CITATION: McDonald v. Home Capital Group, 2017 ONSC 5004
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2017 ONSC 5004 (CanLII)

SUPERIOR COURT OF JUSTICE - ONTARIO

RE: Claire R. McDonald (Plaintiff)

AND:

Home Capital Group Inc., Gerald M. Soloway,

Robert Morton and Robert J Blowes (Defendants)

BEFORE: Justice R. Raikes

COUNSEL: Michael Robb and Douglas Worndl, for the plaintiffs
Peter Howard and Samaneh Hosseini, for the defendant, Home Capital Group Inc.
James Douglas, for the defendants, Morton and Blowes
Niklas Holmberg, for the defendant, Soloway

HEARD: August 21, 2017

ENDORSEMENT

[1] The plaintiff moves for an order approving the terms of the proposed settlement of this class proceeding, the Distribution Protocol, the Notice Plan, short and long form notices to the Class and the Claim Form. The plaintiff also seeks ancillary relief related to the approvals. I will deal with approval of class counsel fees and disbursements in a separate endorsement.

[2] This motion came before me on August 21, 2017. I endorsed that I approve the settlement pursuant to s. 29(2) of the *Class Proceedings Act,* 1992, S.O. 1992, c. 6 ("*CPA*") subject to certain changes to the draft order provided by counsel at the hearing, with reasons to follow. These are those reasons.

[3] This action was commenced by Notice of Action issued February 13, 2017. The Statement of Claim was issued February 24, 2017.

[4] The plaintiff Class is comprised of persons who acquired common shares of Home Capital Group Inc. ("Home Capital") between November 5, 2014 and the close of trading on the Toronto Stock Exchange on July 10, 2015. The plaintiff alleges that misrepresentations were contained in documents released by Home Capital pursuant to its statutory continuous disclosure obligations and in oral public statements made by Home Capital's CEO and CFO. Home Capital failed to disclose irregularities in its mortgage

origination practices. The failure to disclose the irregularities caused Home Capital's share values to remain artificially high until disclosure was made on July 10, 2015.

[5] On April 19, 2017, the Ontario Securities Commission ("OSC") filed a Statement of Allegations against the defendants (except Mr. Blowes). The allegations in the OSC proceeding were similar to those asserted in this action.

[6] On June 14, 2017, the parties reached agreement to settle the action following several days of arm's length negotiations with the assistance of a mediator, the Honourable Warren Winkler Q.C. Counsel then prepared a Settlement Agreement dated June 22, 2017. The settlement negotiated with the mediator resolved both the OSC proceeding and this action subject to approval of both the OSC and this Court.

[7] On consent, the action was certified for settlement approval purposes on June 28, 2017. RicePoint Administration Inc. ("RicePoint") was appointed Administrator for the purpose of implementing the first phase of the Notice Plan pursuant to which it provided notice of certification and how to opt out, and of the motion for settlement approval and how to object.

[8] Five shareholders opted out of the Class. The number of shares affected by the opt-outs falls below the threshold in the Settlement Agreement that would permit the defendant, Home Capital, to terminate the agreement.

[9] No one provided written notice of objection, nor did anyone attend the settlement approval hearing to object in person to the terms of the settlement.

[10] On August 9, 2017, the OSC approval hearing was held in Toronto. The panel approved the terms of the settlement of the OSC proceeding subject to approval of the settlement of the class proceeding.

[11] The principal terms of the settlement are:

a. the defendants will pay the sum of $29.5 million in settlement of both the class proceeding and OSC proceeding ($11 million for the OSC proceeding) for the benefit of the class members;

b. the settlement funds will be used to pay class counsel costs, the Administrator's costs and the balance will be distributed among class members who apply pursuant to the Distribution Protocol;

c. the defendants do not admit liability;

d. the action as against the defendants is dismissed; and

e. the plaintiff Class, excepting those who opted out, release the defendants from the claims asserted in the action.

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[12] The test for approval of a settlement of a class proceeding is whether the settlement is fair, reasonable and in the best interests of the class. Section 138.10 of the Ontario *Securities Act*, R.S.O. 1990, c. S.5 ("*OSA*") requires that an action under s. 138.3 may only be settled with approval of the court. The *OSA* does not specify the test for court approval; however, where the claim advanced is on behalf of a class of shareholders, the test of "fair, reasonable and in the best interests" meets the underlying policy objectives in s. 138.3 of the *OSA*. For greater certainty, I find that the test applicable under s. 138.10 is the same as that required for approval of a settlement of a class proceeding.

[13] On a motion for approval of a settlement of a class proceeding, the court must consider:

a. whether there are any indicators of collusion or conflicts of interest in the settlement or the process leading to the settlement that might call into question its fairness; and

b. whether the compromise embodied by the settlement falls within the range of reasonableness in the particular circumstances of the case.

[14] In this case, there are no indicators of collusion or conflicts of interest. The parties were represented by experienced counsel who engaged in arm's-length negotiations with the assistance of the pre-eminent class actions mediator. The mediation took six days of which part addressed resolution of the OSC proceeding. The OSC were separately represented.

[15] The early negotiation and resolution of this action and the companion OSC proceeding is unusual but does not give rise to any concerns of collusion. The commencement of the class proceeding and the OSC proceeding had immediate and significant business implications for the defendant, Home Capital. Its share value declined. Its liquidity was imperilled which necessitated urgent financing at less than optimal terms that were not sustainable in the long term. There was a material risk to the Class that Home Capital would be unable to continue its operations as a going concern.

[16] Home Capital had layers of insurance which, arguably, could respond to the plaintiff's claim. However, those policies declined as legal costs were incurred to defend each of the class proceeding and OSC proceeding. In short, there would be ever reducing insurance available to satisfy a successful claim the longer the litigation went on.

[17] In addition, despite the potentially helpful presence of the OSC proceeding and the allegations therein, the plaintiffs claim in this action was not without risk for all or part of the claim period. Complex litigation is not without peril.

[18] It is to the parties' credit that rather than rushing headlong into the early skirmishes common in litigation, common sense prevailed leading to meaningful discussion and an early resolution took place. That is the context within which the negotiations and settlement arose. Far from raising eyebrows that suggest a quick and convenient agreement, the circumstances here evidence reasoned, hard-fought negotiation with a measure of compromise on both sides.

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[19] Both the plaintiff and defendants engaged experts to quantify damages. There were defences available to the defendants which had the potential to defeat the plaintiff's claim for all or part of the claim period. The range of potential damages varied dramatically depending upon assumptions about whether and to what extent the defendants' liability defences applied. It is to be noted that the defendants denied any liability and continue to do so.

[20] The preliminary range of damages estimated by the plaintiff's expert was $36.8 million to $139.6 million. That range is so broad because it encompasses three different reporting periods and, therefore, three sets of disclosure documents. If the matter went to trial, each set of disclosure documents would have to be assessed to determine whether there was a misrepresentation. A court could well find that any or all of the disclosure documents was satisfactory; i.e. there was no misrepresentation.

[21] The defendants' expert estimated damages between $3.207 million and $91 million depending on the assumptions made. Of course, if the defendants were entirely successful on liability, there would be no damages.

[22] Thus, the settlement amount of $29.5 million represents a compromise between the parties that recognizes the divergence of possible results, the risk of success or failure at trial, and the ever present business risks that militated in favour of an early resolution.

[23] The mediation discussed above included mediation as between the various insurers whose compromise was necessary to resolve and fund the settlement. Their interests and their willingness to defend their insured adds a degree of complexity and risk.

[24] The quid pro quo for the substantial payment of $29.5 million is dismissal of the action and a release of the defendants by class members of the claims asserted in the statement of claim. These terms are standard terms found in any settlement. No sane defendant would pay out money without the certainty and closure that a dismissal and release provides.

[25] I am satisfied that the settlement amount of $29.5 million is a fair and reasonable compromise of the litigation interests of the plaintiff Class having regard to the risks of success in the action and ultimate recovery. It is not possible at this stage to be able to determine with accuracy what any individual class member will recover. There are simply too many variables including, but not limited to, the price paid for each share, the amount which they received on sale, and the aggregate number of shares in the take up of the settlement.

[26] I find that the settlement is in the best interests of the Class. Suffice to say, the settlement amount provides a significant pool of money that will provide a material contribution to the losses allegedly sustained. It is extremely unlikely that any but a very few of the shareholders could have or would have pursued individual litigation but for the class proceeding. The settlement eliminates risks to recovery and provides an immediate and substantial benefit to class members in exchange for the release of their claims.

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[27] I turn now to the Distribution Protocol. The proposed Distribution Protocol and a Guide have been posted on class counsel's website since June 29, 2017. Those documents have also been posted to the case dedicated website created by the Administrator, RicePoint.

[28] The Protocol sets out the process for class members to have their respective compensation entitlements determined. It uses a damage calculation formula which I am advised is analogous to the formulae set out in s. 138.5 of the *OSA*. The approach taken is consistent with that taken in other distribution protocols in security class actions approved by the Court and with the plaintiff's damages theory.

[29] The steps to calculate a class member's compensation are set out at paras. 7-12 and 27 of the Protocol and are explained in simple language in the Guide. In addition, I have directed that class counsel and the Administrator post on their respective websites a copy of a completed Claim Form as an aid to class members.

[30] The distribution protocol takes into account,

a. the date on which the common shares were acquired by the class member;

b. the date on which the common shares were disposed of, if at all, by the class member; and

c. the difference between the amount paid by the class member to acquire the shares and the total proceeds paid to class members for the sale of the shares.

[31] The Administrator is required to apply a "first in first out" methodology to all purchases of common shares by the class members. Class members who held Home Capital shares at the commencement of the class period must have completely sold those shares before shares acquired in the class period are considered sold.

[32] The Administrator then calculates the class members share of the net settlement funds by incorporating the date the shares were purchased and sold, as well as the risk of values assigned to those shares. That gives rise to a notional entitlement which will determine the class member's pro rata share of the net settlement funds.

[33] The Protocol applies a risk factor based on when shares were purchased. Claims based on shares purchased from and after November 4, 2014 but before May 6, 2015 are discounted by one-third. Claims based on shares purchased on or after May 6, 2015 are not discounted.

[34] May 6, 2015 is the date on which Home Capital's first quarter 2015 interim financial statements were issued. Class members who purchased shares on or after that date have a lower litigation risk than those who purchased earlier. For that reason, a discount of one-third is applied to the earlier shares. In my view, the discount represents a fair and reasonable allocation of the risk of the litigation and benefit of the settlement.

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[35] Finally, I note that none of the settlement proceeds will revert to the defendant or to class counsel. If the amount left over after distribution is $25,000 or less, that amount will be paid to the OSC. That sum is simply too small to parse out among the many class members. The cost to do so would likely exceed that amount.

[36] Paragraph 30 of the draft Distribution Protocol gave authority to the Administrator and class counsel to extend the "claims bar deadline"; that is, the deadline by which claims must be submitted to the Administrator. However, the power to extend was limited to that deadline.

[37] The Distribution Protocol provides a mechanism by which the Administrator may notify a class member that the Claim Form has not been properly submitted. There may be information missing or documentation required that has not been provided. The draft Distribution Protocol contemplated that once the Administrator sent out notice of the deficiency, the class member had 21 days to rectify the deficiency failing which his or her claim was barred. That time period is simply too short.

[38] I discussed with counsel and all counsel agreed that that time period should be extended to 45 days, and class counsel and the Administrator should have the ability to extend any deadline if, in doing so, it will not adversely affect the efficient administration of the settlement and is in the best interests of the class to do so. In my view, such flexibility is essential. There could be a myriad of good reasons why someone is unable to respond even in 45 days. Thus, it is expected that the Administrator and class counsel will exercise this flexibility in a generous and fair manner.

[39] I turn now to the Notice Plan and administration proposal. The plaintiff proposes that RicePoint effect the second notice to the class which sets out the Court's approval and how to go about making a claim, and act as the Administrator of the settlement funds. Class counsel has used RicePoint previously in similar settlements without issue.

[40] I am satisfied that RicePoint has the appropriate skill and experience to carry out its mandate as Administrator. The estimated costs for their efforts are reasonable having regard to the requirements of the notice program, and the anticipated number of potential claimants and claim process.

[41] There were some slight modifications required to the form of the second notice, the Claim Form and the draft order provided which do not bear discussion in these reasons. It is sufficient to indicate that these matters were fully discussed with counsel who agreed to provide a further revised draft order with the modifications to the notice and Claim Form. I have since received that order and have carefully reviewed it. It includes the various changes discussed and is acceptable.

[42] I will not set out the terms of the order in these reasons. It is quite lengthy with various attachments. The order with attachments is available through the Court and will be on class counsel's website and that of the Administrator.

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[43] In summary, I have approved the settlement of the class proceeding, the Distribution Protocol, Notice Plan, Claim Form and notice to the Class. I have also appointed RicePoint as Administrator to implement the settlement and Notice Plan.

"Justice R. Raikes"
Justice R. Raikes

Date: August 23, 2017

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