CITATION: Fischer v. IG Investment Management Ltd., 2012 ONCA 47
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# COURT OF APPEAL FOR ONTARIO

Winkler C.J.O., Epstein J.A. and Pardu J. (*ad hoc*)

BETWEEN

Dennis Fischer, Sheila Snyder, Lawrence Dykun, Ray Shugar and Wayne Dzeoba

Plaintiffs (Respondents)

and

IG Investment Management Ltd., CI Mutual Funds Inc., Franklin Templeton Investments Corp., AGF Funds Inc. and AIC Limited

Defendants (Appellants)

Benjamin Zarnett, Jessica Kimmel and Melanie Ouanounou, for the appellant CI Mutual Funds Inc.

James D.G. Douglas, David Di Paolo and Heather Pessione, for the appellant AIC Limited

Joel Rochon, Peter Jervis and Sakie Tambakos, for the respondents

Heard: December 6, 2011

On appeal from the order of the Divisional Court (Anne M. Molloy, Katherine E. Swinton and Thea P. Herman J.J.), dated January 31, 2011, with reasons reported at 2011 ONSC 292, 104 O.R. (3d) 615, allowing an appeal from the order of Justice Paul M. Perell of the Superior Court of Justice, dated January 12, 2010, with reasons reported at 2010 ONSC 296, 89 C.P.C. (6th) 205.

**Winkler C.J.O.:**

## I. Introduction

[1] This appeal raises the question whether a class action by investors against certain mutual fund managers is the preferable procedure for resolving the class members' claims. The statement of claim alleges that the five defendant mutual fund managers, including the two appellants, CI Mutual Funds Inc. ("CI") and AIC Limited ("AIC"),[1] permitted securities market conduct referred to as "market timing"[2] in certain mutual funds that they managed. Market timing is alleged to have caused long-term investors in the affected mutual funds to suffer losses in the value of their investments of several hundred million dollars.

[2] Before the class action was started, the Ontario Securities Commission ("OSC") conducted a lengthy investigation into the practice of market timing in the mutual fund industry. The investigation led the OSC to bring enforcement proceedings against the five mutual fund managers who were named as defendants in the proposed class action. The enforcement proceedings concerned the same market timing conduct that the investors complain about in the present action.

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[1] As indicated in the reasons below, at para. 23, the three other defendants, IG Investment Management Ltd., Franklin Templeton Investments Corp. and AGF Funds Inc., entered into settlements with the plaintiffs after the motion to certify the class action was denied at first instance.

[2] Market timing, as discussed further, at para. 11, involves short-term trading of mutual fund securities to take advantage of short-term discrepancies between the "stale" values of securities in a mutual fund's portfolio and the current market value of the securities.

[3] All of the defendant fund managers entered into settlement agreements with the OSC staff. The terms of the settlements required the five defendants to pay $205.6 million to investors in the relevant mutual funds. For purposes of the OSC settlement agreements, the defendants admitted that: they entered into arrangements with third-party investors, who engaged in market timing; the market timing conduct had occurred; the market timers made profits that adversely affected investors in the relevant mutual funds; and the defendants earned commissions from their arrangements with the market timers. These factual admissions were made on the basis that they were "without prejudice" to the defendants in "any civil or other proceedings which may be brought".

[4] Hearings were then held before a panel of the OSC for the purpose of deciding whether to approve the settlement agreements as being in the public interest pursuant to s. 127 of the *Securities Act*, R.S.O. 1990, c. S. 5. These hearings, which led to the approval of the settlements, were conducted *in camera.*

[5] After the settlements were approved, the plaintiffs brought a motion for certification of a class action. The central contentious issue on the motion was whether the proposed class action met the preferable procedure criterion in s. 5(1)(d) of the *Class Proceedings Act, 1992*, S.O. 1992, c. 6 ("*CPA*"). The motion judge concluded that although the action otherwise satisfied the criteria for certification, it did not satisfy the preferable procedure requirement. This was because, in the motion judge's view, the completed OSC proceedings and settlement agreements fulfilled the judicial economy, access to justice and behaviour modification purposes of the *CPA*.

[6] The Divisional Court disagreed. Writing for the court, Molloy J. held that the OSC proceedings could not be the preferable procedure for recovering damages because the investors' action was for significant monetary damages *beyond* the amount that had been recovered through the OSC proceedings. The court was satisfied that the class action was the only viable procedure for recovering these substantial additional damages. The court went on to grant the motion for certification on certain specified conditions.

[7] The appellant mutual fund managers appeal, with leave of this court, from the Divisional Court's order granting certification of the class action. The appellants submit that the Divisional Court erred in concluding that the class action is a preferable procedure to the OSC proceedings.

[8] I cannot accede to this submission. As will be explained further, in considering whether an alternative means of resolving the class members' claims is preferable to the mechanism of a class action, a court must examine the fundamental characteristics of the proposed alternative proceeding, such as the scope and nature of the jurisdiction and remedial powers of the alternative forum, the procedural safeguards that apply, and the accessibility of the alternative proceeding. The court must then compare these characteristics to those of a class proceeding in order to determine which is the preferable means of fulfilling the judicial economy, access to justice and behaviour modification purposes of the *CPA*. In a given case, certain characteristics will drive the preferability analysis more than others.

[9] In this case, the OSC commenced investigatory and enforcement proceedings into the market timing conduct in question. The OSC staff reached agreements with the defendants to settle the proceedings, and those settlement agreements were then approved by the OSC. The investors did not participate in the proceedings before the OSC and, quite properly, the OSC in approving the settlements did not purport to settle the claims of the investors in a full and final manner. In the circumstances, it would not have been empowered to do so. The essence of the OSC initiative was that of a parallel or complementary proceeding to any civil action brought by the investors.

[10] In my view, the courts below erred by focusing on the substantive outcome of the OSC proceedings, which is not a relevant factor in the comparative analysis under s. 5(1)(d) of the *CPA*. The courts ought instead to have considered the regulatory nature of the OSC's jurisdiction and its remedial powers, as well as the lack of participatory rights afforded to affected investors by the OSC proceedings. A consideration of these two particular characteristics compels the conclusion that the OSC proceedings would not fulfill the *CPA* goal of providing class members with access to justice in relation to their claims. Thus, the OSC proceedings cannot constitute a preferable procedure to the proposed class action for purposes of the *CPA*. The Divisional Court came to the same conclusion, albeit for different reasons, and I would therefore dismiss the appeal.

## II. Background

### i) OSC Investigation and Enforcement Proceedings Concerning Market Timing

[11] In November 2003, the OSC launched an investigation into the practice of market timing in the mutual fund industry. "Market timers" seek to take advantage of the fact that the value of mutual funds – unlike other traded securities – is calculated only once a day (at 4:00 p.m. EST). As a result of time zone differences, the prices of securities principally traded on foreign exchanges may be as much as 12-15 hours old at the time the daily mutual fund valuation is done. As a result, the daily value of a fund may be, for a short period of time, artificially low. Market timers purchase mutual funds they believe are undervalued for a short-term turnaround, unlike the vast majority of unit holders who invest in mutual funds as long-term investments.

[12] Although market timing is not an illegal activity, the profit made by market timers is at the expense of long-term investors. Also, market timing activity in a fund impedes the efficient operation of the fund in a number of ways. The OSC, in launching its investigation, was concerned that some managers of mutual funds were not taking steps to control market timing and were therefore not acting in the best interests of the relevant mutual funds.

[13] At the conclusion of its investigation, the OSC initiated enforcement proceedings against the five defendant mutual fund managers for failing to act in the public interest in relation to market timing activity in the affected funds. The OSC staff entered into

settlement agreements with the defendant managers, pursuant to which the defendants agreed to pay a total of $205.6 million to their investors.

[14] Two separate hearings were held before a panel of the OSC to consider whether to approve these settlement agreements as being in the public interest pursuant to s. 127 of the *Securities Act*. The OSC issued general public notices that the hearings were being held, but gave no direct notice to investors.[3]

[15] The first hearing occurred on December 16, 2004, and involved CI, AIC, IG Investment Management Inc. and AGF Funds Inc. These four parties jointly requested that the matter proceed on an *in camera* basis. The Chair of the OSC agreed to this request, stating:

> We will now go *in camera*. So I would ask those persons in the hearing room who are not associated with any of the four parties, their counsel, or the two Commissions [the Ontario and the Manitoba Securities Commissions] or the MFDA [the Mutual Fund Dealers Association], please, leave.

[16] A second hearing was held on March 3, 2005, to consider the settlement agreement between the OSC staff and Franklin Templeton Investments. It was also conducted *in camera*.

[17] The OSC approved the settlement agreements with the five defendants. All of the agreements specified that the "agreement of facts" are "without prejudice" to the parties in "any civil or other proceedings which may be brought by any other person or agency."

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[3] Four days' notice was given for the first hearing and three days' notice was given for the second hearing.

### ii) Class Proceedings Commenced Against the Defendants

[18] Shortly after the settlements were approved, several investors in mutual funds managed by the defendants commenced a class action on behalf of investors in the funds. The amended statement of claim alleges that the defendants are liable to class members for breach of a fiduciary duty and/or breach of a duty of care owed to class members for failing to take appropriate steps to stop market timing in the affected funds. The plaintiffs seek declaratory and restitutionary relief, as well as general and special damages.

[19] The plaintiffs allege that, by permitting the market timing to occur, the defendants failed to act in the best interests of the fund and all investors in the fund. They assert that market timing caused an annual loss in the value of the affected mutual funds of several hundred million dollars. In addition, they allege that market timing led to the imposition of increased transaction costs on long-term investors, as well as other transaction costs arising from inefficiencies caused by the market timing conduct. The plaintiffs further assert that the amount paid by the defendants to investors under the OSC settlement agreements falls well short of providing full reparation to investors and fails to account for management and transaction costs associated with market timing activity.

### iii) Certification Motion

[20] The plaintiffs' motion to certify the proposed action was heard in December 2009. They filed expert evidence on the motion in support of the assertion that the OSC settlements do not constitute full compensation to investors. According to this evidence,

the settlement with CI represents only 1/7 of the actual loss of CI investors and the AIC settlement represents only 1/3 of the total harm to AIC investors.

[21] The defendants' primary argument in opposing the certification motion was that the action does not satisfy the preferable procedure criterion in s. 5(1)(d) of the *CPA* because the completed OSC proceedings were the preferable procedure for resolving the investors' claims. Section 5(1)(d) states:

> 5. (1) The court shall certify a class proceeding on a motion under section 2, 3 or 4 if,
>
> ...
>
> (d) a class proceeding would be the preferable procedure for the resolution of the common issues...

[22] The motion judge agreed with the defendants' position and refused to certify the action. He concluded that the other four criteria for certification in s. 5(1) were satisfied: (a) the pleadings disclose a cause of action; (b) there is an identifiable class; (c) the claims raise common issues; and (e) there are appropriate representative plaintiffs who could produce a workable litigation plan. Nevertheless, the plaintiffs' failure to satisfy the preferable procedure criterion was fatal to the motion for certification.

**iv) Appeal to the Divisional Court**

[23] The plaintiffs appealed the motion judge's decision to the Divisional Court. By the time the appeal was argued, three of the five defendants had entered into settlements of the class proceedings with the plaintiffs and only CI and AIC remained (and still remain) as defendants.

[24] In reasons delivered on behalf of the court, Molloy J. allowed the plaintiffs' appeal and granted a certification order. The court concluded that the motion judge's analysis of the impact of the OSC settlements on the preferable procedure assessment was "fundamentally flawed" and held that the preferable procedure criterion was satisfied.

[25] Given that this appeal turns on the preferable procedure issue, I now describe in more detail the reasons of the motion judge and the Divisional Court on this issue.

## III. Reasons of the Courts Below

### i) The Motion Judge's Preferable Procedure Analysis

[26] The motion judge described, at paras. 195-200, the general principles regarding the preferable procedure criterion in s. 5(1)(d) of the *CPA*. He noted, citing *Markson v. MBNA Canada Bank*, 2007 ONCA 334, 85 O.R. (3d) 321, at para. 69, leave to appeal to S.C.C. refused, [2007] S.C.C.A. No. 346, and *Hollick v. Toronto (City)*, 2001 SCC 68, [2001] 3 S.C.R. 158, at para. 27, that the preferability inquiry is to be conducted through the lens of the three principal advantages of class actions: judicial economy, access to justice and behaviour modification.

[27] As recognized by the motion judge, at paras. 221-22, there are two core elements of the preferable procedure inquiry: see *Hollick*, at para. 28; *Markson*, at para. 69. The first element is whether the class action would be a fair, efficient and manageable method for advancing the claim. The second element is whether a class action would be preferable to other reasonably available means of resolving the class members' claims.

This question of preferability turns not only on whether a class action would be preferable to individual civil actions, but also on whether a class action would be preferable to "all reasonably available means of resolving the class members' claims": *Hollick*, at para. 31.

[28] The motion judge concluded, at para. 210, that if the OSC proceedings had not taken place, a class action would have been the preferable procedure. And he observed, at para. 221, that even when the availability of the OSC proceedings is considered, a class action would meet the first element of the *Hollick* inquiry because it constitutes a fair, efficient and manageable method for resolving the claims of the class members. However, the motion judge went on to conclude that the proposed class action does not meet the second element of the *Hollick* inquiry because the action is not preferable to other reasonably available means of resolving the class members' claims. In his view, the OSC proceedings were the preferable procedure for resolving these claims.

[29] In reaching this conclusion, the motion judge found that the OSC proceedings accomplished the *CPA* goals of behaviour modification, judicial economy and access to justice: see paras. 235-60. In his view, behaviour modification was achieved by penalizing the defendants for their failure to respond to the market timing conduct (para. 236); judicial economy was achieved by securing compensation for all investors in "an efficient, principled, and consistent way" (para. 238); and access to justice was accomplished because the OSC settlements included the same form of remedy sought by the class action (*i.e.*, monetary relief), and in reaching the settlements, the OSC staff took

an adversarial stance towards the defendants in a manner akin to the role of class counsel, demanding concessions from the defendants and the payment of compensation for the investors (paras. 246-48).

[30] The motion judge further observed, at para. 252, that the debate over whether the OSC proceedings were the preferable procedure could not be "converted into a settlement approval hearing" under the *CPA*. However, he was of the view that the criteria that a court applies when deciding whether to approve a negotiated settlement of a class action are relevant "when a court considers the issue of preferable procedure and the issues of behaviour modification, judicial economy and access to justice" (at para 252). After setting out the settlement approval criteria, the motion judge held, at para. 254, that, with one exception, the application of these criteria "favour the conclusion that the OSC proceeding was the preferable procedure."

[31] Finally, before leaving the discussion of access to justice – which he saw as the definitive issue weighing against certification – the motion judge considered the plaintiffs' argument that the quality of the access to justice provided by the OSC proceedings was "in doubt because the OSC may have left the investors' money on the table" (para. 255). The motion judge refused to give effect to this argument and instead accepted the defendants' submission that, once the court is satisfied that the OSC's purpose was to obtain restitutionary compensation for the harm suffered by the investors and that the process to do so was adequate, the court should not "second-guess" the access to justice provided by the OSC proceedings (at paras. 256-57).

**ii) The Divisional Court's Preferable Procedure Analysis**

[32] The Divisional Court allowed the plaintiffs' appeal from the motion judge's order refusing certification. In doing so, Molloy J. described three errors in the motion judge's preferable procedure analysis, at para. 33:

> 1) he failed to apply the low evidentiary burden on the plaintiffs at the certification stage;
>
> 2) he improperly found that the "completed OSC proceeding was a preferable proceeding for the remaining portion of the plaintiffs' claims going forward"; and
>
> 3) he erred in law by considering the criteria for approval of a settlement at the certification stage.

[33] Molloy J. explained that the first two errors are closely related. On the one hand, the motion judge found that there was "some basis in fact" to support the investors' assertion that the OSC settlement only represented part of the total damages claimed by the investors. However, in Molloy J.'s view, the motion judge went on to disregard this finding in his analysis of the preferable procedure.

[34] According to Molloy J., at para. 8, the plaintiffs' action "does not seek the recovery of the $205 million already paid; it seeks recovery of the damages not recovered through the OSC proceeding." In her opinion: "Unless it can be said that the plaintiffs have achieved full, or at the very least substantially full, recovery, they are entitled to maintain this action. There is no other viable alternative for recovering the shortfall after the OSC settlement".

[35] Molloy J. went on to conclude, at para. 41, that the key point indicating that a class action is the preferable procedure is that "it is ... illogical to characterize the OSC proceeding as a preferable procedure for recovering that money which the OSC proceeding failed to recover in the first place. It is by definition not a preferable procedure in those circumstances."

[36] Molloy J. held, at para. 47, that the motion judge further erred by applying the test for approval of a settlement in the context of a certification motion. She explained, at paras. 48-57, why these criteria should not be taken into account at the certification stage.

## IV. Analysis

[37] On appeal to this court, the appellants contend that the Divisional Court committed two errors:

1) the Divisional Court applied the incorrect standard of review to the motion judge's decision; and

2) the Divisional Court erred in its preferable procedure analysis.

[38] I will first briefly deal with the standard of review issue and then turn to the issue of the preferable procedure analysis.

### 1) Standard of Review Applied by the Divisional Court

[39] The appellants submit that the Divisional Court failed to accord the "special deference" owed to the motion judge's exercise of discretion in deciding that the preferable procedure requirement was not met, citing *Pearson v. Inco Ltd.* (2006), 78

O.R. (3d) 641 (C.A.), at para. 43, leave to appeal to S.C.C. refused, [2006] S.C.C.A. No. 1. As stated in their factum, the motion judge "was sensitive to the applicable legal principles to be brought to bear in the preferable procedure analysis."

[40] I agree with the appellants that substantial deference must be accorded to motion judges in certification proceedings and that a reviewing court should only intervene with a motion judge's certification decision when the judge makes a palpable and overriding error of fact or otherwise errs in principle. This standard of review is well-established in the jurisprudence: see *Pearson*, at para. 43; *Cassano v. The Toronto-Dominion Bank*, 2007 ONCA 781, 87 O.R. (3d) 401, at para. 23, leave to appeal to S.C.C. refused, [2008] S.C.C.A. No. 15; *Markson*, at para. 33; *Cloud v. Canada (A.G.)* (2004), 73 O.R. (3d) 401 (C.A.), at para. 39, leave to appeal to S.C.C. refused, [2005] S.C.C.A. No. 50.

[41] In my view, however, the Divisional Court did not err in its application of the standard of review. The court identified, at para. 58, errors in principle in the motion judge's approach to the preferable procedure inquiry, which provided the basis for appellate intervention. Among the errors in principle identified by the Divisional Court were the motion judge's application of "the wrong test in his consideration of the preferable procedure test for certification" and the motion judge's error in considering factors relevant to the approval of a settlement at the certification stage. Deference cannot shield errors in principle.

[42] I agree with the Divisional Court's holding that the motion judge erred in principle in reaching the conclusion that the OSC proceedings provided the preferable procedure for resolving the class members' claims. However, as I will now discuss, my reasons for reaching this conclusion differ from those expressed by the Divisional Court.

### 2) The Preferable Procedure Inquiry

[43] Turning to the merits of the Divisional Court's preferable procedure analysis, in my view, the error in principle that led to the motion judge's incorrect conclusion on preferability was more fundamental than his alleged failure to recognize that a substantial amount of the monetary damages claimed by investors went uncompensated in the completed OSC proceedings. The question whether the OSC settlements provided investors with all or substantially all of the monetary relief that they seek in the class action is not the proper focus of the preferable procedure inquiry.[4] In other words, the Divisional Court did not ask itself the right question.

[44] The second element of the preferability inquiry described in *Hollick* requires a comparative analysis as to whether a class action would be preferable to other reasonably available means of resolving the class members' claims.[5] The preferability inquiry must necessarily take into account the central characteristics of the proposed alternative proceeding as a means of resolving the claims. This exercise includes, but is not limited

[4] I will explain this specific point in more detail, at paras. 75-79.
[5] McLachlin C.J. noted in *Hollick*, at para. 29, that s. 5(1)(d) of the *CPA* requires that a class action be the preferable procedure for "the resolution of the *common issues*" (emphasis added), rather than the preferable procedure for the resolution of the class members' claims. However, as she went on to explain, at para. 30, the question of preferability "must take into account the importance of the common issues in relation to the claims as a whole."

to, considering the following characteristics of the alternative proceeding: the impartiality and independence of the forum; the scope and nature of the alternative forum's jurisdiction and remedial powers; the procedural safeguards that apply in the alternative proceeding, including the right to participate either in person or through counsel and the transparency of the decision-making process; and the accessibility of the alternative proceeding, including such factors as the costs associated with accessing the process and the convenience of doing so.

[45] These characteristics must be considered in relation to the type of liability and damages issues raised by the class members' claims against the defendants in the putative class action and the manner in which they are addressed, if at all, in the alternative proceeding. The court must then compare these characteristics to those of a class proceeding through the lens of the goals of the *CPA*: judicial economy, access to justice and behaviour modification.

[46] Not all of the characteristics outlined above will be material in a given case. Each case will of course turn on its own facts. The requisite comparative analysis in the instant case, however, reveals the following important differences between the OSC proceedings and the class proceeding, which support a conclusion that a class proceeding is preferable for resolving the class members' claims:

> i) The jurisdiction of the OSC under s. 127 of the *Securities Act* is regulatory (*i.e.*, protective and preventative), not compensatory. Accordingly, the remedial powers available to the OSC under the section

> are insufficient to enable it to fully address the class members' claims in the proposed class proceeding.
>
> ii) The OSC proceedings did not provide comparable rights of participation to the affected investors as the procedural rights enshrined in the *CPA*, or any participatory rights for that matter.

[47] I will now elaborate on the significance of these distinctions, particularly in relation to the second element of the preferable procedure inquiry as described in *Hollick* (*i.e.*, whether a class action would be preferable to other reasonably available means of resolving the class members' claims). While I agree with the motion judge that the critical question in this regard is whether the OSC proceedings met the objective under the *CPA* of providing the proposed class members with access to justice, in my view, a comparative examination of the key characteristics of the OSC proceedings with the proposed class action reveals that the OSC proceedings did not provide class members with access to justice and thus cannot be the preferable procedure for resolving their claims.

### 1. The Essential Differences Between the OSC Proceedings and the Proposed Class Action

#### i) The Scope and Nature of the OSC's Jurisdiction and Remedial Powers

[48] In arguing that the preferable procedure requirement was met, the plaintiffs provided evidence about the scope and purpose of the OSC's jurisdiction and remedial powers in the form of an affidavit from Professor Poonam Puri, an Associate Professor at

Osgoode Hall Law School and Head of Research and Policy at the Capital Markets Institute of the Rotman School of Management. In her affidavit, Professor Puri explained:

> Public enforcement by securities regulators and criminal enforcement by criminal law authorities, as well as private enforcement by investors through private suits and class action proceedings all play an important role in ensuring that public company managers and mutual fund managers act in the best interests of shareholders and unit holders, respectively. None of these mechanisms is mutually exclusive. [Footnote omitted.]

[49] Professor Puri's evidence outlined the essential purposes of the OSC enforcement proceedings as well as the role of private enforcement, including class action litigation, in regulating the behaviour of capital market participants such as the defendants. As Professor Puri explained in her affidavit, the OSC's regulatory jurisdiction over the defendants under s. 127 of the *Securities Act* was exercised in a different context and for a different purpose than the court's jurisdiction to adjudicate class actions and other civil claims concerning the defendants' conduct.

[50] For ease of reference, s. 127 of the *Securities Act* provides in part as follows:

> 127. (1) The Commission may make one or more of the following orders if in its opinion it is in the public interest to make the order or orders:
>
> 1. An order that the registration or recognition granted to a person or company under Ontario securities law be suspended or restricted for such period as is specified in the order or be terminated, or that terms and conditions be imposed on the registration or recognition.
>
> 2. An order that trading in any securities by or of a person or company or that trading in any derivatives by a person or

company cease permanently or for such period as is specified in the order.

…

3. An order that any exemptions contained in Ontario securities law do not apply to a person or company permanently or for such period as is specified in the order.

4. An order that a market participant submit to a review of his, her or its practices and procedures and institute such changes as may be ordered by the Commission.

…

6. An order that a person or company be reprimanded.

7. An order that a person resign one or more positions that the person holds as a director or officer of an issuer.

…

8.4 An order that a person is prohibited from becoming or acting as a director or officer of an investment fund manager.

8.5 An order that a person or company is prohibited from becoming or acting as a registrant, as an investment fund manager or as a promoter.

9. If a person or company has not complied with Ontario securities law, an order requiring the person or company to pay an administrative penalty of not more than $1 million for each failure to comply.

10. If a person or company has not complied with Ontario securities law, an order requiring the person or company to disgorge to the Commission any amounts obtained as a result of the non-compliance.

(2) An order under this section may be subject to such terms and conditions as the Commission may impose.

…

> (4) No order shall be made under this section without a hearing, subject to section 4 of the *Statutory Powers Procedure Act*.

[51] The decision of the Supreme Court of Canada in *Committee for the Equal Treatment of Asbestos Minority Shareholders v. Ontario (Securities Commission)*, 2001 SCC 37, [2001] 2 S.C.R. 132, illustrates the distinction referred to by Professor Puri. In this decision, Iacobucci J. described the scope and purpose of the OSC's jurisdiction under s. 127 of the *Securities Act*. At para. 42, he cited with approval the following statement by Laskin J.A. in the decision under appeal: "The purpose of the Commission's public interest jurisdiction is neither remedial nor punitive; it is protective and preventive, intended to be exercised to prevent likely future harm to Ontario's capital markets". Iacobucci J. elaborated on the nature and extent of the OSC's jurisdiction under s. 127 as follows, at para. 45:

> In summary, pursuant to s. 127(1), the OSC has the jurisdiction and a broad discretion to intervene in Ontario capital markets if it is in the public interest to do so. However, the discretion to act in the public interest is not unlimited. In exercising its discretion, the OSC should consider the protection of investors and the efficiency of, and public confidence in, capital markets generally. In addition, s. 127(1) is a regulatory provision. The sanctions under the section are preventive in nature and prospective in orientation. Therefore, s. 127 cannot be used merely to remedy *Securities Act* misconduct alleged to have caused harm or damages to private parties or individuals.

[52] These passages from *Asbestos Minority Shareholders* make it clear that s. 127 is not intended to serve as a compensatory or remedial provision with respect to harm done to individual investors. Rather, this provision empowers the OSC to regulate capital

markets in a way that protects investors and the efficiency of capital markets. For example, s. 127 permits the OSC to make orders to: cease trade; prohibit an individual from becoming an officer or director of a public company; issue reprimands; levy an administrative penalty of up to $1 million for each failure to comply with Ontario securities law; and make an order for disgorgement to the OSC of any amounts obtained as a result of non-compliance with Ontario securities law. Section 127 does not empower the OSC to make orders requiring a party to make compensation or restitution or to pay damages to affected individuals.

[53] In contrast, s. 128 of the *Securities Act* allows the OSC to apply to a judge of the Superior Court to make a variety of orders, including orders requiring compensation or restitution to the aggrieved person or company, and requiring payment of general or punitive damages to any person or company. The OSC did not bring a s. 128 application in relation to the market timing conduct in issue here.

[54] The OSC proceedings and the civil action in the form of the proposed class proceeding are intended as parallel, not mutually exclusive, proceedings. It is worth noting, for purposes of analogy, that a court may make an order under s. 128 (including an order for restitution or punitive damages) despite the existence of any order made by the OSC under s. 127.

[55] Unlike enforcement proceedings under s. 127 of the *Securities Act*, the purpose of the proposed class proceeding is to obtain relief for investors – monetary or otherwise –

who claim to have suffered losses from the defendants' impugned conduct. While the OSC in this case approved settlement agreements that included a compensatory element for investors arising from the same impugned conduct, such voluntary payments by the defendants cannot alter the regulatory purpose of the OSC proceedings for purposes of the preferability analysis under the *CPA*. The role of the OSC proceedings was not to assess the liability issues raised in the statement of claim, such as the alleged breaches by the defendants of a fiduciary duty or a duty of care owed to the investors, or to quantify the harm allegedly caused by such breaches.

[56] The disparate purpose of the OSC proceedings and the proposed class action is emphasized by comments made by Commission counsel during the settlement approval hearing. In response to a request by the Chair of the OSC for an explanation of the basis upon which the settlement quantum was determined, counsel stated:

> We didn't include a formula for the calculation in the Settlement Agreement because there are different ways of determining the amount and different legitimate theories as to what the proper method of calculation would be. And it would be quite possible that the Respondents [the defendant mutual fund managers] would have chosen a different method that was also justified, or Staff could have chosen a different method that was also justified if this had been a contested proceeding. So the method that was used was the parties tried to relate it to the standard that would have been expected of the fund managers at the time of trading.

These comments by Commission counsel reflect that the OSC did not attempt to quantify the payment arrived at in the settlement agreements in a manner analogous to the way in which damages might be calculated in a civil action brought by investors.

[57] This comment also demonstrates another important distinction between the OSC proceedings and the proposed class action. As discussed next, the procedure adopted by the OSC was characterized by the marked lack of access – both participatory and informational – that was provided to the investors.

**ii) Lack of Participatory Rights of Investors in the OSC Proceedings**

[58] In contrast to the procedure underpinning a class proceeding, which is premised on facilitating transparency and participation on a class-wide basis, the OSC proceedings provided little to no basis for investor participation.

[59] While a general notice of the settlement hearings was posted on the OSC's website, there was no attempt to notify the affected investors that the hearings were being held. Neither the investors nor their counsel attended the hearings or made submissions. Moreover, the substantive portions of the hearings took place *in camera* and were thus closed to anyone but counsel for the defendants and the relevant regulatory commissions.

[60] Similarly, the procedure by which the settlements were arrived at did not facilitate investor participation. The amount of compensation that the defendants agreed to pay to the affected investors as a term of the settlement agreements was calculated without any opportunity for the investors to participate and without any details in the record of the OSC proceedings as to how this amount was calculated.

[61] In contrast, the purpose of the procedural vehicle of the class action is to allow for the appointment of a representative plaintiff who shares a sufficient common interest with

members of the class. The representative plaintiff conducts the litigation on behalf of class members under court supervision[6] and within the presumptive principle of an open court.

[62] The observations about the accessibility of the OSC proceedings are not meant to suggest that the elements of confidentiality and lack of participation by the investors made the hearings and settlement agreements somehow inappropriate or nefarious. On the contrary, the point is that the OSC proceedings were not intended or designed to provide the investors with access to justice for purposes of adjudicating the claims advanced in the proposed class proceeding. In short, the investors were not, and were not intended to be, parties to the OSC process.

[63] Indeed, it is worth repeating that the settlement agreements signed by the defendants expressly contemplated that they could face civil law suits in relation to the conduct that gave rise to the settlements. The OSC settlements simply resolved the proceedings taken by the OSC against the defendants. The settlements did not finally resolve the claims of the investors as against the defendants, nor did they purport to do so.

[64] I will now explain how the courts below failed to consider these essential differences between the OSC proceedings and the class proceeding in the preferable procedure analysis.

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[6] See *Fantl v. Transamerica Life Canada*, 2009 ONCA 377, 95 O.R. (3d) 767, at paras. 44-47.

**2. Errors in the Preferable Procedure Analysis of the Courts Below**

[65] The motion judge's reasons, at paras. 57-69, for dismissing the plaintiffs' argument that they would be denied access to justice if the class proceeding were not certified reflect his failure to properly consider the defining characteristics of the OSC proceedings in his preferability analysis. The motion judge, at para. 60, dismissed the evidence and argument concerning the different and, indeed, complimentary purposes of the OSC regulatory proceedings and the proposed class proceeding as "largely irrelevant to the objective issues that I must decide". He classified this discussion as a debate about procedural fairness and gave three reasons for concluding that the issue of procedural fairness "is not material or is subsumed by the debate about access to justice":

> 1) The OSC proceedings did not bind the investors, who are free to commence a proposed class proceeding and seek its certification (para. 61).
>
> 2) The investors did not have the right to opt out of the OSC proceedings and they would have the right to opt out of class proceedings. Nevertheless, it is unlikely any member of the class would opt out, because a class proceeding would be the only viable means for them to exercise their private rights. Moreover, "it would be a pointless argument to suggest on behalf of the investors that a class proceeding provides procedural fairness and is the preferable procedure because one has the opportunity to opt out of it" (para. 62).
>
> 3) Procedural fairness considerations must include the fact that class members will not have their "day in court" in the conventional sense because it is only the representative plaintiff and class counsel who have a truly participatory role. The procedural fairness that justifies binding the class members to the outcome of

> the common issues trial or a negotiated settlement is only provided by proxy (para. 67).

[66] These three factors – when properly analyzed – support, rather than militate against, a finding that a class action would be the preferable procedure for resolving the common issues raised by the class members' claims.

[67] The fact that the OSC proceedings did not bind investors is a reflection of why it cannot be said that the investors have had access to justice. In the words of the motion judge, at para. 61: "the Defendants are not denying an investor's ability to seek private recourse through the court system." The only conclusion that could be drawn is that even the defendants contemplated the prospect of civil proceedings. The reasons for this are clear: no settlement on compensation was ever agreed to by the class members; nor was the matter of compensation adjudicated by any body of competent jurisdiction, such as might have the effect of limiting juridical recourse.

[68] The motion judge's second reason also contains the recognition that a class action is the preferable procedure in light of the principle of access to justice. He observed that an individual action is not a viable process "given the small size of the individual claims and the difficulties of forensic proof" (para. 62). However, the motion judge concluded that because no one would want to opt out of the class action, the right to opt out is irrelevant to access to justice considerations.

[69] While this speculation about future opting out may ultimately prove to be correct, it ignores the well-settled principle that a right to opt out is an important element of

procedural fairness in class proceedings. It is not an illusory right that should be negated by speculation, judicial or otherwise. Further, on a practical level, the fact that the economics of judicial recourse is a potential barrier to proceeding individually is an argument in favour of – not against – certification of a class proceeding.

[70] The motion judge's third reason for dismissing the plaintiffs' argument regarding procedural fairness misconstrues the very rationale for and approach to class proceedings in this province. According to the motion judge, at paras. 67-69, even if a class action were to be certified, investors would not truly have their day in court unless individual assessment trials were required. In support of this conclusion, the motion judge noted that class action litigation is prosecuted by representative plaintiffs and class counsel and, accordingly, investors "would be non-participants in the resolution of the common issues" (at para. 69). The motion judge then equated the non-participation by investors in the OSC proceedings with the so-called non-participation by investors in a class action, at para. 69:

> In my opinion, the issue in this case is not whether the investors *who were non-participants in the OSC proceedings and who would be non-participants in the resolution of the common issues* had or would have procedural fairness. The issue is whether they have had access to justice and whether the other important values of the *Class Proceedings Act, 1992* have been satisfied. The considerable power of the subjective and emotive plea that the investors have not had their day in court misdirects the analysis from the access to justice and other policy issues that inform the preferable procedure debate... [Emphasis added.]

[71] The notion that class members would not have their day in court unless individual assessment trials were to take place is contrary to the very essence of a class proceeding. Were it to be accepted as a general principle, it would serve to defeat every certification motion. The fundamental purpose of the class proceeding is to provide access to justice, not to deny it. Equating the *total* lack of participation by investors in the OSC proceedings with their alleged non-participation in resolving the common issues in the class proceeding ignores the underlying representative structure of a class proceeding. The purpose of ensuring that there is an adequate representative plaintiff is to ensure that the rights of each class member are protected and the claims of each are advanced vigorously.

[72] As stated in *Hollick*, at para. 15: "by distributing fixed litigation costs amongst a large number of class members, class actions improve access to justice by making economical the prosecution of claims that any one class member would find too costly to prosecute on his or her own". This economy is achieved, in part, by appointing a representative plaintiff who shares a sufficient common interest with other members of the class and by allowing the representative plaintiff, under court supervision, to conduct the litigation on behalf of class members. The notion of representation that is inherent in the procedural mechanism of a class proceeding is a very far cry from the complete absence of participation by investors in the OSC proceedings. The motion judge erred in dismissing this critical distinction as simply a "subjective and emotive plea" that has nothing to do with access to justice.

[73] Moreover, the above passage clearly reveals the motion judge's failure to properly consider the accessibility of the OSC proceedings insofar as the class members are concerned. To repeat, in his view, "the issue in this case is not whether the investors ... had or would have procedural fairness. The issue is whether they have had access to justice". Yet access to justice by the investors surely could not be achieved through the completion of a process that was not made accessible to them.

[74] By ignoring the essential differences between the scope of the OSC's jurisdiction and remedial powers and by treating as irrelevant the lack of participation in those proceedings by class members or their representatives, the motion judge viewed the OSC proceedings as if they were a reasonable alternative to a class proceeding. He then analyzed the motion before him as though the key issue were the propriety of the settlements attained through the s. 127 proceedings. Thereafter, he applied the settlement approval criteria under the *CPA* to the settlements flowing from the OSC proceedings as a basis for finding that those proceedings were a reasonable alternative to the proposed class proceeding. This circular analysis compounded the initial error in principle.

[75] The Divisional Court properly identified the motion judge's error in applying the test for approval of a settlement to the preferable procedure question under s. 5(1)(d) of the *CPA*. Molloy J. explained in detail, at paras. 48-57, why these criteria are not applicable at the certification stage. I would add that settlement criteria relative to a class action settlement cannot be applied to an OSC settlement for the simple reason that those

criteria are based on a certification order appointing a representative plaintiff to represent the absent class members. An OSC proceeding lacks this fundamental quality.

[76] However, at para. 44, Molloy J. made the observation: "There may even be situations where it would be appropriate to consider the appropriateness of a class action in light of a prior settlement that resulted in substantial compensation for the plaintiffs, even if not reaching 100 cents on the dollar." In my view, this observation reflects the same error that the motion judge committed. In order to assess if a settlement reached through an alternative procedure resulted in "substantial compensation" to the plaintiffs, it would be necessary to consider some of the same criteria that a court takes into account in deciding whether to approve a settlement, such as the likelihood of recovery, the recommendation and experience of counsel, and the future expense, likely duration of the litigation and risk. Yet, as Molloy J. explained, these criteria should not be applied when deciding the issue of preferable procedure.

[77] Moreover, because "substantial compensation" is a relative term, in order to determine if an amount was "substantial" it must be contextualized. This requires measuring the compensation awarded in the alternative forum against some other amount, such as the potential amount of damages available in the proposed class action lawsuit. However, at the certification stage, in most instances, no reliable yardstick is available because the amount recoverable in the proposed class proceeding would be as yet unknown. Put another way, the preferability analysis should not be reduced to an *ex post*

*facto* assessment of the adequacy of the award arrived at through the alternative procedure.

[78] An even more fundamental reason why the preferability analysis should not be conducted in this way is the fact that a certification motion is a procedural matter. It is not a determination of the merits of the dispute: see s. 5(5) of the *CPA*. An evaluation of the adequacy of a prior settlement as a basis for reaching a decision on preferability would require a determination that is tantamount to making a finding on the merits of the dispute. An evaluation of this sort would be a marked departure from the stipulation in *Hollick* that there need only be "some basis in fact" to ground the conclusion that a class proceeding is the preferable procedure. Indeed, as McLachlin C.J. stated in *Hollick* at para 16: "the certification stage is decidedly not meant to be a test of the merits of the action."

[79] In my view, as stated above, the preferable procedure inquiry must instead focus on the underlying purpose and nature of the alternative proceeding as compared with the class proceeding. The court must assess the capacity of the alternative procedure to adequately resolve the claims raised by the class members. The *CPA* mandates that this must be a procedural discussion. Hence the wording of the s. 5(1)(d), which provides "a class proceeding would be the preferable procedure for the resolution of the common issues".

## V. Conclusion

[80] In summary, the motion judge erred in principle by treating the negotiated payments that were made to investors in the OSC settlements as somehow eliminating the need to compare the purely regulatory function served by the OSC proceedings with the private remedial function to be played by the proposed class action. This fundamental error led the motion judge to wrongly dismiss as irrelevant important access to justice considerations, including that the OSC lacked the jurisdiction under its enabling provision of s. 127(1) of the *Securities Act* to decide the liability and damages issues raised in the private law action, as well as the consideration that the class members had no standing in the OSC proceedings and those proceedings were conducted behind closed doors.

[81] Had the motion judge taken these considerations into account in his preferability analysis, it is clear from the balance of his reasons that he would have granted the order to certify the class action. As he said, at para. 273, "had the action been the preferable procedure, the appropriate thing to do would have been to certify the class action conditionally on the court approving a revised litigation plan."

[82] Finally, I note that Molloy J. stated, at para. 58, that the motion judge "also erred by concluding that the test for preferable procedure could be met by a proceeding that had already been concluded. This was a fundamental error in principle." I do not agree

with Molloy J. on this point as a general proposition.[7] It seems to me that the analysis of whether an alternative proceeding is preferable to a class proceeding will depend on a thorough consideration of the central characteristics of the alternative proceeding, rather than on whether the other proceeding has concluded, is pending or remains ongoing.

## VI. Disposition

[83] For these reasons, I would dismiss the appeal from the Divisional Court's order granting certification of the proposed class action, on the condition that the motion judge approves a revised litigation plan.

[84] The parties may make written submissions on costs to be delivered within 10 days of the release of these reasons.

RELEASED: January 27, 2012

"W.K. Winkler C.J.O."

"WKW" "I agree G.J. Epstein J.A."

"I agree G. Pardu J. *(ad hoc)*"

[7] As Molloy J. herself went on to note, at para. 59, she did "not wish to be taken as having ruled that the existence of a past settlement or a concluded proceeding relating to the same claims can never be taken into account at the certification stage."