SUPERIOR COURT OF JUSTICE

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RE: IRONWORKERS ONTARION PENSION FUNE ET AL. v. MANULIFE FINANCIAL CORPORATION, ET AL.
COURT FILE NO.: CV-09-383998-CP

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Thank you.

CITATION: Ironworkers Ontario Pension Fund v. Manulife Financial 2017 ONSC 2669
COURT FILE NO.: CV-09-383998-CP
DATE: 20170508

SUPERIOR COURT OF JUSTICE - ONTARIO

RE: IRONWORKERS ONTARIO PENSION FUND and LEONARD SCHWARTZ, Plaintiffs

AND:

MANULIFE FINANCIAL CORPORATION, DOMINIC D'ALESSANDRO and PETER RUBENOVITCH, Defendants

Proceeding under the *Class Proceedings Act, 1992*

BEFORE: Justice Edward P. Belobaba

COUNSEL: *Daniel Bach, Michael Wright* and *Alex Dimson* for the Plaintiffs

Patricia D. S. Jackson for Manulife Financial Corporation

HEARD: April 28, 2017

CLASS ACTION SETTLEMENT AND RELATED APPROVALS

[1] After almost eight years of litigation, this securities class action against the country's largest life insurance company has settled for $69 million.

[2] The plaintiffs bring three motions seeking judicial approval of (i) the settlement, the plan of allocation and the payment of honoraria to the representative plaintiffs; (ii) the payment of class counsel contingency-based legal fees; and (iii) the payment of a preliminary commission to a third-party litigation funder.

[3] This is a settlement of the Ontario Action commenced in 2009, with leave and certification granted in 2013,[1] and the Quebec Action also commenced in 2009, with authorization to proceed granted in 2011.[2] These are parallel class proceedings that have been brought on behalf of current and former shareholders of Manulife Financial Corporation ("MFC") in Ontario and Quebec and have been prosecuted in tandem.

[4] The actions were settled in December, 2016 after several mediations just as a summary judgment motion was being scheduled in the Ontario Action and a few months before the trial was to start in the Quebec Action. This was a "late stage" settlement. In a late stage settlement, the supervising class action judge will be justified in assuming that class counsel had a complete or almost complete understanding of the risks and rewards of further litigation and will be more comfortable relying on class counsel's recommendation that the settlement is indeed fair and reasonable and in the best interests of the class.

[5] For the reasons set out below, the $69 million settlement is approved, as is the plan of allocation, the payment of honoraria to the representative plaintiffs, the payment of class counsel contingency-based legal fees, and the payment of a preliminary commission to a third-party litigation funder.

Background

[6] The background facts were set out in my leave and certification decision[3] and can be briefly summarized as follows. Manulife Financial Corporation ("MFC") is the largest life insurance company in Canada. In early 2004, MFC added several new guaranteed investment products ("the Guaranteed Products") to its segregated funds line-up. Unlike with the older variable annuity products, MFC decided that the new products would not be hedged or reinsured. The risk of fluctuations in the equity market and in generating the money needed to provide the promised return on the Guaranteed Products would be fully borne by MFC itself.

[7] The new Guaranteed Products line was a success. MFC proceeded to grow the business from about $71 billion in early 2004 to about $165 billion by year-end 2008. But all or almost all of it was unhedged and uninsured. When the full force of the global financial crisis hit in the fall of 2008 and the Canadian and American equity markets fell by more than 35%, MFC found itself badly overexposed.

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[1] *Dugal v. Manulife Financial*, 2013 ONSC 4083.

[2] *Lamoureux v Société Financière Manuvie*, (Case no. 200-06-000117-096, July 8, 2011).

[3] *Dugal, supra*, note, 1 at paras. 6 -14.

[8] On February 12, 2009 MFC released its annual financial statements for year-end 2008. The financial statements noted that over the year, corporate profits had fallen by almost $3.8 billion (almost $2 billion of this was attributed to the Guaranteed Products line) and earnings per share had dropped from $2.78 just one year earlier to 32 cents. The financial statements also made clear that the company had to increase its reserves by more than ten times, from $526 million at year-end 2007 to $5.783 billion at year-end 2008, because of its unhedged exposure to the equity market. Noting these losses and the fact that "unlike most of the other large writers of variable annuities and segregated funds in North America, [MFC] has not implemented a comprehensive equity hedging program," Moody's placed MFC's ratings on review for a possible downgrade.

[9] The market reacted immediately. The MFC share price dropped 6% on February 12 on heavy trading volume. Over the next ten days the share price dropped another 37%. By the end of the first quarter of 2009, the shares were trading at $8.92, down from $38.28 just six months earlier—a drop of almost 77%.

[10] The Ontario and Quebec Actions followed soon thereafter. A class action was also commenced by MFC shareholders in the U.S.[4]

(1) Settlement and plan of allocation approval

[11] Section 29(2) of the *Class Proceedings Act*[5] requires the court to approve the class action settlement before it can take effect. The judge must be satisfied that the proposed settlement is fair and reasonable and in the best interests of the class.[6]

[12] The vast majority of class action settlements materialize just before or just after certification. In most of the cases, documents have not been exchanged, discoveries have not taken place and class counsel's knowledge level about the risks and rewards of further litigation is, to say the least, at a minimum. In such early stage settlements, most judges, myself included, need to be satisfied that the settlement falls within "a zone of reasonableness."[7]

[13] As already noted, this was not an early stage settlement. Quite the contrary. Statements of defence were filed; there was extensive production and review of more

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[4] *In Re Manulife Financial Corporation Securities Litigation*, 09 Civ. 6185 (JFK) (S.D.N.Y., May 23, 2011).)

[5] *Class Proceedings Act, 1992*, S.O. 1992, c. 6.

[6] *Dobbs v. Sun Life Assurance*, (1998) 40 O.R. (3d) 429 (Gen. Div.), aff'd (1998) 41 O.R. (3d) 97 (C.A.), leave to appeal to S.C.C. refused Oct. 22, 1998.

[7] Discussed more fully in *Clegg v. HMQ Ontario*, 2016 ONSC 2662, at paras. 26-36.

than 300,000 documents; discoveries of numerous witnesses were conducted over some ten days; the key issues were analyzed in more than a dozen expert reports; the litigation progressed through several court decisions both here and in Quebec, and there were a number of confidential mediation sessions.

[14] In a late-stage settlement such as the one here, I am prepared to accept that class counsel was well informed about the risks and rewards of further litigation when the settlement was reached and that the settlement was indeed in the best interests of the class.

[15] The various litigation risks and legal impediments that could have resulted in the action being dismissed were legitimately identified by class counsel as follows:

- *No misrepresentations.* There was compelling evidence that MFC's lack of hedging was fully understood by market analysts. In various conference calls, MFC disclosed that the company had no hedging program and retained most of the risk associated with the variable annuity products. Moody's wrote that MFC "foregoes a hedging program on the view that value-added from hedging in the long-term does not justify the costs," and Standard and Poor's explained that one of MFC's weaknesses was that the company's "[v]ariable annuities book since 2004 remains largely unhedged."

- *Reasonable investigation defence.* There was compelling evidence that MFC's risk management practices had been reviewed by Deloitte, Oliver Wyman, Moody's, Standard & Poor's, Towers Perrin Tillinghast, and PricewaterhouseCoopers, all of whom determined that the risk management practices were broadly consistent with industry practice.

- *No correction.* The defendants deny that a corrective disclosure occurred on February 12, 2009. The information released on this date, they say, was incremental to the information provided in a previous disclosure in December, 2008, when MFC revealed information about the company's expected loss for fiscal 2008 and disclosed that they would increase their Guaranteed Products related reserves to approximately $5 billion by year-end (the actual amount of the increase disclosed on February 12 was $5.783 billion). The defendants say that the information released on February 12, 2009 was "stale" and irrelevant in an efficient market and was certainly no "correction."

- *Economic crisis.* The pleaded correction occurred in the midst of an economic crisis. The defendants' event study arguably shows that after controlling for market and industry-wide factors, MFC's "excess return" (the portion of the stock's return that can be attributed to MFC-specific information) on the date of the alleged correction was statistically insignificant. The defendants take the

position that it was this once-in-a-lifetime collapse of the global financial system and not any company-specific issue that caused MFC's losses.

- *The failed U.S. action.* The U.S. class action, based on substantially the same allegations as those made herein, was dismissed. The American judge found that the misrepresentations alleged by the plaintiffs amounted to "fraud-by-hindsight,"[8] that MFC did not attempt to conceal their exposure to market changes,[9] and that "[MFC] clearly disclosed the risks of an equity market downturn to its investors."[10] The American judge also found that the so-called correction on February 12, 2009 simply "confirmed many of the negative forecasts [MFC] made in early December 2008."[11]

- *Challenges in the Quebec Action.* The action in Quebec was met with similar judicial skepticism. The Quebec judge indicated that it was unlikely MFC breached its disclosure obligations and that the alleged misrepresentations or omissions "depend… on conclusions drawn *a posteriori*, obviously resulting from the stock market crash that began in 2008."[12] The fact that the Quebec judge's remarks echoed what was said by the American judge was obviously a source of concern for class counsel.

- *OSC investigation.* As was the fact that after issuing an enforcement notice, the Ontario Securities Commission decided not to pursue the matter further and declined to seek any order.

[16] In sum, class counsel was well informed about the risks and rewards of further litigation. I can comfortably accept class counsel's assessment of these risks and their recommendation that the $69 million settlement be approved.

[17] I find the settlement to be fair and reasonable and in the best interests of the class. The settlement is approved.

[18] The proposed Plan of Allocation, designed to provide a fair, streamlined and efficient claims and compensation process, is also approved.

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[8] *Ibid.*, at 30.

[9] *Ibid.*, at 32.

[10] *Ibid.*, at 35.

[11] *Ibid.*, at 20.

[12] *Supra,* note 2, at para. 81.

(2) Honoraria to representative plaintiffs

[19] Class counsel requests that a $10,000 honorarium be paid to each of the two representative plaintiffs. I am satisfied that such a payment should be made.

[20] Both Ironworkers and Mr. Schwartz and have devoted more than seven years to this litigation and played a key role throughout the prosecution of the Ontario Action. They provided affidavits and were cross-examined and they participated in the approval of the litigation funding agreement, the execution of the tolling agreement, the several mediations and the final settlement negotiations – instructing counsel throughout. In short, they represented the interests of the class members with impressive dedication and diligence.

[21] Class counsel suggests that the $20,000 honoraria be paid out of its fees. The better practice, in my view, is for honoraria be paid out of the settlement amount. As the Court of Appeal noted in *Smith Estate v. National Money Mart*[13]:

> As a general matter the representative plaintiff's fee should be paid out of the settlement fund and not out of class counsel fees. Class counsel fees are predicated on the work that class counsel have done for the class. Allocating a part of that fee to a layperson, especially a representative plaintiff, raises the spectre of fee splitting ...[14]

[22] The payment of a $10,000 honorarium to each of the two representative plaintiffs is approved – such payment to be drawn from the settlement fund.

(3) Legal fees approval

[23] As set out in the retainer agreements with the representative plaintiffs, class counsel seeks a 22.5 per cent contingency fee plus disbursements and taxes. For the purposes of the fee approval motion, which applies to the counsel fees payable in the Ontario Action, class counsel in the two actions have notionally allocated 92% of the settlement amount (which now includes some $91,495.90 in interest) to the Ontario class members and 8 per cent to the Quebec class members. This allocation will only be used to provide an amount against which the fee requests may be calculated. The notional

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[13] *Smith Estate v. National Money Mart Company*, 2011 ONCA 233.

[63]*Ibid.,* at para. 135. The same point (that honoraria should be paid out of the settlement fund and not out of class counsel's fees) is also made in Morabito, "Additional Compensation to Representative Plaintiffs in Ontario: Conceptual, Empirical and Comparative Perspectives," (2014) Queen's L.J. 341.

allocation will not affect the distribution of the settlement among class members which will be determined by the Plan of Allocation.

[24] As I explained in *Cannon*[15] and again in *Middlemiss v. Penn West Petroleum*,[16] I am prepared to accord presumptive validity to a properly executed contingency fee arrangement such as the one that is before me. It is only through a robust contingency compensation system that class counsel will be appropriately rewarded for the wins and losses over many files and many years of litigation and that the class action will continue to remain viable as a meaningful vehicle for access to justice.[17]

[25] The representative plaintiffs support class counsel's fee request and no class members have filed objections. Class counsel in the Ontario Action is entitled to receive 22.5 percent of 92 per cent of the $69 million recovery (plus $91,496 in interest) which amounts to just over $14.3 million in fees. Class counsel is also entitled to disbursements[18] and taxes. The legal fees request is approved.

(4) Preliminary commission to CFI

[26] The plaintiffs entered into a funding agreement with litigation funder CFI whereby CFI would pay any adverse cost award in return for a commission of 7% of any settlement or judgment, subject to a cap of $5 million. CFI secured its costs exposure by depositing letters of credit with the accountant of this court.

[27] The plaintiffs ask that the letters of credit be released and a preliminary commission of $1,711,540.09 be paid to CFI in accordance with the terms of the funding agreement, which was previously approved by this court and which requires payment "as soon as practicable" and "in any event prior to the distribution of funds to class members."

[28] I have no difficulty approving these requests.

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[15] *Cannon v. Funds for Canada Foundation,* 2013 ONSC 7686.

[16] *Middlemiss v. Penn West Petroleum,* 2016 ONSC 3537.

[17] *Ibid.,* at para. 19. Also see *Ramdath v. George Brown College of Applied Arts and Technology,* 2016 ONSC 3536, at note 14: "Over a period of years, plaintiff-side class action firms will win cases and lose cases. The "risk" that contingency lawyers face cannot be assessed case-by-case or one-off, but must be measured across a great many files. A "large" contingency recovery in one case will offset the loss or losses in other cases. That is why the "multiplier" approach that purports to assess risk by considering only the case that is currently before the court is fundamentally flawed, indeed unprincipled."

[18] The disbursements were just over $2.3 million largely because of the more than $1.9 million that was paid for the preparation of numerous expert reports.

Disposition

[29] Orders to go approving the $69 million settlement, the proposed Plan of Allocation, the payment of a $10,000 honorarium to each of the two representative plaintiffs, the payment of class counsel legal fees based on the 22.5 per cent contingency agreement, plus disbursements and taxes, and the payment of a preliminary commission to CFI.

[30] My congratulations to counsel on both sides in achieving what in my view is a fair and reasonable resolution.

Justice Edward P. Belobaba

Date: May 8, 2017