first option under the definition of a responsible issuer found in Section 138.1 of the Ontario Securities Act.[47] Nonetheless, the company is incorporated in Canada, sells its shares to Canadian investors, and has its principal executive office located in Ontario.[48] The Court of Appeal determined that "an issuer that is not a reporting issuer [under the Ontario Securities Act], but that has a real and substantial connection to Ontario within the meaning of the [Ontario Securities Act], can constitute a 'responsible issuer', and therefore be subject to a statutory cause of action by purchasers in the secondary market. . . ."[49]

Additionally, section 138.3(4) creates liability exposure on a responsible issuer that fails to make a timely disclosure, as defined under the Act, for the benefit of an investor who "acquires or disposes of the issuer's security between the time when the material change was required to be disclosed and the subsequent disclosure of the material change . . . ."[50] This statute creates liability for a responsible issuer irrespective of whether the plaintiff relied on whether such issuer complied with its disclosure requirements.[51] Although section 138.3(4) eliminates the requirement of reliance, section 138.4(5) does not allow an investor to recover damages if the plaintiff acquired or disposed of the security with knowledge that the communication contained a material misrepresentation, or "with knowledge of the material change."[52]

Section 138.4(3) precludes the imposition of liability upon a person or company (but not for, among others, a responsible issuer or officer of a responsible issuer[53]) who does not make timely disclosure–unless the plaintiff proves that such person or company knew, and failed to timely disclose, the material change, or deliberately evaded knowledge of the change, or was "guilty of gross misconduct" in the failure to timely disclose.[54] But importantly, section 138.4(4) provides that a plaintiff is not required to prove the foregoing

> pert, and [c] if the public oral statement was made by a person other than the expert, the expert consented in writing to the use of the report, statement or opinion in the public oral statement.

Id. at § 138.3(2).

46. Abdula v. Canadian Solar Inc. (2012) 110 O.R. 3d 256 (Can. Ont. C.A.). One of the authors of this article, Marc I. Steinberg, was an expert witness in this case.

47. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.1 (Can.).

48. Abdula v. Canadian Solar Inc., 2012 ONCA 211 at para. 3.

49. *Id.* at ¶¶ 1, 2. *See also* Silver v. Imax Corp. (2009), 105 O.R. 3d 212 (Can. Ont. Sup. Ct.) (certifying global class action consisting of Canadian and non-Canadian investors, regardless whether the subject shares were purchased on the NASDAQ or TSX); McCann v. CP Ships Ltd., [2009] O.J. No. 5182 (Can. Ont. Sup. Ct.) (refusing to certify a class comprised of non-Canadian investors where shares were listed on the NYSE and TSX).

50. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.3(4) (Can.).

51. *Id.*

52. *Id.* § 138.4(5).

53. *Id.* at § 138.4(4). Section 138.4(4) states that a plaintiff does not need to prove the matters described in section 138.4(3) in relation to a "responsible issuer; an officer of a responsible issuer; an investment fund manager; or an officer of an investment fund manager." *Id.*

54. *Id.* § 138.4(3).

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(e.g., knowing misconduct) in a lawsuit against "a responsible issuer; an officer of a responsible issuer"; an investment fund manager; or an officer of an investment fund manager."[55].

Section 138.4 describes the plaintiff's burden of proof.[56] When seeking damages for non-core documents,[57] plaintiffs must satisfy a higher burden of proof compared to core documents where defendants must prove that they conducted a reasonable investigation and "had no reasonable grounds to believe that the [core] document or public oral statement contained the misrepresentation."[58] In an action brought under section 138.3 regarding a non-core document, the plaintiff must prove that the person or company: knew at the time the document was released that it contained a material misrepresentation; deliberately avoided inquiring into the document before its release; or was guilty of "gross misconduct" with respect to the release of the document.[59] But, the plaintiff is not required to prove the above if the section 138.3 action involves an expert-defendant.[60]

Section 138.6(1) provides that when several defendants are found liable, each defendant will bear proportionate liability, being liable for the portion of the damages that corresponds to its responsibility for such damages.[61] But, if the court determines that a defendant "authorized, permitted or acquiesced in the making of the misrepresentation or the failure to make timely disclosure while knowing it to be a misrepresentation or a failure to make timely disclosure," the plaintiff may recover the entire amount from such defendant, regardless of its responsibility level.[62] The statute allows a defendant who is ordered to pay the entire amount to seek contribution from any other defendant found liable in the action.[63]

2. *Damages*

Section 138.5(1) outlines the amount of damages recoverable for a complainant who acquires the issuer's securities in the secondary market after either the making of a public oral statement, or the release of a document containing a material misrepresentation, or after the failure to make timely disclosure.[64] With respect to securities "disposed of on or before the 10th trading day after the public correction of the misrepresentation or the disclosure of the material change in the manner required under this Act or the regula-

55. *Id.* § 138.3(4).
56. *Id.* § 138.4.
57. *Id.* § 138.1. Non-core documents are those documents that are not defined as a core document. *Id. See supra* note 12.
58. Note that this standard, with certain exceptions, applies to public oral statements and failure to make timely disclosure. *See* Pritchard & Sarra, *supra* note 9 at 894.
59. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.4(1) (Can.). Moreover, with respect to forward-looking information that contains a material misrepresentation, the subject company or person may avoid liability by proving that: the forward-looking statement contained adequate cautionary language; it set forth the significant factors or assumptions that were employed; and the defendant "had a reasonable basis for drawing the conclusions or making the forecasts and projections set out in the forward-looking information." *Id.* § 138.4(9).
60. *Id.* § 138.4(2). Note that this same standard applies to public oral statements. *See supra* notes 44-45 and accompanying text.
61. *Id.* § 138.6(1)
62. *Id.* § 138.6(2)
63. *Id.* § 138.6(4)
64. *Id.* § 138.5(1).

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tions," damages will equal the difference between the average price paid for the securities and the price received upon the sale of the securities.[65]

If a plaintiff has not disposed of its securities, damages will be awarded in an amount similar to the damages awarded for securities disposed of after the tenth trading day.[66] The defendant may reduce or eliminate damages otherwise incurred by proving that the change in the market price of the securities was not caused by the misrepresentation or failure to timely disclose.[67] One benefit of the damages provision is that plaintiffs likely will not pursue litigation with unrealistic expectations of potential damages, thereby facilitating settlement discussions.[68]

Section 138.7(1) limits the amount of damages recoverable under Section 138.5, when "the actual damages assessed are greater than the liability limits."[69] Section 138.7(1) limits damages, in a Section 138.3 action, to the lesser of the total damages levied against the person or company, and the liability limit for the particular defendant.[70] But other than for the responsible issuer, there is no limit on damages if the plaintiff can prove that the subject person or company knowingly "authorized, permitted or acquiesced" in the wrongdoing.[71] Section 138.7(2) focuses on the knowledge requirement, stating that the plaintiff must prove that the defendant either made the misrepresentation knowingly, or "influenced the making of the misrepresentation . . . while knowing it was a misrepresentation . . . ."[72] In this respect, the liability limits found in Section 138.7 may have been

65. *Id.* If the securities were disposed of after the tenth trading day, damages will be the lesser of: (i) the average price paid for the shares and the price received upon the sale of the securities; and (ii) the difference between the average price paid for the securities and the trading price for the ten trading days following either the public correction of the misrepresentation or disclosure of a material change. *Id. See infra* note 127.

66. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.5(1) (Can.). *See infra* note 127. Section 138.5(1)3 provides:

> In respect of any of the securities of the responsible issuer that the person or company has not disposed of, assessed damages shall equal the number of securities acquired, multiplied by the difference between the average price per security paid for those securities (including any commissions paid in respect thereof determined on a per security basis) and,
>
> i. if the issuer's securities trade on a published market, the trading price of the issuer' securities on the principal market (as those terms are defined in the regulation) for the 10 trading days following the public correction of the misrepresentation or the disclosure of the material change in the manner required under this Act or the regulations, or
>
> ii. if there is no published market, the amount that the court considers just.

Id.

67. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.5(3) (Can.).

68. Andrea Laing & Robert Carson, *Whether Common Law Claims for Secondary Market Misrepresentation?: An Analysis of Certification Decisions in McCann v. CP Ships, Silver v. Imax, McKenna v. Gammon Gold, and Dobbie v. Arctic Glacier*, 7 CANADIAN CLASS ACTION REV. 103, 113 (2011), *available at* http://www.osler.com/uploadedFiles/Our_People/Profiles/L/CCAR%20Vol%207%20No%201%20Article%205%20(Common%20Law%20Claims)%2022363379_1%20(3).PDF.

69. Province of Ontario Securities Act, R.S.O. 1990 c. S.5 § 138.7(1) (Can.).

70. *Id.* The limits on damages are addressed *supra* notes 64-68 and accompanying text; *infra* notes 96-102 and accompanying text.

71. *Id.* § 138.7(2).

72. *Id.*

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added to the Securities Act to offset the elimination of the reliance and causation requirements.[73]

B. Process for Filing a Class Action

Before an investor may pursue a securities class action in Canada, the court must certify the class. Canadian courts thus serve a gatekeeping function; a class action suit must be certified before it can proceed, thereby minimizing frivolous claims.[74] The Canadian Securities Administration explained the reasoning for requiring leave of the court:

> This screening mechanism is designed not only to minimize the prospects of an adverse court award in the absence of a meritorious claim but, more importantly, to try to ensure that unmeritorious litigation and the time and expense it imposes on defendants, is avoided or brought to an end in the litigation process.[75]

Notably, in certifying the class in *Silver v. Imax Corp.*, the court opined that the Ontario Securities Act sets a "relatively low threshold for a plaintiff seeking leave to proceed with an action."[76] This holding may induce investors to more frequently initiate securities class actions in Ontario.[77] Additionally, the relative flexibility of certifying a securities class action, as compared to the United States,[78] may induce investors outside Canada to pursue meritorious class actions based in Ontario.[79] Canadian courts have continued to follow the relatively low threshold set forth in *Imax* to determine whether to grant leave.[80]

Before certifying a class action, a Canadian court thus must assess that the following criteria are met:

> the pleadings disclose a cause of action; that there is an identifiable class of persons that could be represented; that the claims raise common issues that preferably should be resolved together; and that there is a representative plaintiff or plaintiffs who would fairly and adequately represent the interests of the class without conflict of interest and who has a workable plan for advancing the proceeding.[81]

Judicial consideration of the class action claim occurs when the class files the Leave Motion.[82] Section 138.8(1) of the Ontario Securities Act provides that the court will only

73. Laing & Carson, *supra* note 69, at 107.
74. Pritchard & Sarra, *supra* note 9, at 886.
75. *Recent Developments in Securities Class Actions in Ontario*, *supra* note 17; CSA Notice 53-302 (2000), 23 OSCB 7383 at 7390 [CSA Notice 53-302].
76. Silver v. Imax Corp. (2009), 184 A.C.W.S. (3d) 259 (Can. Ont. Sup. Ct. J.) (Leave to Appeal Decision), at ¶ 25.
77. Emily C. Cole, Recent Developments in Canadian Securities Class-Action Law, A.B.A. Sec. Litig. J. 13 (2010); CSA Notice 53-302 (2000), 23 OSCB 7383 at 7390 [CSA Notice 53-302].
78. *See* Gelowitz, *supra* note 6.
79. *Id.* Note that the U.S. Supreme Court's continued recognition of the "fraud on the market" theory to establish a rebuttable presumption of reliance in Section 10(b) actions under the Securities Exchange Act, thereby facilitating class certification, signifies that securities class actions will remain a vital part of the U.S. securities litigation framework. *See* Halliburton Co. v. Erica P. John Fund, Inc., 134 S. Ct. 2398 (2014).
80. *See, e.g.*, Gould v. W. Coal Corp. (2012), 221 A.C.W.S. (3d) 789 (Can. Ont. Sup. Ct.); Dobbie v. Arctic Glacier Income Fund (2012), 3 C.P.C. (7th) 261 (Can. Ont. Sup. Ct.).
81. Pritchard & Sarra, *supra* note 9, at 886-87.
82. Province of Ontario Securities Act, R.S.O. 1990, c.S.5 § 138.8(1) (Can.).

grant leave when it "is (a) satisfied that the action is being brought in good faith; and, (b) there is a reasonable possibility that the action will be resolved at trial in favor of the plaintiff."[83] In order to assess whether the plaintiff has a "reasonable possibility" to win at trial, Section 138.8(2) of the Act requires each party to provide an affidavit containing the material facts upon which it will rely.[84]

In a number of cases, the good faith requirement has been interpreted to require the plaintiffs to establish that they are bringing the action in the honest belief that they have a legitimate and arguable claim, for the purpose of the statutory cause of action, and not for a secondary or alternative purpose.[85] In these cases, it was found that the plaintiffs complied with this standard and thus met the criterion.[86]

With respect to adherence to the "reasonable possibility" requirement, the *Imax* court opined that "there must be something more than a de minimis possibility or chance that the plaintiff will succeed at trial"[87] and that "the adjective 'reasonable' also reminds the court that the conclusion that a plaintiff has a reasonable possibility of success at trial must be based on a reasoned consideration of the evidence."[88] More recently, in *Gould v. Western Coal Corporation*, the court endorsed this threshold standard regarding a plaintiff's possible success at trial.[89] Applying this standard, the *Gould* court denied leave.[90] In so holding, the court reasoned that there was not a requisite possibility that the plaintiff's claims would be successful.[91] The court's decision in *Gould* represents the first denial for leave to bring a class action in the secondary securities market setting premised on an assessment of the merits of the action.[92]

Additionally, Section 138.14 of the Ontario Securities Act provides limitations on when a plaintiff may file suit.[93] The statute limits the time an action may be commenced to three years from the making of the misrepresentation or failure to make timely disclosure.[94] Both the leave requirement and the limitations period to file suit restrict to some extent this statutory right of action.[95]

83. Id. § 138.8(1); Steinberg et. al., *supra* note 3, at 138.
84. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.8(2) (Can.).
85. Silver v. Imax Corp. (2009), 105 O.R. 3d 212 (Can. Ont. Sup. Ct.), at ¶ 308; Cole, *supra* note 77, at 13.
86. Cole, *supra* note 77, at 13-14.
87. Silver v. Imax Corp. (2009), 105 O.R. 3d 212 (Can. Ont. Sup. Ct.), at ¶ 324.
88. *Id.*
89. Gould v. W. Coal Corp. (2012), 221 A.C.W.S. (3d) 789 (Can. Ont. Sup. Ct.), ¶¶ 237, 239.
90. *Id.*
91. *Id.*
92. David Di Paolo & Margot Finley, *Strategy for Defendants Facing a Leave Motion to Commence a Class Action Under the Securities Act*, 8 CANADIAN CLASS ACTION REV. 169 (2013), *available at* http://www.blg.com/en/NewsAndPublications/Documents/TCCAR_-_Strategy_for_Defendants_Facing_a_Leave_Motion_to_Commence_a_Class-Action_Under_the_Securities_Act.pdf.
93. Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.14 (Can.). In the case of a misrepresentation in a document or public statement, investors are barred from filing suit, later than the earlier of (i) three years after the date of first release of the document, or (ii) date of the public statement, containing the misrepresentation, or (iii) six months after the issuance of a news release granting leave to commence an action under Section 138.3 or under similar legislation regarding the same misrepresentation in another province or territory in Canada. *Id.*
94. *Id.* Note that this limitations period is shortened to "six months after the issuance of a news release disclosing that leave has been granted to commence an action under section 138.3 or other comparable legislation in another province or territory of Canada [with respect to the alleged violation]."
95. Laing & Carson, *supra* note 62, at 111.

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C. Cap on Losses

Although the amendments to the Ontario Securities Act provide an easier avenue for investors to recover damages in the secondary market context, the amendments impose a cap on the amount recoverable.[96] In the case of a responsible issuer, Section 138.1 of the Ontario Securities Act states that the cap on damages is the greater of $1 million or 5 percent of the company's market capitalization.[97]

The liability cap for an individual director, officer, or influential person[98] is the greater of $25,000 or fifty percent of such person's total yearly compensation.[99] But except for the responsible issuer, there is no cap on damages with respect to a subject officer, director, influential person, or other subject defendant if it can be proven that such defendant knowingly authorized, allowed, or acquiesced in the making of the misrepresentation or the failure to make timely disclosure.[100]

The damages cap provides many benefits for Canadian courts in dealing with securities class actions; however, there are some negative consequences as well:

> The damage cap seeks to balance remedies for investors against the desire to protect and advance capital activity through the protection of officers and other persons. The limit on damages encourages plaintiffs to focus on actions that likely have merit. The downside is that it is likely to result in investors recovering less than the full amount of their losses, absent clear evidence of fraud. Even then, the liability cap for issuers means that investors are unlikely to recover full compensation in cases of significant fraud.[101]

Nonetheless, the cases thus far settled indicate that the damages cap has functioned in the manner the legislature intended: providing meaningful monetary recovery to investors while limiting what may be perceived as excessive damages.[102]

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96. *See* Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.1.

97. *Id.* In this regard, Section 138.7(1) also must be considered which provides that the damages payable by a subject defendant under Section 138.3 is the lesser of:

> (a) the aggregate damages assessed against the person or company in the action; and
>
> (b) the liability limit for the person or company less the aggregate of all damages assessed after appeals, if any, against the person or company in all other actions brought under section 138.3, and under comparable legislation in other provinces or territories in Canada in respect of that misrepresentation or failure to make timely disclosure, and less any amount paid in settlement of any such actions.

Id.

98. *Id.* § 138.7

99. *Id.* For experts, liability is capped at the greater of $1 million or "the revenue that the expert and its affiliates of the expert have earned from the responsible issuer and its affiliates during the 12 months preceding the misrepresentation." *Id.*

100. *Id.* § 138.7(2). *See* Steinberg et al., *supra* note 3, at 139.

101. Pritchard & Sarra, *supra* note 9, at 905.

102. *See id.*; *see also* NERA 2013, *supra* note 1.

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IV. *Morrison* Compared to *Canadian Solar*

In view of the investor-friendly provisions of the Ontario Securities Act, and the contrasting holdings in *Morrison v. National Australia Bank*[103] and *Canadian Solar*, the issue arises whether U.S. investors will file suit in Canada when the opportunity arises. The plaintiffs in *Morrison* were Australian investors who sued an Australian bank in a U.S. court based on alleged misconduct that occurred in the United States.[104] The Supreme Court in *Morrison* restricted the reach of Section 10(b) of the Exchange Act to situations where there is "the purchase or sale of a security listed on an American stock exchange, and the purchase or sale of any other security in the United States."[105] Because the plaintiffs acquired their securities in Australia, the Supreme Court affirmed the dismissal of the petitioner's claims.[106]

By contrast, the Ontario Court of Appeals in *Canadian Solar* allowed the plaintiff-investors to pursue their claims, even though the Canadian Solar shares were not publicly traded in Canada, but rather on a U.S. exchange.[107] The Ontario Court of Appeals reasoned:

> The subject matter of [the statute] is a remedy to investors for misrepresentation in certain issuers' secondary market disclosure. In this case, at least some of that disclosure emanated from Ontario. That, together with the relationship of Canadian Solar to Ontario, constitutes a sufficient connection between Ontario and Canadian Solar to potentially subject Canadian Solar to a statutory cause of action pursuant to [the Ontario Securities Act].[108]

The Court found the defendants had a sufficient connection to Ontario because the company was incorporated in Canada, its principal executive office was located in Ontario, the company held its annual business meeting in Ontario, and the alleged misrepresentations were contained in documents released in Ontario.[109]

The decision in *Canadian Solar* is far more investor-friendly when compared to *Morrison*. The Court of Appeals decision in *Canadian Solar* "clearly signals Canada's willingness to allow actions against foreign issuers if a real and substantial connection to Canada is established, and may cause plaintiffs to regard Canada as a viable alternative to the United States following its decision in *Morrison*."[110] Some believe that because of Canada's close proximity to the United States, coupled with the comparatively low standard set forth in *Canadian Solar*, "Canada is a natural venue for securities litigation that can no longer be

103. Morrison v. National Australia Bank, 130 S. Ct. 2869 (2010).
104. *Id.* at 2872-73.
105. *Id.* at 2888. The "listing" theory also has been rejected to date. Accordingly, section 10(b) is unavailable when the subject security is listed on a U.S. exchange if the purchase or sale occurs on a foreign exchange. *See, e.g.* City of Pontiac Policemen's and Firemen's Ret. Sys., 752 F.3d 173 (2d Cir. 2014). *See generally* Marc I. Steinberg & Kelly Flanagan, *Transnational Dealings–Morrison Continues to Make Waves*, 46 INT'L LAW 829 (2012).
106. *Morrison*, 130 S. Ct. at 2888
107. Abdula v. Canadian Solar Inc. (2012), 110 O.R. 3d 256 (Can. Ont. C.A.), at ¶ 2.
108. *Id.* at ¶ 49.
109. *Id.* at ¶ 9.
110. Poonam Puri, *Securities Litigation and Enforcement: The Canadian Perspective*, 37 BROOK. J. INT'L L. 967, 1017 (2012).

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conducted in the United States after *Morrison*."[111] The opportunity for U.S. investors to bring their claims in Ontario when the Section 10(b) action is precluded due to *Morrison* should prompt U.S. investors, when feasible, to pursue redress under the Ontario remedial framework.

V. Ontario Securities Class Actions Compared to the United States

In many regards, the Ontario Securities Act is more favorable towards plaintiff-investors than the United States federal securities laws. The United States securities legislation most similar to Section 138 of the Ontario Securities Act is Section 10(b) of the Securities Exchange Act (Exchange Act) and Rule 10b-5 promulgated thereunder by the SEC. To satisfy the requirements of a Section 10(b) action, plaintiffs must plead and prove several elements.[112] For example, plaintiffs must plead and prove that the defendant acted with scienter, "which is a mental state embracing intent to deceive, manipulate or defraud."[113] The pleading requirement sets forth a rigorous standard for plaintiffs to hurdle, the failure of which results in the dismissal of the action.[114] By contrast, a Section 138 pleading may be established without alleging scienter; moreover, the pleading requirements are far more relaxed.[115] In this respect, all that is required in a secondary market class action in Ontario under Section 138, with respect to "core" documents, is the occurrence of an alleged material misrepresentation or failure to correct such a misrepresentation–unless the company, its officers, and its directors reasonably believed, after conducting a reasonable investigation, that the representation was accurate.[116] By not requiring investor-plaintiffs ordinarily to prove scienter, Ontario courts have provided an easier avenue to recover damages.

Another important difference involves the requirement of reliance. In a Section 10(b) cause of action, Section 10(b) generally requires a finding of reliance on the alleged misrepresentation (although recognition of the "fraud-on-the-market" theory to establish a

111. Wulf A. Kaal & Richard W. Painter, *Forum Competition and Choice of Law Competition in Securities Law After Morrison v. National Australia Bank*, 97 MINN. L. REV. 132, 186 (2012).

112. A private action under Section 10(b) requires a plaintiff to establish the following:

- Requisite jurisdictional means
- Status as purchaser or seller of the securities
- Manipulation or deception
- Materiality
- Defendant's scienter
- Reliance
- Loss causation
- Damages

MARC I. STEINBERG, UNDERSTANDING SECURITIES LAW 261-63 (6th ed. 2014).

113. Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976). Final Rule: Selective Disclosure and Insider Trading, SEC Rel. No. 34-43154 (Aug. 21, 2000).

114. Tellabs, Inc. v. Makor Issues & Rights, 551 U.S. 308 (2007). *See* Marc I. Steinberg, *Pleading Securities Fraud Claims–Only Part of the Story*, 45 LOY. U. CHI. L.J. 603 (2014).

115. Emerson & Clarke, *supra* note 34; *see* generally Province of Ontario Securities Act, R.S.O. 1990, c. S.5 (Can.).

116. Province of Ontario Securities Act, R.S.O. 1990, c. S.5 (Can.); STEINBERG ET AL., *supra* note 3, at 138; *supra* notes 11-13 and accompanying text.

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rebuttable presumption of reliance alleviates this burden in an efficient market).[117] This requirement poses an additional obstacle before a plaintiff can recover damages. By contrast, under the Ontario Securities Act, Section 138 provides investors with a deemed reliance feature, providing an investor the right to sue "without regard to whether the person or company relied on the misrepresentation . . . ."[118] The deemed reliance feature lowers the burden for an investor to recover damages.[119] Moreover, Section 10(b) does not differentiate between categories of disclosure; for instance, oral statements and press releases generally are treated the same as documents filed with the SEC.[120]

The Securities Exchange Act also differs from Section 138 of the Ontario Securities Act regarding the elements of loss causation and damages. Under Section 21D(b)(4) of the Exchange Act, a plaintiff carries the burden of proving loss causation and damages.[121] Section 21D(b)(4) provides: "In any private action arising under this title, the plaintiff shall have the burden of proving that the [defendant's violative] act or omission . . . caused the loss for which the plaintiff seeks to recover damages."[122] Section 138 of the Ontario Securities Act differs from the Exchange Act by placing the burden on the defendant to prove that the losses were not caused by its misconduct.[123] Section 138.5(3) states that damages shall not include any amount the defendant can prove is "unrelated to the misrepresentation or the failure to make timely disclosure."[124] Therefore, the defendant must prove that the damages are unrelated to the misrepresentation, unlike the United States' requirement that the plaintiff must establish that the damages are caused by the misrepresentation. This difference illustrates how Section 138 of the Ontario Securities Act is more beneficial to plaintiffs than the Exchange Act.

Although in many regards Section 138 of the Ontario Securities Act is friendlier towards plaintiff-investors than the U.S. Exchange Act, Ontario's ceiling on damages is one drawback. As described above, Section 138 provides for a ceiling on damages, where plaintiffs may only recover (from a company) the greater of $1 million dollars or 5 percent of the company's market capitalization, and from an individual director, officer, or influential person, the greater of $25,000 or fifty percent of such person's total yearly compensation.[125] Significantly, Section 138 does not limit the amount of damages that may be imposed upon such individual if he/she knew about the misrepresentation.[126] Section 10(b) of the Exchange Act does not impose such a ceiling for damages, a benefit for plaintiff-investors in the United States compared to Ontario. Note, however, that the Ex-

117. *See, e.g.*, Halliburton Co. v. Erica P. John Fund, Inc., 134 S. Ct. 2398 (2014) (upholding rebuttable presumption of reliance under fraud on the market theory); Basic, Inc. v. Levinson, 485 U.S. 224, 243 (1988) (adopting fraud on the market theory to provide a rebuttable presumption of reliance).

118. Emerson & Clarke, *supra* note 34; *see generally*, Province of Ontario Securities Act. R.S.O. 1990, c. S.5 (Can).

119. Emerson & Clarke, *supra* note 34.

120. *See* Pritchard & Sarra, *supra* note 9, at 905.

121. Securities Exchange Act of 1934, Pub. L. 73-291, 48 Stat. 881 (codified at 15 U.S.C. §78(a) (2012)). *See* Dura Pharm., Inc. v. Broudo, 544 U.S. 336 (2005).

122. Securities Exchange Act of 1934, at §21D(b)(4).

123. *See* Province of Ontario Securities Act, R.S.O. 1990, c. S.5, § 138.3(1) (Can.).

124. *Id.* § 138.5(3).

125. *Id.* § 138.1

126. *Id.* § 138.7.

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change Act does set forth a formula determined by market price that acts as a limitation on a plaintiff's maximum recovery.[127]

But this seeming benefit may be overrated as recovery may be obtained in a Section 10(b) action only if such elements as scienter and loss causation are proven. Looked at in this fashion, if scienter (i.e., knowledge) is established in an Ontario secondary market case, the cap on damages would be inapplicable with respect to, among others, the responsible officers and directors.[128] Additionally, NERA reports that the median settlement amount for a securities class action lawsuit in the U.S. in 2013 was $9.1 million, compared to a median settlement amount of $8.6 million in Canada.[129] The close proximity in median settlement supports the proposition that, while the damages cap seemingly provides a benefit to Canadian defendants, the actual benefit in reality is smaller.

VI. Conclusion

As discussed above, Section 138 of the Ontario Securities Act is favorable towards investor-plaintiffs because it creates causes of action for plaintiffs and flexible requirements for courts to certify a class. The favorable rules found in Section 138 help to explain why there has been an increase in securities class actions in Canada, and more specifically Ontario. Additionally, the statistics found in the NERA yearly reports indicate that securities class actions filed in Canada have sharply increased since 2005, when Section 138 was introduced. The NERA reports opine that the recent secondary market liability provisions are a chief cause for the increase in securities class actions filed in Canada, and specifically Ontario.[130] Additionally, NERA reports that as of 2013, the thirty-one active Section 138 cases total more than $16 billion in total claims,[131] a significant amount that should incentivize plaintiff-investors to seek recompense.

Because of the plaintiff-friendly provisions found in the Ontario Securities Act, combined with favorable court decisions, U.S. investors will likely seek to litigate future claims that have a sufficient nexus to Canada in the Canadian courts. Moreover, court decisions that certify a global class will shape future litigation in Canada. Due to these developments, securities class actions in Canada (and particularly Ontario) should remain vibrant and may well provide a forum for adequate redress for non-Canadian investors in appropriate cases. It indeed is an interesting shift that today the Ontario securities laws provide

127. Securities Exchange Act, § 21D(e) (setting forth a limitation or "cap" on damages, using the difference between the price that was paid for the security by the purchaser or seller and the security's average price during the 90 days following the date that the corrective disclosure was made). *See* Julia Pashin, *The PSLRA Cap on Securities Fraud Damages: An Empirical Evaluation of the 90-Day "Bounce-Back,"* 41 Sec. Reg. L.J. 169 (2013). By contrast, the Ontario Securities Act provides a damages formula, using a ten trading day period. *See* § 138.5. Section 138.5 "provides a damages formula for three different scenarios, when the plaintiff: (1) sells the stock within the first 10 trading days of the corrective disclosure, (2) sells the stock after the first 10 trading days have passed, and (3) continues to hold the stock." Pashin, 41 Sec. Reg. L.J. at 173. *See supra* notes 65-69 and accompanying text.

128. Province of Ontario Securities Act, R.S.O. 1990, c. S.5 (Can.).

129. *Canadian Securities Class Actions Steady in 2013, According to NERA Economics Consulting Report*, NERA, http://www.nera.com/news-events/press-releases/2014/canadian-securities-class-action-steady-in-2013-according-to-ne.html (Feb. 19, 2014).

130. *See* NERA 2011, *supra* note 4.

131. *See* NERA 2013, *supra* note 1.

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in many instances better investor recompense than Section 10(b) of the Securities Exchange Act.

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