CITATION: Zaniewicz v. Zungui Haixi Corporation, 2013 ONSC 5490
COURT FILE NO.: 11-CV-436360-00CP
DATE: August 27, 2013

ONTARIO
SUPERIOR COURT OF JUSTICE

BETWEEN:	
JERZY ROBERT ZANIEWICZ and EDWARD C. CLARKE Plaintiffs	*Charles M. Wright* and *Douglas M. Worndl* for the Plaintiffs
– and –	
ZUNGUI HAIXI CORPORATION, E&Y, FENGYI CAI, JIXU CAI, YANDA CAI, MICHELLE GOBIN, MICHAEL W. MANLEY, PATRICK A. RYAN, ELLIOTT WAHLE, MARGARET CORNISH, CIBC WORLD MARKETS INC., CANACCORD GENUITY CORP. (f.k.a. CANACCORD FINANCIAL LTD)., GMP SECURITIES LP and MACKIE RESEARCH CAPITAL CORPORATION (f.k.a. RESEARCH CAPITAL CORPORATION) Defendants	*Deborah Berlach* for the Defendant Zungui Haizi Corporation *Margaret L. Waddell* for the Defendant Michelle Gobin *Michael A. Eizenga* for the Defendant Michael W. Manley *James S.F. Wilson* for the Defendants, Patrick A. Ryan, Elliott Wahle, and Margaret Cornish *Linda L. Fuerst* for the Defendant Ernst &Young LLP. *Kent Thomson* and *Derek Ricci* for the Defendants CIBC World Markets Inc., Canaccord Genuity Corp. (f.k.a. Canaccord Financial Ltd.) and Mackie Research Capital Corporation (f.k.a. Research Capital Corporation and GMP Securities LP.
Proceeding under the *Class Proceedings Act*	**HEARD:** August 27, 2013

PERELL, J.

REASONS FOR DECISION

A. INTRODUCTION AND OVERVIEW

[1] This is a securities class action under the *Class Proceedings Act, 1992*, S.O. 1992, c. 6 and the Ontario *Securities Act,* R.S.O. 1990, c. S.5. The Plaintiffs Jerzy Robert Zaniewicz and Edward C. Clarke advance common law tort claims and also statutory claims with respect to the sale of the shares of Zungui Haizi Corporation in the primary and secondary markets.

[2] The Plaintiffs bring this motion for: (a) certification for settlement purposes as against the Defendants CIBC World Markets Inc., Canaccord Genuity Corp., GMP Securities LP, and Mackie Research Capital Corporation (the "Underwriting Syndicate"); (b) approval of three settlements; (c) ancillary orders, including the appointment of an administrator; (d) approval of the notice program; and (e) approval of the plan of distribution (the "Plan of Allocation") for the settlement funds.

[3] Class Counsel also bring a motion for approval of its counsel fees and disbursements. Class Counsel seeks $2,250,000.00, plus disbursements, interest on disbursements, and applicable taxes. The total request is for $2,807,037.56.

[4] For the reasons that follow, I certify the action as against the Underwriting Syndicate for settlement purposes. I approve the three settlements and Class Counsel's request for counsel fees. I approve the requests for ancillary orders. However, I do not approve the proposed Plan of Allocation, and, rather, I have varied the plan and approved a modified Plan of Allocation.

[5] As I will explain, in this case, the court has the jurisdiction to approve the settlement agreements and then establish a plan of distribution that is different than the plan of distribution proposed by the parties.

B. FACTUAL BACKGROUND TO THE CLASS ACTION

[6] See *Zaniewicz v. Zungui Haixi Corp.*, 2013 ONSC 2959, which sets out most of the factual background and the procedural history. See also: *Zaniewicz v. Zungui Haixi Corp.*, *Zaniewicz v. Zungui Haixi Corp.*, 2012 ONSC 4842, *Zaniewicz v. Zungui Haixi Corp.*, 2012 ONSC 4904, and *Zaniewicz v. Zungui Haixi Corp.*, 2012 ONSC 6061.

[7] In December 2009, Zungui made an initial public offering ("IPO"), and it raised approximately $40 million in Ontario's capital markets.

[8] Zungui and its directors and officers had a statutory obligation under the Ontario *Securities Act* to provide Zungui's investors with timely and accurate disclosure regarding the business of Zungui, including disclosure in Zungui's interim and annual financial statements.

[9] In its interim and annual financial statements, Zungui and the Defendants Yanda, Fengyi, and Zungui Cai (the "Cai Brothers") assured investors that Zungui's financial statements presented fairly, in all material respects, the financial position of Zungui in accordance with GAAP. They represented that the Zungui's offering documents contained full true and plain disclosure of all material facts relating to the offering of securities.

[10] The Plaintiffs are residents of Ontario. Each purchased common shares of Zungui in the primary market. Mr. Clarke also purchased common shares of Zungui in the secondary market.

[11] On August 22, 2011, Zungui issued a press release announcing that its auditor, Ernst & Young LLP ("E&Y"), had suspended its audit of Zungui's financial statements for the year ended June 30, 2011. With that announcement, Zungui's shares immediately lost 77% of their value. Subsequently, Zungui's shares became the subject of various temporary and permanent cease trade orders, and they are now worthless.

[12] On September 22, 2011, Zungui's Chief Financial Officer and all independent members of the Board resigned, in part, because the special committee formed to investigate E&Y's concerns had been prevented from fulfilling its mandate.

[13] On September 23, 2011, E&Y resigned as Zungui's auditor. E&Y withdrew its opinions that Zungui's financial statements were GAAP compliant.

[14] On February 2, 2012, the Ontario Securities Commission ("OSC") ruled that Yanda, Fengyi, and Zungui Cai had engaged in conduct contrary to the public interest, and on August 28, 2012, the OSC ordered, among other things, that Yanda and Fengyi resign as directors or officers of Zungui and be permanently prohibited from acting as directors or officers of any issuer.

[15] The OSC investigation revealed that when E&Y resigned, it advised that all of its audit opinions that formed part of the IPO Prospectus, as well as Zungui's June 2010 financial statements could no longer be relied upon.

[16] On October 3, 2011, Mr. Zaniewicz, commenced the action by the issuance of a Notice of Action. On November 2, 2011, he filed his Statement of Claim. On February 7, 2012 and February 10, 2012, I made orders granting leave to amend the Statement of Claim to add Mr. Clarke as a plaintiff and to correct the description of two of the Underwriters incorrectly described in the style of cause.

[17] On February 8, 2012, the Plaintiffs filed their Fresh as Amended Statement of Claim.

[18] In the action, the Plaintiffs sue not only Zungui and the Cai Brothers, but others allegedly responsible for ensuring that Zungui's public disclosure to primary and secondary market investors was timely and accurate in accordance with securities law. The Plaintiffs allege various statutory claims under the Ontario *Securities Act* and also common law claims.

[19] The Plaintiffs allege that Zungui's IPO Prospectus was misleading as it contained material misrepresentations. The Plaintiffs allege that the representations were materially false, and Zungui's financial statements contained in the prospectus, and other financial statements later prepared and disseminated in the secondary securities market, were neither accurate nor reliable in respect of reported revenues, net income, assets, and shareholders' equity. Moreover, the Plaintiffs allege that the financial statements did not fairly present, in all material respects, the financial condition, results of operations and cash flows of Zungui for the reporting periods presented.

[20] Alan Mak, who is a chartered accountant, a member of the Institute of Chartered Accountants of Ontario, and a member of the Association of Certified Fraud Examiners opined that the audits conducted by Ernst & Young were not in accordance with GAAP and that Ernst & Young's unqualified audit opinions should not have been given for the 2006 through 2010 reporting periods. E&Y does not admit that it was negligent.

[21] In the class action, the Class Definition is as follows:

> All persons or entities wherever they may reside or be domiciled, other than Excluded Persons and Opt-Out Parties, who acquired Eligible Shares.
>
> Eligible Shares means the Shares acquired by a Class Member or Opt-Out Party during the Class Period.
>
> Class Period means the period from and including August 11, 2009 to and including August 22, 2011.
>
> Excluded Persons means each Defendant, the past or present subsidiaries or affiliates, officers, directors, partners, legal representatives, consultants, agents, successors and assigns of Zungui and any member of each Defendant's families, their heirs, successors or assigns, and includes any Southern Zungui Acquirers who acted as a consultant or provided other professional services to Zungui or its subsidiaries in connection with the IPO.

[22] The Class is comprised of three (3) types of acquirers of Zungui common shares: (1) primary market purchasers; (2) secondary market purchasers; and (3) share exchange acquirors (i.e. anyone who was a shareholder of Zungui's subsidiary, Southern Trends International Holding Company (BVI), who entered into an agreement with Zungui, before its IPO, to exchange their Southern Trends shares for Zungui common shares on a basis of 1:5,000.

[23] Paul Mulholland, a US based certified forensic accountant, was retained by the Plaintiffs, to among other things, calculate the damages of class members. Mr. Mulholland's estimate of damages was $23.76 million comprised of: (a) $10.1 million in damage to primary market purchasers; $12.9 million in damage to secondary market Purchasers; and $0.7 million in damage to share exchange acquirors. (The original Statement of Claim sought damages of $30 million.)

[24] The Defendants, of course, do not admit liability or the amount of the Class Member's alleged losses.

C. CERTIFICATION FOR SETTLEMENT PURPOSES

[25] I have already certified this action for settlement purposes as against Zungui, Michelle Gobin, Michael W. Manley, Patrick A. Ryan, Elliott Wahle, and Margaret Cornish (the "Zungui Defendants") and against Ernst & Young LLP and the Cai Brothers.

[26] I am satisfied that that action should now be certified for settlement purposes as against the Underwriting Syndicate, and an Order should issue accordingly.

D. SETTLEMENT APPROVAL

[27] The Plaintiffs have concluded three settlements: (1) the Auditor Settlement; (2) the Zungui Settlement; and (3) Underwriter Settlement.

[28] The Auditor Settlement is for $2 million. The Zungui Settlement is for $8 million, and the Underwriter Settlement is for $750,000.00.

[29] The Zungui Defendants have agreed to contribute an additional $100,000.00 if the Plaintiffs: (a) settled their claims against the Underwriting Syndicate before the scheduled settlement approval hearings for the Auditor Settlement and the Zungui Settlement; and (b) obtained the Court's approval of a settlement with the Underwriting Syndicate. Thus, if all the settlements are approved, the settlement funds will total $10,850,000.00 plus interest before deductions for counsel fee and administrative expenses.

[30] The settlement funds under the Auditor Settlement were received on May 17, 2013, and have been accruing interest since that date. The settlement funds under the Zungui Settlement were received on May 24, 2013, and have been accruing interest since February 22, 2013. The settlement funds under the Underwriter Settlement will be paid within fourteen days of execution of the Underwriter Agreement (i.e., by September 2, 2013).

[31] The Settlement Amounts that have been received are currently invested at RBC in interest bearing accounts. Each settlement amount is held in a separate escrow account.

[32] Class Counsel has been informed that, as of August 16, 2013, the escrow accounts contain: (1) Zungui Escrow Account, $7,984,781.20; and (2) Auditor Escrow Account, $1,995,373.52. These accounts reflect the payment of $48,931.32 for the publication of the First Notice (allocated, $39,145.07 from the Zungui Escrow Account and $9,786.25 from the Auditor Escrow Account) and the accrual of $23,926.27 in interest on the Zungui Settlement Amount and $5,159.68 in interest on the Auditor Settlement Amount.

[33] Notice of the certification of the action as against the Zungui Defendants, Ernst & Young LLP, and the Cai Brothers has been given to the Class Members. There were

no opt-outs. The notice also provided notice of the Auditor Settlement and the Zungui Settlement.

[34] Notice of the proposed Underwriter Settlement has recently been given to the Class Members pursuant to a recent court order made at a case conference. Having already had a right to opt-out, class members do not have a right to opt-out with respect to the certification of the action as against the Underwriting Syndicate. When there are partial or progressive certifications of a class action, provided that there was adequate notice, the right to opt-out is a procedural right that may only be exercised once: *Eidoo v. Infineon Technologies AG*, 2012 ONSC 7299 at paras. 29-32; *Nutech Brands Inc. v. Air Canada*, [2008] O.J. No. 1065 (SCJ).

[35] Under the settlements, the Plaintiffs and the Class will provide releases to all of the Defendants. The Cai Brothers will be released as part of the Zungui Settlement. The settlements, if approved, would complete the class action.

[36] The key terms of the settlement agreements are as follows:

- The settlement will be administered by an Administrator;
- the Defendants will pay their respective settlement amounts for the benefit of the Class;
- the settlement funds will be distributed, after payment of any administration expenses and Class Counsel fees, disbursements, and taxes as awarded by the Court;
- the settlement funds will be distributed in accordance with a Plan of Allocation that is in a form satisfactory to the Defendants or as fixed by the Court;
- if the settlement is approved by the court, the Notices of the Settlement will provide Class Members with information concerning their right to participate by filing a Claim Form;
- the settlement funds will be distributed among all Class Members who timely submit valid Claim Forms to the Administrator;
- there are no rights of reversion;
- the Plan of Allocation provides for the possibility of a *cy près* distribution to the Small Investor Protection Association Canada in the event that less than $25,000.00 remains 180 days from the date on which the Administrator distributes the net settlement amount; and
- the Plaintiffs and the Class Members will release the Defendants and certain identified associated entities.

[37] Under the Plan of Notice, the Short Form Notice of Settlement will be published: (a) in the English language, in the business/legal section of the national weekend editions of the *National Post* and the *Globe and Mail*; (b) in the French language, in the business section of *La Presse*; and (c) in the French and English languages across *Marketwire*, a major business newswire in Canada.

[38] Under the Plan of Notice, the Long Form Notice of Settlement will be: (a) posted in both the French and English languages on www.classaction.ca; (b) posted in both the French and English languages on the Administrator's website; and (c) mailed or emailed, along with the Claim Form and the Opt-Out Form, directly to persons that have contacted Class Counsel and have provided their contact information.

[39] Also in accordance with the Plan of Notice, the Long Form Notice of Settlement and the Claim Form will be sent by the Administrator: (a) directly to persons identified as Class Members by way of a computer-generated list provided by Zungui's litigation receiver to Class Counsel and the Administrator; and (b) to the brokerage firms in the Administrator's proprietary databases, requesting that these firms either send a copy of these materials to all individuals and entities identified as Class Members, or to send the names and addresses of all such individuals and entities to the Administrator, who will mail these materials to the individuals and entities so identified.

[40] The estimated cost of implementing the Plan of Notice, excluding the First Notice that has already been published and paid for, will be approximately $140,000.00 (before tax). Of that amount, approximately $85,000.00 is attributable to the cost of effecting direct notice.

[41] David Weir, the President of NPT RicePoint Class Action Services, the proposed Administrator, deposes that the broker outreach portion of the notice plan is likely to bring the settlement to the attention of the Class Members in a manner consistent with other notice programs in securities class actions.

[42] Class Counsel believes that the Approval Notices, disseminated in accordance with the Plan of Notice, will come to the attention of a substantial portion of the Class.

[43] Class Counsel recommends that the court approve the settlements. Class Counsel is of the view that the settlement terms and conditions are fair and reasonable, and represent a significant recovery for Class Members in a securities class action.

[44] Based on the expert opinion of Paul Mulholland, CFA, Class Counsel believes that the combined settlement amounts represent close to 50% of the damages allegedly suffered by the Class Members as calculated by Mr. Muhlholland. I would calculate the class's gross recovery as 46% of the damages allegedly suffered and the class's net recovery after the payment of administrative expenses and legal fees, as claimed, as approximately 33%.

[45] The Plaintiffs have instructed Class Counsel to seek approval of the settlements.

[46] No objections to the quantum of the Settlements have been received to date. However, Class Counsel has received: (a) one objection to the release provisions in the Zungui Agreement insofar as they apply to the Cai Brothers; and (b) one written objection to the proposed Plan of Allocation, discussed below, concerning the proposed ineligibility for any payment to Class Members for shares purchased in the secondary market after the alleged corrective press release on August 22, 2011.

[47] Section 29(2) of the *Class Proceedings Act, 1992* provides that a settlement of a class proceeding is not binding unless approved by the court. To approve a settlement of a class proceeding, the court must find that, in all the circumstances, the settlement is fair, reasonable, and in the best interests of the class: *Fantl v. Transamerica Life Canada*, [2009] O.J. No. 3366 (S.C.J.) at para 57; *Farkas v. Sunnybrook and Women's Health Sciences Centre*, [2009] O.J. No. 3533 (S.C.J.), at para. 43; *Kidd v. Canada Life Assurance Company*, 2013 ONSC 1868.

[48] In determining whether a settlement is reasonable and in the best interests of the class, the following factors may be considered: (a) the likelihood of recovery or likelihood of success; (b) the amount and nature of discovery, evidence or investigation; (c) the proposed settlement terms and conditions; (d) the recommendation and experience of counsel; (e) the future expense and likely duration of litigation; (f) the number of objectors and nature of objections; (g) the presence of good faith, arm's-length bargaining and the absence of collusion; (h) the information conveying to the court the dynamics of, and the positions taken by, the parties during the negotiations; and, (i) the nature of communications by counsel and the representative plaintiff with class members during the litigation. See: *Fantl v. Transamerica Life Canada*, *supra* at para 59; *Corless v. KPMG LLP*, [2008] O.J. No. 3092 (S.C.J.), at para. 38; *Farkas v. Sunnybrook and Women's Health Sciences Centre*, *supra,* at para. 45; *Kidd v. Canada Life Assurance Company*, 2013 ONSC 1868.

[49] In my opinion - independent of the matter of the Plan of Allocation (the plan of distribution) - having regard to the various criteria set out above, the three settlement agreements taken together are fair, reasonable, and in the best interests of the Class Members.

[50] Therefore, independent of the matter of the Plan of Allocation, which I will discuss next, I approve the three settlements.

E. DISTRIBUTION PLAN

1. The Court's Jurisdiction to Approve the Distribution Plan

[51] In the case at bar, the court's authority to approve the plan of distribution, the Plan of Allocation, comes from the settlement agreements, where the plan of distribution is referred to as a Plan of Allocation.

[52] The settlement agreements define the "Plan of Allocation" as follows:

> Plan of Allocation means the distribution plan distributing the proposed settlement in a form satisfactory to the Settling Defendants or as fixed by the Court.

[53] As I interpret the settlement agreements, and as confirmed by the Plaintiffs during argument, I can approve the settlements independent of approving the Plan of Allocation, which is what I have done. In other words, I have approved the settlements, which are now binding on the parties and on the Class Members, and I shall determine or fix the Plan of Allocation.

[54] For reasons that I will set out below, I do not approve of the Plan of Allocation proposed by the parties, but I shall vary it, and I shall approve a different plan of distribution.

[55] Had the settlement agreements in the case at bar not left it to the court to ultimately determine what is an appropriate plan of distribution, I would not have approved the settlements, because I do not think the proposed Plan of Allocation is fair and reasonable and in the best interests of the class. I also would not have approved Class Counsel's fees because the settlements would not have been approved.

2. *The Test for Approving a Distribution Plan*

[56] In the situation where there is a judgment in a certified class action, the court's authority to determine or approve a plan of distribution comes from s. 26 of the *Class Proceedings Act, 1992*, which states:

> *Judgment distribution*
>
> 26. (1) The court may direct any means of distribution of amounts awarded under section 24 or 25 that it considers appropriate.
>
> *Idem*
>
> (2) In giving directions under subsection (1), the court may order that,
>
> (a) the defendant distribute directly to class members the amount of monetary relief to which each class member is entitled by any means authorized by the court, including abatement and credit;
>
> (b) the defendant pay into court or some other appropriate depository the total amount of the defendant's liability to the class until further order of the court; and
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> (c) any person other than the defendant distribute directly to class members the amount of monetary relief to which each member is entitled by any means authorized by the court.
>
> *Idem*
>
> (3) In deciding whether to make an order under clause (2) (a), the court shall consider whether distribution by the defendant is the most practical way of distributing the award for any reason, including the fact that the amount of monetary relief to which each class member is entitled can be determined from the records of the defendant.
>
> *Idem*
>
> (4) The court may order that all or a part of an award under section 24 that has not been distributed within a time set by the court be applied in any manner that may reasonably be expected to benefit class members, even though the order does not provide for monetary relief to individual class members, if the court is satisfied that a reasonable number of class members who would not otherwise receive monetary relief would benefit from the order.

Idem

(5) The court may make an order under subsection (4) whether or not all class members can be identified or all of their shares can be exactly determined.

Idem

(6) The court may make an order under subsection (4) even if the order would benefit,

(a) persons who are not class members; or

(b) persons who may otherwise receive monetary relief as a result of the class proceeding.

Supervisory role of the court

(7) The court shall supervise the execution of judgments and the distribution of awards under section 24 or 25 and may stay the whole or any part of an execution or distribution for a reasonable period on such terms as it considers appropriate.

Payment of awards

(8) The court may order that an award made under section 24 or 25 be paid,

(a) in a lump sum, forthwith or within a time set by the court; or

(b) in instalments, on such terms as the court considers appropriate.

Costs of distribution

(9) The court may order that the costs of distribution of an award under section 24 or 25, including the costs of notice associated with the distribution and the fees payable to a person administering the distribution, be paid out of the proceeds of the judgment or may make such other order as it considers appropriate.

Return of unclaimed amounts

(10) Any part of an award for division among individual class members that remains unclaimed or otherwise undistributed after a time set by the court shall be returned to the party against whom the award was made, without further order of the court.

[57] It may be noted that under s. 26(1) of the *Class Proceedings Act, 1992*, the court may direct any means of distribution of amounts awarded that it considers appropriate. I am not aware of any caselaw actually applying s. 26(1), although numerous cases have suggested that the court has ample discretion and ample scope for creativity in employing s. 26.

[58] In the case at bar, as noted above, the court's authority to approve the plan of distribution comes from the settlement agreements, where the plan of distribution is referred to as a Plan of Allocation, and, as noted above, as I interpret the settlement agreements, I can determine or fix the Plan of Allocation as I think appropriate.

[59] In determining what is appropriate, I intend to apply the same test or standard that the court applies when deciding whether to approve a settlement. Thus, a plan of

distribution will be appropriate if in all the circumstances, the plan of distribution is fair, reasonable, and in the best interests of the class.

3. The Proposed Plan of Allocation

[60] For reasons that I will set out below, I do not approve of the Plan of Allocation proposed by the parties, but I shall vary it and approve a different plan of distribution.

[61] Class Counsel, with Mr. Mulholland's assistance, developed the Plan of Allocation. This plan was structured to reflect Mr. Mulholland's opinion that Zungui suffered two share price falls that were statistically significant, net of external market factors. These events occurred on: (1) June 2, 2011, when Muddy Waters LLC issued a report about Sino-Forest Corporation in which a fraud was alleged; and (2) August 22, 2011, when Zungui issued the press release announcing the suspension of 2011 audit procedures by Ernst & Young LLP.

[62] The Plaintiffs' damages theory is that the value of Zungui's common shares was at all times artificially inflated by misrepresentation and that the artificial inflation, equivalent to $1.52 per share, was removed from the share value by the close of TSX-V trading on August 22, 2011. The Plaintiff's theory is that the artificial inflation was removed: in part, on June 2, 2011, in an amount of $0.26; and in balance, on August 22, 2011, in an amount of $1.26.

[63] The amount of each Class Member's compensation will depend upon: whether the Class Member is a Primary Market Purchaser and/or a Secondary Market Purchaser and/or Share Exchange Acquiror; the number and price of Zungui common shares purchased by the Class Member during the Class Period; whether and when the Class Member sold Zungui common shares purchased during the Class Period, and the price at which these common shares were sold; whether the Class Member continues to hold some or all of the Zungui common shares purchased during the Class Period; and the total number and value of all claims for compensation filed with the Administrator.

[64] The Plan of Allocation provides that no compensation shall be paid for any shares disposed of before June 2, 2011, which is consistent with Mr. Mulholland's opinion that June 2, 2011 was the first time that Zungui's common shares were subject to a statistically significant event, net of external market factors.

[65] The Plan of Allocation provides that no compensation shall be paid for any shares purchased after the time of the making of the alleged corrective disclosure on August 22, 2011. The main rationale for the disqualification of these shares is that they purchased when it was publicly known that audit issues existed. I note, however, that it was not until another month later that E&Y disavowed that Zungui's financial statements were GAAP compliant.

[66] In any event, although a purchaser of Zungai shares on Aug 22, 2011 is a Class Member, under the proposed Plan of Allocation, he or she is not entitled to receive compensation.

[67] These background circumstances bring me to the written objection to the Plan of Allocation delivered by Dr. Christopher Lane, which I set out below:

> My name is Dr. Christopher Lane (psychologist) and I would like to register an objection to the terms of the proposed "Plan of Allocation," particularly under the heading "Secondary Market Purchasers," and under "VII" which states: "No Nominal Entitlement shall be recognized for any Eligible Shares purchased after the time of the making of the alleged corrective disclosure on August 22, 2011." This statement appears to eliminate the right of anyone who purchased shares of ZUN on August 22, 2011 to receive any compensation whatsoever and to thereby lose 100% of their investment. I happen to be one of those individuals who purchased shares on that fateful August 22, 2011 day, as did my brother, Brian Lane. Indeed, I bought a total of 117,000 shares of ZUN that day at a "book value" (according to my bank statements) of $47,735.83 (average cost per share of 40.8 cents). As one might expect, I am very upset by the wording of the proposed "Plan of Allocation" and would like to offer a suggestion of a fairer settlement, as the one proposed is, in my mind, overly punitive and leaves investors in my position with a feeling of defeat and lack of justice.
>
> .... While it is true that the announcement indicated that Ernst & Young suspended procedures until Zungui "clarifies and substantiates its position with respect to issues pertaining to the current and prior year" this does not clearly foreshadow the events that followed, which turned out to be devastating to the investors who held the stock and represented a "worst case scenario" with the stock never trading again after August 22, 2011. Clearly this was bad news and sent the stock tumbling from approximately 1.50 down to trading around 40 cents per share for most of the day on August 22, 2011 and ending the day around 34 cents per share. Of course, in hindsight it is easy to suggest that one shouldn't have bought stock in ZUN that day, but at that time there were also many who felt the negative reaction was entirely overblow and that clarification of the issues could logically prevail and substantiate the position of the company. In short, there was no way of knowing that the worst possible outcome would come to pass, with investors unable to trade their shares ever again.
>
> I submit that eliminating shareholders who bought ZUN stock on August 22, 2011 from any form of compensation is overly harsh and punitive. It was clear that an important issue existed at that time but issues emerge with Venture Exchange listed stocks quite frequently but without these catastrophic consequences. And it is important to note that investors such as myself have suffered considerably due to this loss of capital. In my case, I lost all of my RRSP, almost all of my cash trading account holdings and a good part of my TFSA. With children entering university I am hard-pressed to pay my part of the costs as well as funding home and business expenses. Indeed, these losses have had a significant negative effect on my quality of life and that of my family and have led to me working long hours to pay for our needs, thereby creating significant hardship.
>
> Hence, I ask that the court consider changing the section dealing with ZUN purchasers of August 22, 2011 to include them in providing some compensation in the class action lawsuit. Of course, I believe that to be fair, the compensation for purchasers on August 22, 2011 should be much less than for those who purchased earlier at prices of $1.52 per share or higher. I would suggest that a discount of 80% of the amount often quoted in the "Plan of Allocation" ($1.52) would be appropriate, which would amount to payment of 30.4 cents per share for individuals who bought shares of ZUN on August 22, 2011. I ask that the court consider this proposal to be fair to all shareholders of ZUN without singling out any in a harsh or punitive manner. We all lost money in this investment and have suffered as a result and it's unfair to single out a subsection of individuals for exclusion of all compensation.

[68] The Plan of Allocation contemplates that for some Class Member's eentitlements, a notional amount of damage based on the application of the calculations in the Plan of Allocation before distribution proration, will be discounted to reflect the risks facing the claimants. Class Counsel considered that the question of whether a discount to a Nominal Entitlement ought to apply for a particular type of acquisition should be determined by considering the particular strengths and weaknesses of the common law and statutory claims are common to all groups

[69] With a view to ensuring that any discount was arrived at in a manner that was objective and fair, a formal mediation session was held on April 29, 2013. Joel Wiesenfeld was the mediator. Mr. Wiesenfeld practiced law as a broker/dealer litigation and securities regulatory counsel for 31 years.

[70] At the mediation, the claimant groups were represented by Class Members holding Eligible Shares as follows: (a) the Plaintiffs, who bought substantially all of their shares in Zungui's IPO, represented Primary Market Purchasers; (b) Nick Angellotti CA, IFA and President and Managing Director of Williams & Partners Forensic Accountants Inc., the representative of a partnership that purchased Zungui's shares in the secondary market, represented Secondary Market Purchasers; and (c) Avi Grewal, President and Chief Executive Officer of Cinaport Capital Inc., a private investment firm which acts as advisor for the Cinaport China Opportunity Fund, a fund with investments in private and public PRC based companies, represented Share Exchange Acquirors.

[71] The representatives were represented by counsel; namely: Charles Wright and Nicholas Baker of Siskinds LLP for the Plaintiffs; Kirk Baert of Koskie Minsky LLP for Mr. Angellotti; and John J. Longo of Aird & Berlis LLP for Mr. Grewal.

[72] I pause here to note that nobody represented the interests of secondary market purchasers who, like Dr. Lane, purchased shares on August 22, 2011.

[73] The negotiations were all conducted at arm's length and the position of each claimant group was advanced by their counsel. The full-day mediation session concluded with the Primary Market Purchasers and Secondary Market Purchasers reaching agreement that the proposed Plan of Allocation should provide for the Nominal Entitlements of primary market purchasers to be undiscounted and the Nominal Entitlements of secondary market purchasers should be discounted by 8%.

[74] The representatives were unable to agree on a discount to be applied to the claims of Share Exchange Acquirors at the mediation, and so the Plaintiffs proposed (and posted on Class Counsel's website) a draft Plan of Allocation with a discount of 60% for Share Exchange Acquiror claims. Subsequently, Class Counsel agreed, to amend the Share Exchange Acquiror Discount to 40 %.

[75] Class Counsel submits that an 8% discount for secondary market purchasers is fair and reflects that: (a) the secondary market purchasers were required to obtain leave under Part XXIII.1 of the Ontario *Securities Act* before asserting the right of action for

misrepresentation in Zungui's secondary market disclosure documents, and such leave would be contested; (b) Part XXIII.1 provides defendants with a number of defences to liability for secondary market misrepresentation, and in this case, the secondary market purchasers could expect to face the "reasonable investigation" defence, an expert reliance defence, and a due diligence; and (c) the secondary market purchasers may not be able to recover the full estimated damages they have suffered, due to liability limits.

[76] Class Counsel submits that no discount for primary market purchasers is fair because it reflects that: (a) these purchasers did not need to obtain leave of the Court to assert their claim; (b) damages are not limited for primary market purchasers in the same way as they are limited for secondary market purchasers; (c) if a prospectus is found to have contained a misrepresentation, then the issuer is strictly liable, (d) certain defendants, such as the issuer's directors and officers, are generally liable, unless they demonstrate on a balance of probabilities that they exercised reasonable diligence prior to issuance of the prospectus; and (e) liability is joint and several and damages can be recovered from any defendant with the means to pay.

[77] Class Counsel initially considered that a 60% discount for Share Exchange Acquirors was fair. However, the Significant Shareholder Group through their counsel at Aird and Berlis LLP, and certain members of the Significant Shareholder Group indicated that they had higher expectations than a settlement with the Underwriting Syndicate at $750,000.00, in part, based on the fact that the Underwriting Syndicate had earned fees of approximately $2.75 million for underwriting the IPO.

[78] However, the Significant Shareholder Group were prepared to support the proposed settlement with the Underwriting Syndicate if two (2) conditions were met: (1) Class Counsel would limit their request for Class Counsel Fees to an agreed amount; and (2) the discount applicable to Share Exchange Acquirors under the proposed Plan of Allocation would be amended from 60% to 40%.

[79] Class Counsel estimates that the impact on the combined settlement fund of the amendment to the discount applicable to Share Exchange Acquirors under the proposed Plan of Allocation will be at most $262,200.00 and more likely the impact will be less, because the maximum impact assumes no proration, which is unlikely to be the case.

[80] Class Counsel communicated with each Class Member who participated in the mediation relating to the Plan of Allocation, and they have instructed that the proposed amended discount applicable to Share Exchange Acquirors is acceptable.

[81] The Plan of Allocation provides for the possibility of a *cy près* distribution to the Small Investor Protection Association Canada in the event that less than $25,000.00 remains in the Allocation Pool 180 days from the date on which the Administrator distributes the Net Settlement Amount to Authorized Claimants.

[82] Notwithstanding the objection to the Plan of Distribution, Class Counsel is of the view that the Plan of Allocation was carefully considered and promotes the interests of the class as a whole, and that it is fair and reasonable and ought to be approved.

[83] At the argument of the fairness hearing, Class Counsel argued that should the court consider it appropriate to have purchasers like Dr. Lane participants in the Plan of Allocation, their claims should be discounted by 98.5%.

4. Discussion and Analysis of the Proposed Plan of Allocation

[84] I do not regard the Proposed Plan of Allocation as appropriate, fair, reasonable, or in the best interests of the class.

[85] In my opinion, Dr. Lane's objection to the Plan of Allocation and his suggestion as to how the plan should be revised has considerable merit.

[86] Although perhaps unlikely to occur, it seems inappropriate and unfair to me that the proposed Plan of Allocation provides for a *cy près* distribution to a small investor association and does not provide any compensation for an investor like Dr. Lane, who is a member of the class. More to the point, in my opinion, it is inappropriate and unfair to include August 22, 2011 purchasers as Class Members and then exclude them from the Plan of Allocation.

[87] Notwithstanding that it was the Defendants who urged that these purchasers be included as Class Members as part of the bargaining for the settlements, once Class Counsel and the Representative Plaintiffs agreed to the joinder of these Class Members, it was unfair and inappropriate for Class Counsel and the Representative Plaintiffs to advocate a theory of the case that August 22, 2011 purchasers were not eligible for any compensation at all.

[88] If Dr. Lane, his brother, and other August 22, 2011 purchasers had appreciated that the parties had included them in the class as a bargaining chip but had excluded them from the theory of the claim and would exclude them from the Plan of Allocation, these putative class members sensibly should have opted-out of the class action rather than add the unrequited value of their releases to the consideration or *quid quo pro* that the Defendants will be receiving for the settlement payments. As it stands, Dr. Lane and those similarly situated are bound by the settlement but receive nothing themselves for being a Class Member.

[89] In my opinion, the appropriate Plan of Allocation is the one proposed by Dr. Lane.

[90] Accordingly, I shall revise the Plan of Allocation in accord with Dr. Lane's suggestion, which I regard as fair and reasonable, and I approve the Plan of Allocation as revised.

F. ADMINISTATION OF THE SETTLEMENT

[91] Class Counsel proposes the appointment of NPT RicePoint Class Action Services as the Administrator. NPT has already served as the Notice Advisor in the Action. NPT has also been administering bilingual class action settlements for over 9

years. In Class Counsel's opinion, NPT has the experience and resources that make them capable of administering the Settlements.

[92] NPT's administration proposal provides for a minimum administration fee of $35,000, and a maximum administration fee cap of $195,000.00, before taxes.

[93] I approve the appointment of NPT RicePoint Class Action Services as the Administrator.

G. FEE APPROVAL

[94] Turning to the matter of Class Counsel's fee request of $2,807,037.56.

[95] The Retainer Agreements with the Plaintiffs provide that Class Counsel may seek a fee of up to 30% of the recovery. Class Counsel are seeking a recovery of 20.75% (a 3.3 multiplier).

[96] As at August 12, 2013, Class Counsel had docketed time of $648,386.00, excluding applicable taxes, disbursements of $226,670.44, exclusive of applicable taxes.

[97] Class Counsel is not seeking to recover, and will not return to request payment of the time and disbursements required to complete the administration of the settlement, which is estimated to be at least $50,000.00.

[98] Class Counsel has agreed to pay, from Class Counsel's fee award the accounts of Aird & Berlis LLP rendered to the Significant Shareholder Group in the amount of $105,796.50, taxes in the amount of $13,896.73 and disbursements in the amount of $1,101.36.

[99] Class Counsel proposes to pay Wolf Popper LLP $105,689.00 (US$) in fees, and (US$) $1,466.73 in disbursements from the Class Counsel's fee award. Mr. Clarke, a representative plaintiff, initially contacted this U.S. law firm to investigate his potential claim. Ms. Patricia Avery, of Wolf Popper LLP, has been a member of the Class Counsel team prosecuting the Action, and Wolf Popper LLP undertook certain tasks that were within the competence of the firm, such as researching risk disclosure practices in North American securities offering documents for issuers with substantial operations in the People's Republic of China.

[100] The disbursements included $40,465.42 in agent fees for investigations in the People's Republic of China, location of the Cai Brothers, translation of correspondence and pleadings, Hague Convention service on the Cai Brothers and the cost of paying for independent counsel to attend at the Plan of Allocation mediation.

[101] The disbursements include $156,842.05 in expert fees and mediation fees for Mr. Mulholland, Mr. Mak, William H. Purcell, a U.S. investment banking expert, in relation to underwriting due diligence practices for companies with substantially all operations in the People's Republic of China, and Mr. Wisenfeld.

[102] The fairness and reasonableness of the fee awarded in respect of class proceedings is to be determined in light of the risk undertaken by the lawyer in conducting the litigation and the degree of success or result achieved: *Parsons v. Canadian Red Cross Society*, [2000] O.J. No. 2374 (S.C.J.), at para. 13; *Smith v. National Money Mart*, [2010] O.J. No. 873 (S.C.J.), at paras. 19-20; *Fischer v. I.G. Investment Management Ltd.*, [2010] O.J. No. 5649 (S.C.J.), at para 25.

[103] Factors relevant in assessing the reasonableness of the fees of class counsel include: (a) the factual and legal complexities of the matters dealt with; (b) the risk undertaken, including the risk that the matter might not be certified; (c) the degree of responsibility assumed by class counsel; (d) the monetary value of the matters in issue; (e) the importance of the matter to the class; (f) the degree of skill and competence demonstrated by class counsel; (g) the results achieved; (h) the ability of the class to pay; (i) the expectations of the class as to the amount of the fees; (j) the opportunity cost to class counsel in the expenditure of time in pursuit of the litigation and settlement: *Smith v. National Money Mart, supra*, at paras. 19-20; *Fischer v. I.G. Investment Management Ltd., supra,* at para 28.

[104] Having regard to these various factors, I approve Class Counsel's request for approval of its legal fees.

H. CONCLUSION

[105] Orders accordingly.

Perell, J.

Released: August 27, 2013

CITATION: Zaniewicz v. Zungui Haixi Corporation, 2013 ONSC 5490
COURT FILE NO.: 11-CV-436360-00CP
DATE: August 27, 2013

ONTARIO
SUPERIOR COURT OF JUSTICE

BETWEEN:

JERZY ROBERT ZANIEWICZ and EDWARD C. CLARKE

Plaintiffs

- and -

ZUNGUI HAIXI CORPORATION, E&Y, FENGYI CAI, JIXU CAI, YANDA CAI, MICHELLE GOBIN, MICHAEL W. MANLEY, PATRICK A. RYAN, ELLIOTT WAHLE, MARGARET CORNISH, CIBC WORLD MARKETS INC., CANACCORD GENUITY CORP. (f.k.a. CANACCORD FINANCIAL LTD)., GMP SECURITIES LP and MACKIE RESEARCH CAPITAL CORPORATION (f.k.a. RESEARCH CAPITAL CORPORATION)

Defendants

REASONS FOR DECISION

Perell, J.

Released: August 27, 2013.