YBM CASE STUDY:

ANATOMY OF A SECURITIES CLASS ACTION SETTLEMENT

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I. INTRODUCTION

In February 2002, the parties to several actions which arose out of the meteoric rise and fall of the fortunes of YBM Magnex International, Inc. ("YBM") announced a settlement agreement (subject to court approval) following a three-week settlement conference. Two of those actions were Ontario class actions. Therefore, the proposed settlement required court approval pursuant to s. 29(2) of the *Class Proceedings Act* ("*CPA*"), which contributed to the substance, form, and structure of the settlement agreement. The unique aspects of the YBM settlement and its complexities are best understood with some knowledge of the background of YBM and the allegations made against the numerous defendants in the YBM class actions.

II. BACKGROUND TO YBM

YBM is an Alberta corporation (now in receivership), which had its head office in Newtown, Pennsylvania. It purported to be involved in the manufacture and global distribution of magnets and magnetic products, bicycles, computer software, and oil. On July 18, 1994, YBM issued 4 million common shares to the public and became a junior capital pool corporation pursuant to the regulations of the Alberta Stock Exchange. Thereafter, its shares began trading on the Toronto Stock Exchange ("T.S.X.") on March 7, 1996. YBM's shares were also traded over the counter on the New York Stock Exchange.

On May 13, 1998, a search warrant of YBM's head office was executed as a result of the coordinated efforts of the Organized Crime Strike Force of the United States Attorney's Office, the Federal Bureau of Investigation, and several other United States government agencies. That day, the Ontario Securities Commission ("O.S.C.") issued a cease trading order in respect of YBM's shares. Those shares have ceased to trade ever since.

The Court of Queen's Bench of Alberta appointed a receiver, on December 8, 1998, to protect YBM's existing assets, to monitor and assess its Eastern European operations, and to prepare a plan of distribution of the net assets of YBM.

On June 7, 1999, YBM, through its Receiver, pleaded guilty in the United States District Court to a multi-object conspiracy to commit fraud, which included fraudulent, manipulative, and deceptive devices in the purchase and sale of YBM securities and the filing of reports with securities regulators which contained material misrepresentations and omissions during the period 1993 to 1998.

Thereafter, three class actions were commenced - one in the United States District Court of the Eastern District of Pennsylvania and two in the Ontario Superior Court of Justice. In all three class actions, allegations were made that YBM failed to disclose material information to the public and made misrepresentations regarding YBM's financial statements. It was also alleged that YBM conducted very little legitimate business and was, in fact, a money laundering operation carried on by members of organized crime.

III. THE THREE CLASS ACTIONS

A Prospectus Class Action (*Royal Trust Corporation of Canada et al. v. Igor Fisherman et al.*)

The proposed representative plaintiffs commenced the action on their own behalves and on behalf of the members of the class of persons in Canada who purchased or acquired common shares of YBM distributed pursuant to a YBM prospectus dated November 17, 1997, and suffered a loss. They claimed damages in the amount of $125 million for negligent misrepresentation at common law, misrepresentation under s. 130 of the Ontario *Securities Act* (and the comparable Acts in British Columbia, Alberta, and Québec), and negligence. The defendants were YBM's officers and directors, auditors, lawyers, and financial advisors/underwriters of the prospectus financing. In essence, the allegations were that, had the defendants acted competently and in accordance with their duties to the class members, the prospectus would not have been receipted by the O.S.C., the class members would not have purchased their shares, and they would not have suffered a loss.

B General Class Action (*Roger Mondor v. Igor Fisherman et al.*)

The other Ontario class action (referred to as the "General Class Action" to distinguish it from the "Prospectus Class Action") was brought by the proposed representative plaintiffs on their own behalves and on behalf of each and every person, wherever resident, who dealt in shares of YBM between March 7, 1996 (the date the shares began to trade on the T.S.X.) and May 14, 1998. The plaintiffs claimed damages in the amount of $750 million and sought a variety of other relief, including a declaration that certain directors, officers, and YBM's auditors

breached the misleading advertising section [s. 52(1)] of the Canada *Competition Act* R.S.C. 1985, c. C.-34, by representing in various statements, press releases, prospectuses etc., that YBM was a legitimate business with income only from legitimate business activities (referred to in the Statement of Claim as "the Representation"), a declaration that the Representation was made negligently or fraudulently or recklessly, and a declaration that certain of the defendants were involved in a conspiracy to deceive the class members for the purpose of maintaining and increasing the price of YBM shares by the issuance of false statements etc. and by their failure to make required timely disclosure of material developments. The defendants were most of same persons and entities named as defendants in the Prospectus Class Action.

C United States Class Action (*John Paraschos et al. v. YBM Magnex International, Inc. et al.*)

A class action was commenced in the United States District Court for the Eastern District of Pennsylvania on behalf of all persons and entities (except certain insiders) that acquired YBM common shares between January 19, 1996 (the date of an earlier prospectus) and May 14, 1998, against many of the same defendants as in the Ontario class actions. It was alleged that certain information made available to members of the public was intended to and did deceive the investing public in that it contained misrepresentations and material omissions and that the market price of YBM shares was artificially inflated as a result. The action was dismissed on December 5, 2000, for reasons of comity; the Court determined that Canada had the greater connection to the matters in issue in the action. The plaintiffs' motion for a reconsideration of the decision was denied. Their appeal to the Court of Appeals for the Third Circuit was pending at the time of the settlement in February 2002.

IV. YBM SETTLEMENT CONFERENCE

The two Ontario class actions were case managed together, along with two other actions commenced by YBM's Receiver/Independent Litigation Supervisor (appointed by the Court for the purpose of prosecuting litigation on behalf of YBM) by the Honourable Mr. Justice Cumming. By the time these actions were settled (over three years after they were commenced), pleadings had not yet closed, productions had not been exchanged, and examinations for discovery had not yet been scheduled. The parties agreed to participate in a mediation in April 2001, however,

it was not successful. Some of the defendants had brought Rule 21 motions, which were denied.[1] The certification motions had been scheduled but not yet heard.

Only six months after the first unsuccessful mediation effort, in November 2001, several of the defendants sought and obtained an order from Cumming J. directing the parties to appear before the Honourable Mr. Justice Winkler for a pre-trial conference pursuant to Rule 50.01 to consider the possibility of settlement of any or all of the issues in the class actions.

The pre-trial conference took place on January 16, 17, 18, 21, and 22, 2002. Counsel for the parties in the U.S. Class Action and YBM's Receiver were invited to participate in the pre-trial conference and did so. On February 7, 2002, settlement of all three class actions and YBM's actions was achieved, subject to the approval of the Ontario, Alberta, and Pennsylvania Courts. Thereafter, several months were spent by all counsel papering the settlement, which involved primarily drafting the consent Judgment to be submitted to Cumming J. for approval in May 2002.

The fact that an earlier mediation effort did not get off the ground demonstrates many of the difficulties in moving parties towards settlement in these kinds of cases. Many of the factors that motivate parties to consider settling class actions, as well as factors that can be obstacles are set out below. Some of them were, no doubt, present in the YBM case.

Among the most important motivations to settlement is the significant costs associated with prosecuting or defending a class action regardless of the perceived merits of the claim or defence. The quantum of damages typically sought in the statement of claim in a securities class action is large, making the stakes sufficiently high for all parties that numerous interlocutory motions and appeals on those motions are perceived to be worthwhile and therefore seem inevitable. As a result, a lengthy period of time may pass between the time the statement of claim is issued and pleadings are closed, during which time the parties' costs are increased significantly and there are numerous delays in having the action tried on its merits. For example, it is not uncommon in class actions for defendants to bring motions under Rule 21, challenging the statement of claim on the basis that it discloses no reasonable cause of action. These motions often involve complex and novel points of law and, consequently, are subject to

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[1] *C & L Dedicated Enterprise Fund (Trustee of) v. Fisherman*, [2001] O.J. No. 4621 (S.C.J.); and *Mondor v. Fisherman*, [2001] O.J. No. 4620 (S.C.J.)

appeals. Also, the recent cases in which substantial costs awards have been made against plaintiffs in class actions will likely motivate plaintiffs in future to consider early settlement.[2]

Common obstacles to settlement, which were present in the YBM class actions, include a lack of information about the merits of the claim and defences, multiple parties with conflicting interests, and similar or overlapping actions in other jurisdictions. Settlement discussions which take place before examinations for discovery have been completed can be hampered by a lack of information about the class size, estimated value of damages suffered by each class member, and extent of or proportionate liability of each defendant. Parties can, of course, overcome this problem by agreeing to exchange information as part of the settlement discussions. In the YBM case, much of the information relating to class size and identity of class members was available at the time of the pre-trial conference because of the work done by YBM's Receiver in the context of the receivership. Moreover, YBM's Independent Litigation Supervisor disclosed that it had conducted an investigation and prepared a report (protected by solicitor-client privilege) of various causes of action against various defendants, which founded YBM's two actions.

In an action where there are numerous defendants having a variety of different interests and, perhaps crossclaims against one another, settlement discussions may prove to be complex and unwieldy. Ultimately, some parties may not willingly participate in settlement discussions, while others may be prepared to come to the bargaining table. Where the pre-trial conference is mandated by the Court under Rule 50 (as was the case in the YBM matter), parties cannot simply choose to withdraw from settlement discussions at will (although, obviously, unless the parties are prepared to participate in the pre-trial conference in a meaningful way, a resolution is unlikely). Moreover, as Cumming J. noted when he later approved the YBM settlement, a settlement agreement which results from a discussion taking place through the auspices of the Court may also be viewed more favourably by the Court which is asked to approve the settlement under s. 29 of the *CPA*.[3]

V. TERMS OF THE YBM SETTLEMENT

A summary of the terms of the settlement is as follows:

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[2] See, for example, *Gariepy v. Shell Oil Co.* (2002), 23 C.P.C. (5th) 393 (S.C.J.); and *Pearson v. Inco Ltd.*, [2002] O.J. No. 3532 (S.C.J.)

[3] *Mondor v. Fisherman*; *CC & L Dedicated Enterprise Fund (Trustee of) v. Fisherman* (2002), 22 C.P.C. (5th) 346 (Ont. S.C.J.)

(1) The Ontario class actions were to be certified as class proceedings on consent;

(2) Some of the defendants and third parties were to pay the sum of $85 million in full and final settlement of all claims against them. The amount of each defendant or third party's contribution was not known by any other party;

(3) The class members were also to receive a distribution, in the receivership, from the assets of YBM, estimated to be valued at approximately $35 million;

(4) The class members in the Prospectus Class Action were to be paid $7,500,000, *pro rata*, as a priority payment, in recognition of their stronger statutory claim. (This was estimated to be approximately Cdn $0.07 for each Cdn $1.00 of net loss.);

(5) Thereafter, the class members in the Prospectus Class Action and the General Class Action were to share the balance of the settlement monies, after payment of expenses and lawyers' fees, on a *pro rata* basis based upon their calculated net loss. (It was estimated that this *pro rata* distribution, plus the distribution by the Receiver of YBM from the assets remaining in the estate of YBM, would be approximately Cdn $0.20 for each Cdn $1.00 of net loss.);

(6) A person would be eligible to participate in the distribution only if that person suffered a net loss in trading in shares of YBM and did not contribute to the wrongdoing involving YBM that gave rise the class actions. A procedure was provided for in respect of disputes with claimants as to either their membership in a class or quantum of net loss;

(7) Ernst & Young YBM Inc., the Receiver of YBM, was to be appointed as administrator of the settlement to operate the plan for distribution and make decisions as to eligibility under the direction of the Court;

(8) The Administrator was to contact known potential class members to inform them of the steps they should take to submit their claims;

(9) The class members were to have until a date fixed by the Court to opt out of the class actions;

(10) No person was permitted to opt out a minor or mentally incapable person without leave of the Court after notice to the Public Guardian and Trustee and/or to the Children's Lawyer;

(11) If a person opted out of one of the class actions, he, she, or it was deemed to have opted out of the other class action;

(12) Every class member (except those who opted out of the class actions) is bound by the settlement, whether or not the person submitted a claim in accordance with the plan for distribution and whether or not the claim has been accepted for payment;

(13) Each class member who did not opt out and his or her heirs and assigns etc. shall be conclusively deemed to have released all settling defendants and third parties from all claims of every nature or kind, including any claim in any way relating to or arising indirectly from the trading in YBM shares and/or YBM's business operations and they shall be forever barred from asserting any such claims;

(14) The class members who did not opt out were to have until a date fixed by the Court to submit a claim seeking to participate in the distribution of the settlement monies. A class member was required to submit a claim establishing a net loss in order to participate in the distribution of the settlement monies;

(15) The settlement and approval would be null and void and of no force in effect if:

(i) General class members and Prospectus class members having net losses valued at more than an amount agreed upon by the parties and approved by the Court opted out of the class actions, unless the defendants and third parties waived this requirement; or

(ii) the appeal in the United States Court of Appeals for the Third Circuit the U.S. class action was not dismissed with prejudice;

(16) The cost of the notice program, the administration, and of the distribution under the plan were to be paid out of the settlement monies;

(17) The fees and disbursements of class counsel in the U.S. and Canadian class actions were to be fixed by the Court and paid out of the settlement monies; and

(18) The Court was to supervise the administration and operation of the plan and issue orders as necessary to implement and enforce the provisions of the plan for distribution.

The YBM settlement agreement took the form of a document called a “Consent and Agreement”, executed by counsel for all the parties. It was filed with the Court and attached a consent Order for approval by Cumming J., which provided for the following:

(1) the parties had agreed to a settlement in the form of an attached draft Judgment (drafted cooperatively by all counsel over the course of several weeks, under the continued supervision of Winkler J. in his capacity as pre-trial conference judge);

(2) the date for the settlement approval hearing was set, at which time the draft Judgment setting out the settlement agreement terms would be submitted to Cumming J. for approval;

(3) the quantum and manner of payment of the settlement monies was set out;

(4) a friend of the court was appointed, whose job it was to receive objections to the settlement (if any) from class members; and

(5) the manner of notice to class members of the settlement approval hearing was ordered.

The implementation of the settlement is reaching its conclusion. An interim distribution of funds has already been made to shareholders and it is anticipated that the final distribution of settlement funds and assets of YBM in the receivership will be made by the end of the year. Because of the number of class members and the fact that the settlement was the first of its kind in many ways, administration of the settlement and distribution of the settlement proceeds to class members will have taken almost two years.

VI. STRUCTURING A CLASS ACTION SETTLEMENT

Pursuant to section 29(2) of the *CPA*, a settlement of a class proceeding is not binding unless approved by the Court, in which case it will bind all class members who do not exercise their right to opt out. The Court will be asked to approve a proposed settlement at what has come to be known as a "fairness hearing", at which time the Court will consider the following:

A. whether the action may be certified (if it has not already been certified);

B. whether the settlement is fair, reasonable, and in the best interests of the members of the class; and

C. whether the process for the administration of the proposed settlement is workable.

Each of these considerations is addressed below.

A Whether the action can be certified

If the action has not already been certified, a certification order must also be sought as part of the fairness hearing so that all members of the class will be bound by the settlement. It will inevitably be a term of the settlement that all parties consent to certification. However, the Court must still decide whether certification is appropriate. Section 5(1) of the *CPA* sets out the criteria which, if established, require the Court to certify a class proceeding.

The general policy considerations in favour of settlements appear to have caused some Courts to relax the stringent requirements for certification under section 5 of the *CPA*. For example, in *Gariepy v. Shell Oil Co.,*[4] the Honourable Mr. Justice Nordheimer approved a proposed settlement and made a certification order, notwithstanding that a previous motion for certification of the action had been denied. Nordheimer J. stated that the requirements for certification in the settlement context are the same as they are in the litigation context, however, their application need not "be as rigorously applied in the settlement context ..., principally because the underlying concerns over the manageability of the ongoing procedures are removed." (It may be that the concerns which Nordheimer J. identified on the certification motion originally were resolved by the manner in which settlement was to be carried out and,

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[4] *Gariepy v. Shell Oil Co.* (2002), 26 C.P.C. (5th) 358 (S.C.J.)

therefore, certification was granted and the settlement approved.[5]) Nordheimer J.'s reasoning in the *Gariepy* case was accepted in *Furlan v. Shell Oil Co.*,[6] in which the Court stated that settlement also provides a measure of certainty and early recovery not available in the litigation context. Similarly, in *Haney Iron Works Ltd. v. Manufacturers Life Insurance Co.*,[7] the Court found that the parties had to establish only a *prima facie* case for certification where settlement approval was sought. Therefore, a Court may decide that a case which ought not to be certified if the litigation were to proceed may still be certified for the purposes of settlement.

This issue did not arise in the YBM actions; Cumming J. simply found that the criteria of s. 5 of the *CPA* were met and that certification was appropriate.[8]

B The settlement must be fair, reasonable, and in the best interests of the class

To approve a settlement, the Court must find that it is "fair, reasonable, and in the best interests of the class". A proposed settlement must not be measured against a standard of perfection. Rather, the Court must balance the need to scrutinize the settlement against the recognition that there may be a number of possible resolutions that fall within the range of reasonableness. The Court must recognize that settlements are, by their nature, the product of compromise and need not (and usually will not) satisfy every single concern of all interested parties. A less than perfect settlement may be in the best interests of those affected by it when compared to the alternative of the risks and costs of litigation. The Court must, therefore, recognize the uncertainties of law and fact in any particular case and the concomitant risks and costs necessarily inherent in taking any litigation to completion.[9]

The resolution of complex litigation through the compromise of claims is encouraged by the Courts and favoured by public policy.[10] The practical value of an expedited recovery is a

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5 *supra,* note 4, paras. 27 - 35

6 (2002), 25 C.P.C. (5th) 363 (B.C. S.C.)

7 (1998), 169 D.L.R. (4th) 565 (B.C. S.C.)

8 *Mondor v. Fisherman*; *CC & L Dedicated Enterprise Fund (Trustee of) v. Fisherman*, *supra*, note 3, para. 15

9 See *Dabbs v. Sun Life Assurance Co. of Canada* (1998), 40 O.R. (3d) 429 (Gen. Div.) at pp. 440 and 444

10 *Ontario New Home Warranty Program et al. v. Chevron Chemical Company et al.* (1999), 46 O.R. (3d) 130 (S.C.J.) at p. 147, cited by Cumming J. in settlement approval decision, note 3, at para. 17

significant factor for consideration since it saves litigants the costs and risks associated with going to trial and reduces the strain on an already overburdened court system.

The parties proposing a settlement have an obligation to provide sufficient evidence to permit the Court to exercise an objective, impartial, and independent assessment of the fairness of the settlement in all the circumstances. One of the reasons for the Court's high level of scrutiny is that the usual safeguards of the adversarial process may not protect members of the class in negotiations between the representative plaintiffs and the defendants. Where the Court is satisfied that the settlement was negotiated at arms length by counsel for the class, particularly under the auspices of the Court, there is a strong initial presumption of fairness, which presumption will be overridden only if the judge concludes that the settlement does not fall within a range of reasonable outcomes.

In determining whether to approve a proposed settlement, the Court may take into account the following factors:

(1) the likelihood of recovery or likelihood of success;

(2) the amount and nature of discovery evidence;

(3) the settlement terms and conditions;

(4) the recommendation and experience of counsel;

(5) the future expense and likely duration of litigation;

(6) the recommendation of neutral parties, if any;

(7) the number of objectors and nature of objections;

(8) the presence of arms-length bargaining and the absence of collusion;

(9) the degree and nature of communications by counsel and the representative plaintiff with class members during the litigation; and

(10) the information conveying to the Court the dynamics of and the positions taken by the parties during the negotiation.[11]

These factors should be a guide in the process and it is not necessary that all factors receive the same consideration. In any particular case, certain of these listed factors will have greater significance than others and weight should be distributed accordingly.

Among the factors considered by Cumming J. in his Reasons for Decision approving the proposed YBM settlement were as follows:

- There are significant uncertainties of law and fact and, therefore, corresponding risks and costs inherent in pursuing litigation to trial [para. 20].

- There are particular problems inherent to any action in Canada based upon alleged misrepresentations relating to the purchase of shares in the secondary market. The law is fundamentally different in the United States [para. 21].

- There is a risk to class members in the General Class Action because of the necessity in Canada of proving individual, actual reliance upon the alleged misrepresentation [para. 22].

- The issue of the negligence of certain defendants (the lawyers and the auditors) may be problematical under the test in *Hercules Managements Ltd. v. Ernst & Young* (1997), 146 D.L.R. (4th) 577 (S.C.C.) [para. 23].

- The claim advanced in the General Class Action under the misleading advertising sections of the Canada *Competition Act* is novel and seems problematic and tenuous [para. 24].

- There is a risk that a portion of the statutory claim by the representative plaintiffs in the Prospectus Class Action might not succeed on the basis that their shares, purchased through a private placement and qualified and issued under the Prospectus, may not meet the statutory requirements. A limitation of actions

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[11] *Parsons v. The Canadian Red Cross Society* (1999), 40 C.P.C. (4th) 151 (S.C.J.) at pp. 172-173, paras. 71 and 73; and *Dabbs v. Sun Life Assurance Co. of Canada*, [1998] O.J. No. 1598 (Gen. Div.) at para. 13

defence, while doubtful, is raised with respect to all Prospectus claimants [para. 25].

- There is a risk that some or all defendants may not be liable in negligence due to their due diligence or the sophistication of the fraud [para. 26].

- The insurance policies available to some defendants provide that legal costs reduce the amount of coverage available [para. 27].

- Some of the defendants are claiming indemnity from YBM [para. 28].

- YBM's Receiver and Independent Litigation Supervisor recommend the proposed settlement [para. 29].

- There has been effective communication with class members through publication and mailing of the notice of the settlement approval hearing. Class counsel have met with some 20 institutional investors who are class members and who expressly support the settlement. The representative plaintiffs, including those in the U.S. Class Action, have all provided affidavits supporting the settlement [para. 32].[12]

Moreover, there was some evidence before the Court, not referred to in Cumming J.'s Reasons for Decision, that the estimated recovery of each shareholder was two to three times the average net recovery in the United States for a comparable level of global damages.

C Does the proposed settlement set out a workable plan?

The settlement proposal must provide an adequate plan for the resolution of the proceeding, or certification will not be ordered in the settlement context.[13] The Court should be presented with a complete proposal and will not become involved in rewriting terms for the parties. Before the settlement is approved, the Court must be satisfied that there is a workable procedure or plan for the administration of the settlement which makes clear who is responsible to do what, sets deadlines for the completion of all the necessary stages of the administration of

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12 *Mondor v. Fisherman*; *CC & L Dedicated Enterprise Fund (Trustee of) v. Fisherman*, *supra*, note 3, paras. 20-32.

13 *McKrow v. Manufacturers Life Insurance Co.* (1998), 9 C.C.L.I. (3d) 161 (Ont. Gen. Div.) at para. 8

the settlement, and anticipates potential problems or disputes. Someone must be identified as responsible for driving the settlement to completion so that it proceeds as quickly and cost-efficiently as possible.

The complexity (and, thereby, the cost) of the settlement will depend upon a variety of factors, including the number of class members, the estimated amount of each class member's claim, and the total amount of the proceeds available for distribution to the class members. A typical plan for the resolution of a proceeding in a class action settlement agreement should deal with the following issues, some of which are practical and some of which are required by the *CPA*.

(1) Requirements for certification

If the action has not already been certified at the time of settlement, the parties must include, in the formal Judgment approving the settlement, all the requirements for a certification order pursuant to s. 8 of the *CPA* and the Judgment should explicitly state that the action is certified as a class action.

For example, a clear definition of the class must be included in the certification order, pursuant to s. 8(1)(a) of the *CPA*, so that those who are entitled to a distribution can easily be identified and the defendants are protected from future claims.

The YBM Judgment contained a separate definition for the members of each of the classes of persons on whose behalf the class actions were brought to cover each and every person (except "excluded persons"), wherever resident, who either: (1) purchased or acquired shares pursuant to the Prospectus; or (2) who purchased shares in YBM - except pursuant to the Prospectus - during the entire period YBM shares traded (July 1, 1994 to May 14, 1998). "Excluded persons" was defined to mean most of the defendants and third parties. Therefore, the Judgment created two worldwide classes comprising all persons who held shares in YBM, except those who were parties defendant in the litigation.

The *CPA* also provides, in s. 8(1)(b) to (d), further matters that must be addressed in the certification order: the names of the representative plaintiffs; the nature of the claims advanced on behalf of the class; the relief sought by the class; and the common issues for the class.

(2) Appointment of administrator

Someone must be appointed to administer the settlement, who is usually paid out of the settlement funds. The administrator may be responsible to give notice to class members, provide class members with information on the progress of the settlement, hold the settlement funds pending their distribution to class members, receive claims from class members, make initial decisions about entitlement, and distribute the funds to each class member [s. 26 *CPA*]. Increasingly, the role of administrator is being assumed by a professional who or which is familiar with class actions and has some financial expertise that allows it to process claims, to ensure the funds are paid out in accordance with the settlement terms, handle taxation issues, and account to the Court. In fact, a new industry of consultants, which market themselves as experts or specialists in class action administration and management, has sprung up.

In the YBM matter, the Receiver was appointed as the Administrator. This enabled the administration of the receivership and the settlement to proceed as parallel processes, costs savings to be achieved, and inconsistent results avoided.

(3) Court oversight of settlement

Pursuant to s. 26(7) of the *CPA*, the Court must supervise the execution of judgments and distribution of awards under ss. 24 and 25. An important part of the settlement approval process in the YBM matter involved the appointment of Winkler J. to oversee the implementation of the settlement and distribution of settlement proceeds to class members. In accordance with the terms of the Judgment, a sub-committee of counsel, referred to as the Management Committee, was appointed by Winkler J. to oversee the completion of the settlement and obtain directions from the Court as necessary. Numerous orders have been made approving the various stages of the settlement administration process and the payment of the necessary expenses. However, in less complex settlement agreements, it may not be desirable or necessary to return to the Court for approval at various stages of the settlement process.

(4) Notification to class members

There must be a means to notify class members at three stages of the proceeding: of the fairness hearing so that objections to the proposed settlement may be heard; that the action has been certified and the settlement approved; and that class members have a right to opt out of the settlement. Deadlines must be imposed. Court approval of the contents of the notices is

necessary [s. 20 *CPA*]. The notice can be made by direct mailing, by publication in newspaper or trade/industry journals, or by other means. In should be borne in mind that newspaper notices published on only a few days can be surprisingly ineffective in reaching people. The Court must be satisfied that the notices are likely to come to the attention of class members, whatever means are used [ss. 17, 18, 19, 23, and 29(4) *CPA*].

The dissemination of information to class members can easily be done through a web-based data base, which allows class members to obtain information about the status of their claim and the progress of the administration of the settlement. In the YBM matter, notice was given directly to those shareholders whose names appeared in the YBM share registry, to those who had filed a proof of claim in the receivership proceedings, to a list of brokers in the United States and Canada, and to certain newspapers circulated widely. Notice was also given to the Public Guardian and Trustee and Children's Lawyer. Copies of all of the orders and proceedings relating to the settlement were posted on a publicly available website at www.ybmclassaction.com. Later, a direct link was made from this website to the Administrator's password-protected web-based data base, which contained information relating to the proof of claim process. Class members were also provided with a toll-free number to call to reach the Administrator. The internet email system was also used to serve court documents, as necessary, upon the numerous counsel involved.

(5) Procedure and date for opt outs

There must be a procedure and deadline for those shareholders who wish to opt out of the settlement [s. 8(1)(f) and 9 *CPA*].

A friend of the court may be appointed to represent the interests of anyone who either objects to the proposed settlement or, once the settlement has been approved and the class action certified, seeks advice as to whether to opt out. This enables objectors to have independent representation and ensures that the Court receives submissions from objectors in an organized and efficient way. If such a person is appointed, there must be provision for payment of that person, usually out of the settlement funds.

In the YBM case, a friend of the court was appointed, however, no class member objected to the settlement or chose to opt out.

(6) Proofs of claim

There must be a procedure for determining class members' claims. Common methods are proof of claim forms and affidavit evidence. There must also be time limit imposed upon potential class members for making claims [s. 24 *CPA*]. There must also be a procedure for appeals by class members of the decision as to eligibility and quantum of damages and someone must be designated to hear the appeals. Provision for payment of that person, usually out of the settlement funds, must be made.

The Judgment in the YBM matter contained, as a schedule, a plan for the determination by the Administrator of eligible persons entitled to be class members and the manner in which a distribution of the settlement monies was to be made to those eligible persons. It set out a proof of claim process, in which the Administrator made a determination of each claimant's eligibility, net loss, and membership in which class. Appeals of the Administrator's decision could be made to a court-appointed Referee in accordance with the procedure set out in a protocol prepared by members of the Management Committee and approved by Order of Winkler J. Information relating to a claimant's eligibility and calculated net loss were posted on the password-protected web-based database.

(7) How the settlement funds are to be paid and held

The proposed settlement agreement must indicate whether the settlement funds are to be paid in a lump sum, by installment over time, or such other method and by whom. The class members may share one finite fund or may be entitled to damages based upon a formula or mechanism. There are risks and benefits to plaintiffs and defendants to each method. The settlement agreement must provide for how the funds are to be held and by whom prior to their distribution to class members. There may be specific protocols or requirements regarding how those funds are to be invested for the benefit of class members.

In the YBM matter, the lump-sum settlement funds paid by the contributing defendants and third parties were paid to counsel for the Prospectus Class Action plaintiffs, to be used to pay the notice expenses approved by the Court and invested in accordance with a protocol prepared by members of the Management Committee and approved by Winkler J. and thereafter, turned over to the Administrator for investment. Essentially, the protocol provided for the settlement funds to be deposited into income generating, low-risk investments.

(8) The costs of administering the settlement

The plan must clearly state how the costs of the settlement are to be funded. Often, those costs come out of the settlement proceeds and the Court will require an estimate of those costs and an accounting after those costs have been incurred to ensure that they are reasonable.

In the YBM matter, the costs of providing notice to potential class members of the fairness hearing and, thereafter, costs of the certification of the class actions, were paid out of the settlement monies by Prospectus Class Action plaintiffs' counsel. The funds were then transferred to the Administrator, which was responsible for paying the further costs of administering the settlement and then distributing them to the class members.

(9) Distribution of settlement funds

The class members with proven claims may be entitled to a proportionate share of a settlement fund paid by the defendants or, alternatively, they may be entitled to damages based upon a mechanism or formula. In any event, the Court must be provided with sufficient information about each shareholder's loss as compared to the class member's expected return to be able to determine the fairness of the settlement. There should be provision for distribution of settlement funds (if any) that are not distributed to class members [s. 26(10)]. The settlement may provide that the funds are to be returned to the contributing defendants.

In the YBM action, the Receiver had some information about the identity of shareholders and the number of shares held by each shareholder, as a result of the company share register and the receivership proof of claims process, which was already under way at the time of the settlement of the class actions. This information was provided to counsel in the class actions and allowed a calculation to be made of the anticipated number of class members and their expected recovery. This information was also provided to the Court for the purposes of the approval motion and to potential class members to enable them to determine whether they wished to make objections to the proposed settlement or to opt out of the settlement. Thereafter, the Administrator made use of it for the notice and proof of claim processes. A distribution will be made based upon a shareholder's net loss, which is the cost of all shares purchased or acquired (including brokerage fees) minus proceeds of the sale or disposition of all shares (including brokerage fees).

(10) Legal fees

There must be court approval of plaintiffs' counsel's legal fees [ss. 32(2) and (3), and 33 of the *CPA*]. The fees often come out of the settlement proceeds. Therefore, an estimate of legal and administration costs must be provided to the Court for the fairness hearing.

(11) What event(s) triggers dissolution of the settlement?

If the class action has a multi-jurisdictional element, the settlement may dissolve automatically if the parties are unable to obtain "global peace", that is, a resolution of all litigation throughout the world. Defendants will undoubtedly want a settlement which achieves "global peace". Therefore, the parties may have to submit the proposed settlement for approval to Courts in other jurisdictions, which may have different approval criteria. In the YBM case, approval was required of the Alberta Court of Queen's Bench (which has jurisdiction over the distribution of YBM's assets under the receivership), the United States Court of Appeals for the Third Circuit (where the U.S. class action appeals were pending), and the Ontario Superior Court of Justice (where the two Canadian class actions were commenced).

The settlement may also dissolve if the number of class members opting out have claims which exceed a predetermined threshold amount. Usually this threshold amount is kept confidential to prevent some class members from holding the entire settlement hostage by trying to bargain for themselves more favourable terms in exchange for their agreement not to opt out.

In the YBM class actions, the Judgment provided that the settlement could be dissolved and the Judgment declared null and void upon the happening of certain events:

- not all of the contributing defendants and third parties contributed their proportionate share of the settlement monies;
- class members having claims of a certain amount (held confidential among counsel) exercised their right to opt out, unless this term was waived by the contributing defendants and third parties (referred to by Cumming J. in the YBM Reasons for Decision as the "blow up" clause[14]); or
- there was no dismissal of the U.S. appeal.

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[14] *supra,* note 3, para. 36

Upon the happening of any of these events, the settlement monies (less any costs already approved by the Court and paid) were to be returned to the contributing defendants and third parties. Once none of these events could occur, the Court made an Order declaring the Judgment in full force and effect.

(12) Further directions

The settlement must provide for the ability of parties or the administrator to seek further directions from the Court if some unanticipated issue arises. The Management Committee members in the YBM matter have dealt with such issues throughout the settlement administration. One of the issues that required direction from Winkler J. and a Court Order was what to do about class members who were otherwise eligible for a distribution except that they had submitted their proofs of claim after the Court-imposed bar date, after the priority distribution to class members of the Prospectus Class Action, or after the interim distribution to all class members. There were also taxation issues. The settlement monies were invested in accordance with a protocol referred to in the Judgment (prepared by the Management Committee and approved by Winkler J.) and, thereby, earned interest income. That interest income was allocated proportionately to each shareholder on the basis that, if it were taxed in the hands of the Administrator, the highest marginal tax rate would apply, while individual class members might have lower tax rates.

(13) Bar orders

Settlement discussions need not fall apart even if some defendants fail to participate or to offer to contribute. The parties may seek Court approval of a settlement with only some defendants through the use of a bar order, a mechanism borrowed from United States jurisprudence, which prevents further action for contribution and indemnity against defendants who have settled with the plaintiff by future defendants or non-settling defendants.[15] Winkler J. has found that the *CPA* contains authority for the use of a bar order in s. 13 (which permits stays of proceedings on such terms as the Court considers appropriate) and s. 12 (which permits the Court to make such orders as are necessary to ensure the fair and expeditious determination of the class proceeding). Making use of a bar order can be effective in ensuring

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[15] See, for example, *Ontario New Home Warranty Program v. Chevron*, *supra*, note 10; and *Sawatzlay v. Société Chirurgicale Instrumentarium Inc.*, [1999] B.C.J. No. 1814 (S.C.)

that a settlement reached by the representative plaintiffs and several of the defendants does not fall apart because other defendants are not prepared to participate or make any contribution.

No bar order was made in the YBM case and it cannot be known whether the possibility that such an order could be obtained provided a motivation for some defendants to participate in settlement discussions.

VII. ISSUES UNIQUE TO SECURITIES CLASS ACTIONS

There were several issues that arose during the course of the implementation of the YBM settlement, which were unique to securities class actions:

(1) duplicate claims

It soon became clear to the Administrator during the proof of claim process that it was in receipt of numerous duplicate claims, particularly on behalf of institutional shareholders. Claims were made, not only by shareholders, but also by the agents/brokers, trustees, custodians, or companies (in circumstances in which they were filing on behalf of the company pension plans).

(2) co-mingling of shares

It was necessary to account for the possibility that shareholders who purchased their shares pursuant to the Prospectus (and thereby were entitled to a *pro rata* portion of the $7.5 million priority payment) may have co-mingled their shares with other YBM shares purchased on the secondary market. In fact, no YBM shareholder kept his, her, or its Prospectus shares segregated. Part of the distribution protocol approved by Winkler J. provided for the calculation of Prospectus Class Action class members' net losses in these circumstances and their entitlement to the priority distribution.

(3) proof of shareholder status

The Administrator discovered that many shareholders were not able to provide trade slips or certificates confirming purchases or sales of YBM securities and, therefore, ultimately accepted copies of brokerage statements. Much reliance was placed upon affidavit evidence in support of claims.

(4) mergers/acquisitions of funds

In many cases, YBM shares were held in funds and it was unclear how a distribution of [1]settlement proceeds should be made within a fund. The manager of one fund indicated that it was able to identify the unit holders of the fund on May 14, 1998 (the date of the cease trade order when the YBM shares became valueless). It proposed to distribute the settlement proceeds to those unit holders in proportion to their holdings. Other fund managers said they had no such records and proposed simply to credit the settlement monies to the fund, even though there may have been a change in the unit holders over time. The result would, obviously, be that some unit holders who did not suffer a loss (because they did not hold units in the fund at the time of the loss) benefited from the settlement proceeds, while others who did suffer a loss (because they sold their units in the fund prior to the settlement distribution) would not be compensated. This issue was beyond the purview of the Court.

(5) shares held in RRSPs

Consideration was given to the treatment of settlement proceeds provided to class members who held their shares in RRSPs, if the RRSPs were collapsed before the distribution.

VIII. CONCLUSION

The YBM settlement provides a useful precedent for a settlement agreement in a securities class action where the parties are numerous, the legal issues complex, and the amounts at issue large. Obviously, the expenses involved in administering a settlement increase with its complexity. This must be balanced against the need to have specific, identifiable problems or issues addressed in advance since planning ahead reduces costs and delays. Innumerable variations to the structure of the YBM settlement can be made to address the many unique issues that arise in each class action so long as the statutory requirements of the *CPA* and the requirements set out in the jurisprudence are met.

Attachments: Order setting fairness hearing date
Notice of Certification
Plan of Distribution

September 9, 2003