A Thesis Regarding The Measurement of Damages As A Result of Misrepresentation In A Prospectus

By William E. McNally and Barbara E. Cotton*

Section 203 of the *Securities Act*, R.S.A. 2000, c. S-4 provides a civil remedy for misrepresentation in a prospectus but does not prescribe how damages are to be measured for breach of its provisions. Certain rules are prescribed, however. An underwriter is not to be liable for more than the total public offering price represented by the portion of the distribution underwritten by him.[1] The defendants are not to be liable for all or any portion of the damages that they prove do not represent the depreciation in value of the security as a result of the misrepresentation relied upon.[2] The amount recoverable is not to exceed the price at which the securities were offered to the public.[3] Beyond these statutory rules, a thesis must be constructed as to the general principles governing the measurement of damages. The need for a thesis becomes particularly acute within the context of a representative plaintiff proceeding /class action context.

As will be seen, the Alberta *Securities Act* both has its origins in the early statute law of England and was influenced by the "blue sky" legislation of the United States. The law pertaining to measurement of damages for misrepresentation in a prospectus has developed from seminal English cases dating from 1860, which law has been adopted and expanded on in Canadian jurisprudence. Further, measurement of damages within the specific context of a class action proceeding resultant from misrepresentation in a prospectus has been recently fine-tuned in American literature and jurisprudence. In developing a thesis with respect to the measurement of damages in a class action proceeding for misrepresentation in a prospectus, therefore, one can

---

1 s. 203(8)

2 s. 203(9)

3 s. 203(13)

* William E. McNally is the senior partner of McNally Cuming & Allchurch, Calgary, Alberta and practices extensively in the class action area; Barbara E. Cotton is the principal of Bottom Line Research & Communications, Calgary, Alberta.

arguably look to this early English jurisprudence, its development in Canadian law and the more recent American literature in order to draw general principles.

Upon this basis, a thesis with respect to the measurement of damages for misrepresentation in a prospectus can be constructed as follows:

(1) The proper measure of damages with respect to misrepresentation in a prospectus is the difference between the purchase money paid for the shares and what would have been a fair price to have been paid for the shares, (the "true value"), had the misrepresentation not been made.[4]

(2) The measure of damages is, in general, the difference between the contract price and the true value of the shares, valued as at the date of the contract of purchase. A corollary to this is that subsequent fluctuations in the value of the shares following disclosure of the misrepresentations, including a subsequent increase in the value of the shares, are irrelevant.[5]

4 *Davidson* v. *Tulloch* (1860), 2 L.T. 97; *Derry* v. *Peek* (1887), 37 Ch. 541, reversed in the result *Derry* v. *Peek* (1889), 14 A.C. 337

5 *McConnel* v. *Wright*, [1903] 1 Ch. 546; *Jamal* v. *Moola Dawood, Sons & Co.*, [1916] 1 A.C. 175; *Secord* v. *Global Securities Corp.* (2000), 81 B.C.L.R. (3d) 235; but see *Uncle Ben's Tartan Holdings Ltd.* v. *Northwest Sports Enterprises* (1974), 46 D.L.R. (3d) 280

(3) Provided that there is an intrinsic value of the shares as of the date of the contract of purchase, the measure of damages as a result of the misrepresentation will ordinarily be calculated as the price paid for the shares minus the value of the shares as of the date of disclosure of the misrepresentation. This is based on the principle that the plaintiff has a duty to mitigate his/her/its damages upon learning the true situation and sell the shares shortly after knowledge of the misrepresentation. This is also based on the principle that the market value of the shares as of the disclosure date is an accurate measure of the true value of the shares as of the date of the date of the contract of purchase, but for the misrepresentation.[6]

(4) The decrease in price of the shares as at the date of disclosure of the misrepresentation can also be influenced by other "investor risks"unrelated to the misrepresentation, such as the loss of a major contract by the company or the removal of the CEO under a cloud of suspicion. At common law the measure of damages should be the difference between the purchase price paid and the value of the shares as of the date of disclosure of the misrepresentation nonetheless, as the plaintiff would not have been subjected to these "investors risks" but for the misrepresentation. The "transaction date rule" is intended to avoid the difficulties in measuring damages resultant from investors risks.[7] But under the Alberta Act a defendant will not be liable for those "investors risks" that he/she/it can prove impacted the damages claimed.

---

6 *Allan* v. *McLennan* (1916), 31 D.L.R. 617; *Burke* v. *Cory* (1959), 19 D.L.R. (2d) 252; *Culling* v. *Sansai Securities Ltd.* (1974), 45 D.L.R. (3d) 456; *Kerr* v. *Danier Leather Inc*., [2001] O.J. No. 4000; *Dixon* v. *Deacon Morgan McEwen Easson et al.* (1993), 102 D.L.R. (4th) 1

7 *Smith Newcourt Securities Ltd.* v. *Scrimgeour Vickers and Citibank N.A.*, [1996] 3 W.L.R. 1051; *Dixon* v. *Deacon Morgan McEwen Easson et al.* (1993), 102 D.L.R. (4th) 1

(5) If the shares were worthless as of the date of the contract of purchase, however, because, for example, the company at the time of issuing the shares was insolvent, the measure of damages will be the full purchase price paid for the shares,[8] subject to the statutory requirement that the amount recoverable is not to exceed the price at which the securities were offered to the public.

(6) The full purchase price may also be recovered if: (a) the misrepresentation has continued to operate after the date of the purchase transaction so as to induce the plaintiff to retain the shares; or (b) the circumstances of the case are such that the plaintiff is, by reason of the misrepresentation, locked into the property.[9]

---

8 *Derry* v. *Peek* (1887), 37 Ch. 541, reversed in the result *Derry* v. *Peek* (1889), 14 A.C. 337; *Twycross* v. *Grant* (1877), 2 C.P.D. 469; *Broome* v. *Speak*, [1903] 1 Ch. 586; *Fawcett* v. *Johnson* (1914), 15 N.S.W. State Rep. 51; *Burke* v. *Cory* (1959), 19 D.L.R. (2d) 252

9 *Smith Newcourt Securities Ltd.* v. *Scrimgeour Vickers and Citibank N.A.*, [1996] 3 W.L.R. 1051

(7) If the plaintiff has sold his/her/its shares, the defendant must be credited with the amount received.[10]

(8) A sophisticated econometric formula to ascertain damages in a class action context for misrepresentation in a prospectus has been developed in American jurisprudence and literature on the basis of the "fraud on the market theory". This formula applies a "value-line" framework. Although the "fraud on the market theory" has been rejected as a basis of liability in Canadian jurisprudence, this rejection has been primarily on the basis that, in Canada, one is required to prove reliance, and the "fraud on the market theory" deems reliance. There are differences in approach in that the American econometric formula factors in the market value of the shares as of the date of disclosure of the misrepresentation(s), and does not appear to provide a vehicle for recovery of the full purchase price paid unless the value of the shares has bottomed-out to zero as of the date of disclosure of the misrepresentation. Moreover, the American econometric model factors in the impact of "investors risks", thereby reducing recovery. Notwithstanding this seeming Canadian rejection of the American "fraud on the market theory", it is arguable that the Canadian rejection can be limited to the objectionable features of the theory, such as deemed reliance. The utility of the econometric formula flowing from this theory should be imported into Canada as a sophisticated aide to measurement of damages in a class action context.

What, then, can we look to for proof of this thesis?

---

10 *Twycross* v. *Grant* (1877), 2 C.P.D. 469; *Smith Newcourt Securities Ltd.* v. *Scrimgeour Vickers and Citibank N.A.*, [1996] 3 W.L.R. 1051

A Brief History of Securities Regulation

Much of the following discussion, which is intended to prove the above set out thesis as to the general principles governing the measurement of damages under s. 203 of the Alberta *Securities Act*, will look to early English authority. The discussion will then turn to a review of American literature and will postulate that the formulas developed in American literature and jurisprudence on the basis of the "fraud on the market theory" of securities regulation can be helpful in fine-tuning the measurement of damages under the Alberta Act. It is therefore necessary to review the history of securities regulation and the influence of English and American regulation on the development and evolution of the Alberta *Securities Act*, and, more particularly, the development of the civil liability provisions for misrepresentation in a prospectus, in order to provide a foundation for a thesis as to the measurement of damages under s. 203.

A broad view of the history of securities regulation can be gained from the esteemed sources of J. Peter Williamson, *Securities Regulation in Canada;*[11] Louis Loss, *Fundamentals of Securities Regulation*[12] and David L. Johnston, *Canadian Securities Regulation.*[13] In these sources

[11] (Toronto: University of Toronto Press, 1960)

[12] (Boston and Toronto; Little Brown and Co., 1983)

[13] (Toronto: Butterworths, 1977)

the history of securities regulation is traced back to an English statute of 1285 which authorized the licensing of stockbrokers in the City of London. Except for the provisions with respect to licensing of brokers, securities legislation is not more than 100 years old.

Williamson notes that there are two philosophies underlying securities regulation, the first being the principle of full disclosure, which allows for the sale of shares provided that the full truth is told. This principle of full disclosure is the basis of the prospectus provisions in the English and Canadian securities legislation, as well as the United States *Securities Exchange Act* of 1933 and 1934. The second type of securities legislation is the so-called "blue sky" regulation, which involves the imposition of standards of conduct on securities issuers going beyond disclosure. (Louis Loss states that the term "blue sky" originated in Kansas with the enactment of its legislation in 1911. The term came into general use to describe the legislation as being aimed at promoters who "would sell building lots in the blue sky for a fee simple".[14]

Modern securities regulation began in England in 1844 with the *Joint Stock Companies Act*.[15] This Act enacted the first modern prospectus requirements and introduced the principle of compulsory disclosure through the registration of a prospectus. There was some backtracking from this legislation but the principles were again affirmed in the English *Companies Act, 1867*.[16] The Act required that all parties to contracts with the company be disclosed and deemed that a failure to disclose such contracts would be fraudulent on the part of the promoters, directors and officers of the company as regards persons taking shares in the company on the basis of the prospectus.[17]

---

14 *Supra*, p. 8

15 1844, 7 & 8 Vict., c. 110

16 1867, 30 & 31 Vict., c. 131

17 *Ibid*, s. 38

The next development led to the establishment of the first civil liability provisions. In the famous case of *Derry* v. *Peek,*[18] the House of Lords had found a director not liable for untrue statements in a prospectus because the director had believed in good faith the truth of the statements, notwithstanding how unreasonable the good faith belief was. Thus the English court required proof of intent to defraud as a requirement for the recovery of damages resulting from a misrepresentation in a prospectus.[19] The English Parliament replied with the *Directors Liability Act, 1890,*[20] which imposed upon every director and promoter liability for loss sustained by reason of an untrue statement in a prospectus to anyone who subscribed for securities on the basis of the prospectus. Liability was not absolute and a test of reasonable belief or reliance was introduced. This provision survives in a modified form in present day companies and securities legislation in Canada and in the United States *Securities Exchange Act* of 1933.[21]

The *Directors Liability Act* was later incorporated into the *Companies (Consolidation) Act, 1908*.[22]

The English *Companies Act, 1900*[23] introduced an elaborate prescription for the contents of a prospectus, and thus modern disclosure requirements.

Johnston states:[24]

---

[18] (1889), 14 A.C. 337

[19] Johnston, p. 11

[20] 1890, 53 & 54 Vict., c. 64

[21] Williamson, p. 5

[22] 1908, 8 Edw. 7, c. 69

[23] 1900, 63 & 64 Vict., c. 48

[24] at p. 9

> Securities regulation as we know it today in Canada has evolved through various statutes. A list of these would include laws relating to the incorporation of companies, the reporting of information by companies, the sale of shares, securities fraud prevention, and the licensing of brokers, with the final product of this evolution being comprehensive securities acts. In tracing this development one may adopt as a framework the three techniques of regulation: . . . registration of persons, registration of securities and anti-fraud measures. All three have their roots in English antecedents. More recently they have been influenced significantly by federal and state legislation in the United States.

With minor exceptions, early Canadian securities regulation consisted of importing provisions from the English Acts. The first general incorporation statute for Canada was the *Canada Joint Stock Companies Letters Patent Act, 1869.*[25] Further Acts such as *The Companies Act*[26] and *The Companies Act Amendment Act* of 1917[27] followed. The 1917 Act imported the prospectus requirements and the provisions with respect to the civil liability of directors and promoters from the English *Companies (Consolidation) Act, 1908*. In s. 7, which amended s.43 of the Revised Statute of Canada 1906, liability was imposed on directors and promoters with respect to all persons who subscribed for shares on the faith of the prospectus for loss or damage resulting from an "untrue statement", subject to listed defences, including reasonable belief or reliance. The 1917 Act did not define "untrue statement".

In 1891 Ontario became the first Canadian jurisdiction to adopt the provisions of the English *Directors Liability Act* pursuant to the *Directors' Liability Act, 1891*[28] and introduce civil liability for directors and promoters for misrepresentation in a prospectus. This Ontario statute is interesting because it defined "untrue statement" to include a concealment or an intentional non-

---

[25] 1869, 32-33 Vict., c. 13

[26] R.S.C. 1906, c. 79; S.C. 1908, c.16; S.C. 1914, cc. 23, 40 and 55

[27] S.C. 1917, c. 25

[28] S.O. 1891, c. 34

disclosure of a material fact known to the director or promoters.[29] In 1907 Ontario enacted the *Companies Act,*[30] which drew on the English *Companies Act* of 1900 with respect to the prospectus requirements[31] and continued the civil liability provisions for untrue statements in a prospectus.[32]

---

[29] s. 2(1)

[30] R.S.O. 1907, c. 191

[31] ss. 95-99

[32] s. 102

The first securities legislation to introduce a comprehensive licensing requirement was the "blue sky" legislation enacted in Kansas in 1911.[33] This Kansas legislation required registration of securities and issuers and set the pattern for early Canadian securities legislation. Within two years Manitoba and Saskatchewan had adopted acts copying the Kansas statute.[34] Alberta followed in 1916 with *The Sale of Shares Act*.[35]

When Alberta became a province in 1905 it inherited the ordinances of the Northwest Territories, which included *The Companies Ordinance* of 1901.[36] In 1914 Alberta added to the prospectus requirements of the Ordinance to forbid the allotment of securities to the public until a prospectus had been filed with the registrar.[37] In 1929 the concept of a private company was introduced in Alberta and a company could not commence business or allot shares until a prospectus had been filed or, if there was no public offering, until a statement had been filed in lieu thereof.[38] In a detailed provision civil liability was imposed on directors and promoters for untrue statements in a prospectus, subject to listed defences, including reasonable belief and reliance.[39]

Ontario had two statutes in place in the 1920s, *The Security Frauds Prevention Act, 1928*[40], aimed at controlling traders in securities rather than the issue of securities, and *The*

---

33 1911, c. 133

34 *The Sale of Shares Act, 1912,* S.M. 1912, c. 75 and *The Sale of Shares Act, 1914,* S.S. 1914, c. 18

35 S.A. 1916, c.8

36 *Consolidated Ordinances of the North-West Territories,* 1901, c. 20

37 *The Companies Ordinance Amendment Act of 1914,* S.A. 1914, c. 10

38 *The Companies Act, 1929*, S.A. 1929, c. 14; Williamson. p. 15

39 s. 86

40 S.O. 1928, c.34

Companies Information Act, 1928[41], which dealt with disclosure requirements and was a significant advancement. *The Security Frauds Prevention Act, 1928* became the model for uniform statutes adopted in almost every province by 1930. The Act was innovative in that it began with a declaration as to what constituted fraud, such as intentional misrepresentation and intentional omission of material facts, promises as to the future which were beyond reasonable expectations or not made in good faith, fictitious trades, *etc*.[42]. There was no attempt to create civil liabilities based on these "fraudulent" acts and they remained punishable by fines or imprisonment.[43]

Representatives from Alberta, British Columbia, Manitoba, Ontario, Quebec and Saskatchewan met to draw up uniform securities legislation, and the uniform Act was enacted in Alberta in 1930 as *The Alberta Security Frauds Prevention Act*, 1930.[44] The Alberta Act defined "fraud", "fraudulent" and "fraudulent act" to mean "any intentional misrepresentation by word, conduct or in any manner of any material fact either present or past, and any intentional omission to disclose any such fact" and "any promise or representation as to the future which is beyond reasonable expectation and not made in good faith", *inter alia*.[45] Breach of the Act was punishable by penalty.[46]

An equivalent English *Protection of Fraud (Investments) Act, 1939*[47] was passed which required dealers and salesmen to be licensed by the Board of Trade. This was replaced by the

41 S.O. 1928, c. 33

42 s. 2(c)

43 s. 16; Williamson, pp. 21, 22

44 S.A. 1930, c. 8

45 s. 2(c)

46 s. 20

47 1939, 2 & 3 Geo. 6, c.16

Prevention of Frauds (Investments) Act, 1958.[48] These Acts made it an offence for any person to make a false, misleading, deceptive or dishonest forecasts, statements or promises which induced or attempted to induce another to invest money. Breach of these provisions was punishable by penalty.[49]

Again taking the lead, Ontario enacted *The Securities Act, 1945*[50] which is considered the first modern Canadian Securities Act. In this Act Ontario consolidated its various statutes relating to the licensing of brokers and salesman and the filing of prospectus'. In this Act a broker or salesman was obliged to deliver to a purchaser a statement containing the company's balance sheet, profit and loss statement and statement of the property owned by the company before sale of a security.[51] The purchaser was entitled to the remedy of rescission if this statement was not provided.[52] Rescission was also a remedy if the broker failed to give notice that he was also acting as a principal.[53]

---

48 1958, 6 & 7 Eliz. 2, c. 45

49 See L.C. Gower, *Review of Investor Protection, A Disclosure Document* (Her Majesty's Stationery Office, London, 1982)

50 S. O. 1945, c. 22

51 s. 55

52 s. 56

53 s. 63

Alberta followed the Ontario lead in 1955 with the enactment of *The Securities Act, 1955*.[54] This Act required the licensing of brokers and salesman and established the Alberta Securities Commission. Rescission was a remedy if a broker failed to give notice he was acting as a principal,[55] and a brokers notice of financial interest also had to be given.[56] The Act specifically prohibited the making of any representation, either written or oral, that any person or company would resell or repurchase a security or refund any or all of the purchase price. There was also a prohibition against the giving of an undertaking, written or oral, relating to the future value or price of the security. Further, a representation that the security would be listed on any stock exchange was prohibited.[57] Offences under the Act were punishable by penalty.[58] Most significantly, the Act incorporated civil liability provisions for "material false statements" in prospectus'.[59] This provision further deemed reliance on statements made in a prospectus by every purchaser of the securities to which the prospectus related.

In 1957 the Alberta *Investments Contract Act*[60] placed the regulation of investment contracts under the authority of the Securities Commission. This Act also was largely based on an Ontario Act. The Act required issuers and salesmen to register, specified the filing of information and permitted investments and "generally (parallelled) the securities acts in greatly simplified form".[61]

---

[54] S.A. 1955, c. 64

[55] s. 83

[56] s. 84

[57] s. 81

[58] s. 97

[59] s. 102

[60] S.A. 1957, c. 36

[61] Williamson, p. 34

In 1963 the Kimber Committee was established in Ontario. Kimber, the then head of the Ontario Securities Commission, was commissioned to recommend up-to-date securities legislation. The proposals of the Kimber Committee in the "Report of the Attorney General's Committee on Securities Legislation in Ontario" in 1965 were implemented almost in their entirety in the *Securities Act, 1966*[62] which became effective early in 1967. Substantially uniform statutes were adopted in Manitoba, Saskatchewan, Alberta and British Columbia. The Kimber Report also influenced the amendment of the Canada *Corporations Act*. The then securities statutes of the four Atlantic Provinces formed another separate uniform group, based on what prior to 1966 was a national model. Quebec's statute was a hybrid based on the earlier national model to which had been grafted the principal features of the 1966 uniform act.[63]

---

62 S.O. 1966, c.142

63 Johnston, p. 8

The Alberta *Securities Act*, modified to reflect the work of the Kimber Committee, was enacted as *The Securities Act, 1967*.[64] The Act set out the requirements for a prospectus [65]and provided the remedy of rescission if the prospectus contained an untrue statement of material fact or if it omitted to state a material fact.[66] A civil liability provision for insider trading was introduced.[67] Offences under the Act were punishable by penalty.[68] Civil liability was imposed on directors and those persons or companies who signed the prospectus certificate (the chief executive officer, the chief financial officer, promoters and others) for "material false statements" contained in the prospectus, subject to listed defences. There was deemed reliance on a material false statement in the prospectus.[69]

Codification of the civil liability provisions under one Part of the *Securities Act* was introduced by way of Alberta Bill 76,[70] which was allowed to die on the order paper after first reading in order to allow the securities industry an opportunity to examine the proposed sections. The Minister, Mr. Harley, in introducing the bill, stated that it was patterned after legislation which was passed in Ontario upon the general notion that there should be uniformity across Canada in securities legislation.[71]

---

64 S.A. 1967, c. 76

65 s. 43

66 s. 64

67 s. 113

68 s. 136

69 s. 141

70 4th Sess., 18th Legis., November, 1978

71 Alberta Hansard, November 1978, p. 1643; Robert L. LeClerc, "Civil Liability on Distributions under the *Securities Act*, *1978* (Bill 76)", (Legal Education Society of Alberta, 1979); J.S. Burns, "Overview of the *Securities Act*", (Legal Education Society of Alberta, 1979)

Bill 76 again reflected Alberta following the legislative lead of Ontario. In 1972 and 1974 Ontario introduced "exposure draft" bills which were intended to consolidate various amendments to the uniform act which had accumulated since 1966. In addition, the bills were based on three major law reform reports, including the 1973 Ontario Select Committee On Company Law report. These draft bills were discussed in detail with the other nine provinces. The legislation was further refined and became *The Securities Act, 1978*.[72]

The new Part of the Alberta Act codifying the civil liability provisions, Part 16, and introducing s. 168 were introduced in Alberta in 1981 with the enactment of the *Securities Act, 1981*.[73] Section 168 was a much more expansive civil liability provision that than of the 1967 Act. Section 168 specifically itemized who could be sued for damages, including the directors, the underwriters, the issuer and selling security holder on whose behalf the distribution was made, every person or company who signed the prospectus and those whose consent had been filed. The deemed reliance provision was continued. The phrase "material false statement" was changed to "misrepresentation". The purchaser was given a right to elect rescission against a person, company or underwriter, in which case he/she would have no right to damages. Certain defences were listed, substantially similar to those of the 1967 Act. Certain damages assessment rules were set out. A purchaser of securities on the basis of misrepresentation was expressly given the right to rescission and damages, which were not to derogate from any other right the purchaser had at law.

Section 168 was amended on several occasions,[74] but not substantively. The 2000 revision to the Statutes of Alberta[75] essentially continued the substantive provisions. Part 16 became Part 17 and s. 168 became s. 203. Section 203(2) more particularly identified that a purchaser had a

---

72 S.O. 1978, c. 47; Johnston, pp. 6, 7

73 S.A. 1981 s. S-6.1

74 1984, c. 64, s. 49; 1988, c. 7, s. 1(42); 1995, c. 28, s. 62

75 R.S.A. 2000, c. S-4

right of rescission against an issuer or selling security holder on whose behalf the distribution was made, each underwriter who was required to sign the certificate and any other underwriter of the securities. In all other respects the section remained the same.

It has been suggested that the Kimber Committee Report, and the subsequent *Ontario Securities Act, 1966*[76] were largely influenced by the *Securities Act* of 1933 and the *Securities Exchange Act* of 1934 in the United States. The *Securities Act* of 1933[77] primarily required that a company issuing securities to the public disclose all material facts relating to the company and to the securities then being issued. One year later the *Securities Exchange Act* of 1934[78] was enacted which broadly prohibited any person from engaging in fraudulent activity in connection with the purchase or sale of securities. In 1942 Rule 10b-5 was promulgated by the Securities Exchange Commission and extended the effect of the provision beyond brokers and dealers and made the prohibitions apply generally to individuals and companies. Civil remedies were provided for in this legislation[79] and have been fashioned by the courts with the goal of furthering the purposes of the legislation, and include rescission, damages, injunctive relief, the appointment of receivers and attachment proceedings.

---

[76] S.O. 1966, c. 142

[77] 48 Stat. 84

[78] 48 Stat 891

[79] For example, the right to rescission created in s. 12(2) of the 1933 Act; the remedy under the 1934 legislation is said to be implied

In 1956 the National Conference of Commissioners on Uniform Statute Laws and the American Bar Association promulgated a new Uniform Securities Act, drafted by Louis Loss. The Uniform Act was then adopted by 36 states, the District of Columbia and Puerto Rico. The First Part of the Uniform Securities Act outlawed fraudulent practices in connection with the sale or purchase of a security. There was no civil liability imposed under this Part, but provision was made under Part IV for civil liability in the case of sales made through fraud or misstatement.

In 1995 the *Private Securities Litigation Reform Act*[80] was enacted which included an new provision which imposed a limitation on the calculation of damages in private actions under the 1934 Act. Typically in an action under the 1934 Act the investor's damages were presumed to be the difference between the price the investor paid for the security and the price of the security on the date the corrective information was disseminated to the market. The 1995 Act introduced a "look back" provision which required that the damages be calculated based on the "mean trading price" of the security. The calculation took into account the value of the security on the date the plaintiff originally bought or sold the security and the value of the security during the 90 day period after dissemination of any information correcting the misleading statement or omission. The intention was to limit damages to those losses caused by the fraud and not by other market conditions.[81]

Thus it can be seen that the modern Alberta *Securities Act* and the civil liability provisions for misrepresentation in a prospectus both have their origins in the early statute law of England, and more particularly in the *Directors Liability Act, 1890*, and were influenced by the "blue sky" legislation of the early Kansas and 1933 and 1934 federal statutes, both directly and through the Kimber Committee report. For these reasons the early English law which established general principles for the measurement of damages should be persuasive in constructing a thesis as to

---

80 109 Stat. 737, 749-50

81 Per Lewis D. Lowenfels and Alan R. Bromberg, "Compensatory Damages in Rule 10b-5 Actions: Pragmatic Justice or Chaos?", (2000), 30 *Seton Hall L.Rev.* 1083

measurement of damages for misrepresentation in a prospectus, as should arguably be the American law regarding measurement of damages developed from the "fraud on the market theory".

Proof of the Thesis Through the Case Law

Many of the cases that we will be subsequently discussing deal with deceit, which is analogous to fraudulent misrepresentation, and not negligent misrepresentation. These cases are of relevance, however. The recent case of *Toronto-Dominion Bank* v. *Leigh Instruments Ltd. (Trustee Of)*,[82] per Winkler J. of the Ontario Court of Justice (General Division)[83] states[84] that the measure of damages is the same for fraudulent misrepresentation and negligent misrepresentation. This principle is also implicitly affirmed by S.M. Waddams in *The Law of Damages.*[85]

---

82 [1998] O.J. No. 2637

83 affirmed at (1999), 45 O.R. (3d) 417

84 at page 101

85 (Aurora, Ontario: Canada Law Book Inc., looseleaf ed.), at p. 5-19

In reviewing the case law we intend to take a chronological historical view. This is because the principles established in the late 1800's have been consistently applied to today's date. Thus, the recent case of *Kerr* v. *Danier Leather Inc*.[86] per Cumming J. of the Ontario Superior Court of Justice, in discussing how a damage assessment can be made in a class action context for misrepresentation in a prospectus, in practice applies the general principles that have been established through the last century, (although he does not in fact reference any case law).

Damage assessment for misrepresentation in a prospectus can be seen to date back to 1860 with the case of *Davidson* v. *Tulloch*.[87] In this case an action was brought by the executors of the shareholder Tulloch against the executors of the deceased director Davidson to recover damages for fraudulent misrepresentations which induced Tulloch to purchase shares in the Aberdeen Bank, *inter alia*. The bank issued new shares and in the subscription contract described the business of the bank to be banking only, that regular books would be kept, that meetings would be at stated times, etc. Davidson was employed as director to prepare the new subscription contract and took an active part in preparing the reports and statement submitted to the shareholders. The plaintiff alleged that Davidson fraudulently promoted the private interests of himself and his friends by making large advances out of the funds of the bank without any security being given. Further, Davidson knowingly and wilfully concealed from the shareholders knowledge of the large amounts of debts incurred and the unsecured advances made and misrepresented the state of the bank's affairs. Sums were lost in the amount of £521,727. The subscription contract described the business of the bank in "flattering" terms and falsely described it as being in prosperous circumstances.

---

86 [2001] O.J. No. 4000

87 (1860), 2 L.T. 97

Tulloch purchased ten shares in the bank at £100 each, which was then the current price for the shares. The bank became insolvent.

The Lord Chancellor stated:[88] "The proper mode of measuring the damages clearly is, to ascertain the difference between the purchase-money and what would have been a fair price to be paid for the shares in the circumstances of the company at the time of the purchase; and that may be made the measure of damages if a trial should take place." Lord Brougham similarly stated:[89] "The difference between what he paid, and what, in the circumstances of the case the real value of the shares was, is the amount of damage which he sustained; and no greater amount can he recover."

The leading early case is *Derry* v. *Peek*.[90] This case is, of course, the famous case dealing with the elements required to prove fraud.

In this case the Act incorporating a tramway company provided that the carriages might be moved by animal power, and, with the consent of the Board of Trade, by steam or other mechanical power. The directors expected that they would obtain without difficulty the consent of the Board of Trade to use steam or mechanical power. They therefore issued a prospectus in which they stated that by their special Act the company had a right to use steam power instead of horses. The plaintiff bought shares on the basis of this prospectus and stated in his evidence that he was induced to take the shares by the statement that the company had the right to use steam power, *inter alia*. The Board of Trade in the result refused to sanction the use of steam power, and the company was wound-up. The plaintiff sued the directors, claiming damages for misrepresentation in the prospectus. The trial judge dismissed the action, but this was overturned by the English Court of Appeal, with the leading decision being written by Cotton L.J. In the result the English Court of

---

88 at pp. 98, 99

89 at p. 99

90 (1887), 37 Ch. 541 (English Court of Appeal), overturned in the result by the House of Lords at (1889), 14 A.C. 337

Appeal was overturned by the House of Lords because they held that the directors had made the statements in good faith. This in turn was addressed by the English *Directors Liability Act* of 1890, which imposed liability upon directors in certain circumstances.

It is the comments of Cotton L.J. with respect to the appropriate measure of damages which have been consistently applied. Cotton L.J. stated:[91]

> "That being so, the Defendants must be held liable. It is not that I attribute to them any intention to commit fraud, but they have made a statement which was incorrect, to induce the Plaintiff to act upon it without any sufficient reason for making that statement, without any sufficient reason for believing it to be true. Therefore they are liable. Then what ought the judgement to be? It is said on the part of the Defendants that the Plaintiff has not made out what the loss is. Well he has made out a *prima facie* case: that is to say, he has shewn, I think, on the evidence that the shares are of a very much less value than the sum which he gave for them. He gave £4,000, and the company is being wound up. There was a witness, though only one, who said that the shares, which are £10 shares, are not worth more than £5. I think the Defendants are not bound by that; but what I think is the proper course will be to declare that the Plaintiff was induced by a misstatement in the prospectus to take the shares and that the Defendants are liable under the circumstances for any loss which he has sustained by taking the shares, <u>and that will be the difference between the sum given for the shares, £4,000, and the value of the shares</u>." (Emphasis added.)

91 at pp. 578, 579

And further in the judgement[92] Cotton L.J. stated:

> "Now, it must not be taken that the value of the shares must be what they would have sold for in the market, because that might not shew the real value at all. I do not know whether there was any market in this case, but the market might have been affected by the representations which were made by the Defendants, which induced the Plaintiff to act, and which might have induced others to act. Neither can the Plaintiff get the benefit of any loss or depreciation in the shares which was occasioned by subsequent acts. If the company at the time was a good company and the shares had an intrinsic value, then no fact which subsequently occurred, as for instance, some Act of Parliament being passed to prevent such tramways from using steam-power, or anything else, ought to add to the damages to be paid by the Defendants . . . Although the value of the shares is not to be ascertained at this subsequent period so as to take into account for the benefit of the Plaintiff events subsequent which depreciated their value, yet those events, if they shew that the company was originally, with the capital which it had got, a company which was worthless, may, in my opinion, be taken into account as evidence of what was the value of the shares immediately after they were allotted to the Plaintiff." (Emphasis added.)

Thus *Derry* v. *Peek* introduced the concept that a plaintiff shareholder can claim the full amount of monies that he/she/it paid for the shares if the company was worthless at the time that the shares were purchased.

[92] at pp. 591, 592

This concept was further developed in *Twycross* v. *Grant*[93] a decision of the English Common Pleas Division, Court of Appeal. In this case the plaintiff sued to recover the amount of money paid by him on shares in the Lisbon Steam Tramway Companies. He alleged fraud on the part of the promoters of the company in omitting from the prospectus two contracts entered into by them as promoters. One contract was between the defendants for the purchase of certain foreign concessions for the construction of tramways which the company was afterwards incorporated to make and the other contract was between the defendants as to certain payments to be made by them in consideration of them obtaining a contract from the company for the construction of the tramways. These contracts were found by the jury to have been material and should have been made known to the intended shareholders in the prospectus. The jury awarded the plaintiff damages of the $700 he had paid for 70 shares in the company and this verdict was upheld by Lord Coleridge C.J. of the Common Pleas Division.

In an oft-quoted passage Lord Coleridge C.J. stated:[94]

> “. . . But the fact that they were quoted at a premium on the Stock Exchange is only evidence of value, not proof of it; and if the jury thought . . . that the quotation on the Stock Exchange did not shew a real, but only a delusive value caused by the fraudulent nature of the prospectus and the mode in which the shares were manipulated by the defendants and others in concert with them, the jury were not only justified in disregarding, but were bound to disregard, such delusive

---

93 (1877), 2 C.P.D. 469

94 at pp. 489, 490

> and factitious value; although, of course, if the plaintiff had sold his shares, he must have credited the defendants with whatever he might have realized by the sale. There is no evidence whatever that the shares ever had any value except that which resulted from the wrongful acts of the defendant; and it would be contrary to all principle to allow them to take advantage of their own wrong, and claim credit for the market price of the shares, when but for their own concealment of the contracts in question there is no reason to suppose that the shares would have had any market value at all . . ."

This was affirmed on appeal, with Cockburn C.J. of the Court of Appeal stating:[95]

> "I should agree that the law as just stated should have been pointedly brought to the attention of the jury with a view to the damages, could I find in the facts of the case any materials to which it would be applicable. But I find none. The shares were wholly valueless at the time the action was brought. They were so when the company was put an end to. In fact they were so from the beginning, from radical defects inherent in the project from its birth. The project failed as it first proposed, because difficulties were found to exist which it would have required too great an expenditure of capital to overcome; in its second form, to which, be it observed, the defendants were equally parties, because the traffic was insufficient to afford a remunerative return. The shares may have had for a time some factitious value in the share-market; but the plaintiff, having invested, was not bound to sell, but was fully entitled to wait until the lines were actually worked. When practically tested the enterprise failed, and the shares proved worthless. The measure of damages is, consequently, the price the plaintiff was induced to give for them by the statutory fraud on which the action is founded."(Emphasis added.)

[95] at p. 545

A similar point was made in *Broome* v. *Speak*.[96] In this case the directors of a newly incorporated company entered into a contract by letter with Broome, as promoter, that, in consideration of Broome advancing a sum of £14,250 to enable the company to pay the deposit on its intended purchase of an undertaking introduced by Broome, and of Broome taking upon himself the risk of forfeiture of the deposit in the event of non-completion of the purchase, the company would repay the deposit by a certain day together with a bonus. The deposit was then raised by Broome and paid to the vendors. Subsequently, by way of another contract, the initial contract was cancelled. The directors then issued a prospectus stating that certain contracts therein specified were the only contracts entered into by the company, without making reference to the contracts with Broome. The plaintiff applied for 400 £10 shares in the company. The company went into liquidation and the plaintiff brought an action against the directors claiming damages resultant from the fraudulent misrepresentation in the prospectus.

The English Court of Appeal held that the contracts should have been specified in the prospectus and that the plaintiff was entitled to damages. The court measured the damages, on the authority of *Derry* v. *Peek,* as being the difference between the price the plaintiff paid for the shares and the fair value of the shares at the date of allotment.

Buckley J. stated:[97]

> "The result of this is that the plaintiff is entitled to damages as against all the defendants. <u>The measure of damages is well fixed. It is the difference between the price which the plaintiff paid for the thing, and the fair value of the thing at the date at which he got it. But, in determining that fair value, regard is to be had to subsequent events</u>. That was laid down in *Peek* v. *Derry* in the Court of Appeal, and Cotton L.J. says: "Nor do I think he ought to be precluded from taking into account the subsequent events. Although the value of the shares

[96] [1903] 1 Ch. 586

[97] at p. 605

> is not to be ascertained at the subsequent period so as to take into account for the benefit of the plaintiff events subsequent which depreciated their value, yet those events, if they shew that the company was originally, with the capital which it had got, a company which was worthless, may, in my opinion, be taken into account as evidence of what was the value of the shares immediately after they were allotted to the plaintiff." The question is not answered by finding what was the market value of the shares at the date of allotment. It may be that the market value was raised by the very misrepresentation of which the plaintiff complains. You have to see what was the fair value at that time, and that has to be answered as best you may. It is a difficult question to answer, no doubt."
>
> In the result an inquiry as to damages was ordered.

A controversial case, subsequently impugned by the Supreme Court of Canada in *Hodgkinson* v. *Simms*[98] is *Waddell* v. *Blockey*,[99] a decision of the English Court of Appeal. In this case Lutscher ordered the defendant to buy rupee paper for him. The defendant sold rupee paper of his own to Lutscher, while he fraudulently led Lutscher to believe that he had sold him rupee paper belonging to third persons. The value of rupee paper afterwards became considerably less, but Lutscher continued to hold the rupee paper that the defendant had sold him for many months, and ultimately resold it at a loss of £43,000. In the result the measure of damages resultant from the fraudulent misrepresentation was held to be not the ultimate loss sustained by Lutscher, but the difference between what he paid for the rupee paper and the price which he would have received if he had resold it in the market soon after having learned of the misrepresentation.

---

98 [1994] 3 S.C.R. 377

99 (1879), 4 Q.B.D. 678

Baggallay L.J. stated:[100]

> "There are several modes in which the damages might be assessed. First, they might be assessed upon the basis of the difference between the price which the insolvent paid for the rupee paper and the price for which he might have bought a similar amount in the market; but this would not entitle the plaintiff to damages unless Lutscher paid too high a price for it. Secondly, they might be assessed upon the basis of the loss which the insolvent actually sustained. This was the course adopted by Huddleston, B.; but I think this view cannot be sustained, for it seems plain that the loss to the plaintiff flowed not from the fraud of the defendant, but from the circumstance that the insolvent held the stock during the period of five months whilst the rupee paper continued to depreciate in value. A third view is that indicated by Bramwell, L.J., namely, that the plaintiff, as representing the insolvent's estate, is entitled to the difference between the price which Lutscher paid for it and the price at which Lutscher might have re-sold it. This view I am prepared to adopt, and I agree that damages should be assessed upon this basis. I think, however, that in ascertaining this difference the price at which Lutscher might have re-sold must be taken to be the price at which he might have re-sold if he had sold upon the same day upon which he bought from the defendant. What occurred after that is not to be taken into account."

[100] at pp. 681, 682

A leading case is *McConnel* v. *Wright*,[101] a decision of the English Court of Appeal. This case stands for the oft-applied principle that the time at which the damages for misrepresentation in a prospectus ought to be assessed is the date of the allotment of the shares to the plaintiff.

In this case a shareholder brought an action against the chairman of Standard Exploration Company Limited for damages for misrepresentation and the omission of material contracts in their prospectus. The prospectus stated that the company had acquired certain shares in the London and Globe Finance Corporation, when the shares had in fact not been acquired. The plaintiff purchased 600 shares in Standard. The company never in fact did any business and was wound up. There were practically no assets in the winding-up for the shareholders.

The London and Globe Finance Corporation shares were in fact transferred to Standard 10 days after the date of allotment of the shares to the plaintiff. Collins, M.R. stated:[102]

> ". . . Now as to that profit which Mr. Whittaker Wright claimed to have established, on the evidence as it now stands and the result of the learned judge's decision, it was not at all certain, at the time when the prospectus was issued, whether the Globe shares would be acquired or not. In point of fact they were not acquired until some time later, and therefore at the date when the prospectus was issued there was a misrepresentation, and <u>damages might have been assessed there and</u>

---

[101] [1903] 1 Ch. 546

[102] at pp. 553

> then on the date on which this gentleman paid his money on the allotment of shares to him. That is clearly the time at which his damages must be assessed. He had paid his money, and he had got in return for it a property which did not contain the 200,000 Globe shares, in respect of which a profit of so large an amount is said to have been obtained. Therefore the position is this, and anyone assessing the damages will have to consider it: What is the difference between the value of the property as it was represented and the property without this large asset in it, having regard to the possibility, certainty, or uncertainty of that asset ever being in fact acquired?" (Emphasis added.)

And further:[103]

> "That obliges me to say something as to the principle upon which damages are assessed in these cases. There is no doubt about it now. It has been laid down by several judges, and particularly by Cotton L.J. in *Peek* v. *Derry*; but the common sense and principle of the thing is this. It is not an action for breach of contract, and, therefore, no damages in respect of prospective gains which the person contracting was entitled by his contract to expect come in, but it is an action of tort - it is an action for a wrong done whereby the plaintiff was tricked out of certain money in his pocket, and therefore, *prima facie*, the highest limit of his damages is the whole extent of his loss, and that loss is measured by the money which was in his pocket and is now in the pocket of the company. That is the ultimate, final, highest standard of his loss. But, insofar as he has got an equivalent for that money, that loss is diminished; and I think, in assessing the damages, *prima facie* the assets as represented are taken to be an equivalent and no more for the money which was paid. So far as the assets are an equivalent, he is not damaged; so far as they fall short of being an equivalent, in that proportion he is damaged. Here there is strong evidence, which the judge has acted on, that there has been a substantial diminution in the equivalent, and, therefore, that the plaintiff has sustained a substantial damage."(Emphasis added.)

And per Romer L.J.:[104] "The proper inquiry is, What was the true value of these shares at the date of allotment?"

[103] at pp. 554, 555

McConnel v. *Wright* has been applied on many occasions, and has been applied with respect to the measure of damages in an action for deceit by the Supreme Court of Canada in *Hepting* v. *Schaaf*.[105]

The Australian court reviewed these principles in *Fawcett* v. *Johnson*.[106] In this case Newman claimed to have invented a device which would increase the efficiency of motor vehicles. Newman tried to raise money and agreed with the defendant to create a company for the purpose of exploiting the invention. The plaintiff applied for 20 shares in the proposed company. The invention was found to be incapable of doing what was alleged and the result was that the plaintiff lost his money. He claimed damages on the basis that he was induced by false and fraudulent representations of the defendant to take the shares.

Pring J. stated that the legal principles regarding the measure of damages was stated in *Broome* v. *Speak* as being the difference between the price which the plaintiff paid for the shares and the fair value of the shares. He then stated:[107]

> "There has been a good deal of argument in the case as to what was the value when the shares were allotted. It has been contended that in such a case the value of the shares is what the public think of them or

---

[104] at p. 558

[105] [1964] S.C.R. 100

[106] (1914), 15 N.S.W. State Rep. 51

[107] at pp. 62, 63

> what the public are ready to give for them. I do not think that that is the correct way of looking at the matter. The real value of the shares must be decided by the value of the asset which is behind them. If that asset is worthless, then, although by the machinations of speculators or the credulity of the public the shares may attain to some fictitious value, that is not the real value of them . . ."

In the result a new trial on the question of damages was ordered.

In *Allan* v. *McLennan*,[108] a decision of the British Columbia Court of Appeal, the plaintiffs purchased shares in the Bank of Vancouver. They sued for rescission of their contracts, or, in the alternative, for damages for deceit. It had been fraudulently represented that the shares offered were the property of the bank, whereas the shares, unknown to the purchasers, were the individual shares of the appellant, who would receive the proceeds of the sale. Damages were awarded, with MacDonald C.J.A. stating: ". . . The measure of damages to be awarded each plaintiff will be the difference in value of the shares with all their incidents, at the time of discovery of the deceit and what was paid for them. . .".

Another leading case is *Burke* v. *Cory*,[109] a decision of the Ontario Court of Appeal per Schroeder J.A. In this case a medical doctor practising in Vancouver was induced to purchase speculative mining shares from the defendant. He purchased 1,000 shares in Fleetwood Yellowknife Mines Ltd. at $0.28 per share in February, 1956; a further 1,000 shares in Fleetwood at a price of $0.36 per share in February, 1956; and a further 2,000 shares in Jack Lake Mines in May, 1956 at an undisclosed price. The Fleetwood shares rose to some extent on the stock exchanges, but then collapsed until they were worth only $0.04 at the time of trial; the Jack Lake Mines shares rose to a high of $0.70 per share but were worth $0.07 per share at the time of trial. The plaintiff sued for damages for misrepresentation. The trial judge awarded damages of $1,687.50, apparently based on

---

108 (1916), 31 D.L.R. 617

109 (1959), 19 D.L.R. (2d) 252

the difference between the price paid for the shares by the plaintiff and the value of the shares at the time of trial.

Schroeder J.A., on appeal, stated:

> "I come now to a consideration to the fourth ground of appeal which relates to the issue of damages. In a case of this kind, as in actions of deceit, the measure of damages is the difference between the actual value of the property and its value if the property had been what it was represented to be, so that when a man has been induced by a false representation contained in a prospectus to take shares in a company, the proper mode of measuring the damages is to ascertain the difference between the price paid for the shares and the actual value at the time of allotment. Counsel for the appellant has cited many authorities in support of this proposition . . . What is the actual value of shares of stock involved in a transaction of this kind at the time of allotment? There may be cases in which such value can be ascertained with reference to the market value at that time, but that applies to those cases where the shares in question have a real intrinsic value backed and supported by solid and substantial assets. The authorities indicate, however, that there are cases in which value is to be ascertained not by the market value at the time of allotment, but by the light of subsequent events, including, in cases in which the company has gone into liquidation, the result of winding-up. This has been clearly declared in *Twycross* v. *Grant* . . ." (Emphasis added.)

Schroeder J. then asked himself what was the fair market value of the shares when the plaintiff was induced to buy them through misrepresentation. He noted that the plaintiff was made aware of the true value of the mining stocks in the beginning of March, 1957, at which time the shares had already fallen significantly in value. The Fleetwood shares were worth $0.06 per share at this time and the Jack Lake shares an average of $0.35 per share. Schroeder J.A. implicitly found that the plaintiff had a duty to mitigate by selling his shares after learning the true situation and therefore assessed damages as being the difference between the amount the plaintiff paid for the mining stocks and the value of the stocks after he learned the truth of the representations in the beginning of March, 1957. Accordingly, he reduced the award of the trial judge to $787.50.

In *Culling* v. *Sansai Securities Ltd.*,[110] a decision of Anderson J. of the British Columbia Supreme Court, the plaintiff bought 7,500 shares in the Nisson company as a result of representations made to her by a salesman employed by the defendant that the shares were either listed on the Tokyo Stock Exchange or were cleared for trading in Japan. The plaintiff sued for losses occasioned by the fall in the value of the shares and was awarded the difference between what she paid for the shares and their market value at the time that she learned that the shares had not been listed on the Tokyo Stock Exchange.

The Supreme Court of Canada decision of *Hodgkinson* v. *Simms*[111] is an important decision in that it may support an argument that the measure of damages should be a full recovery of the amount paid for the shares, and not the difference between the amount paid for the shares and the value of the shares at the date of learning of the misrepresentation. It seems doubtful that the case can be given this broad interpretation, however.

In this case the appellant, Hodgkinson, a stockbroker who was inexperienced in tax planning, hired Simms, an accountant, to give general tax advice. Simms advised investment in four MURBs, and the appellant lost substantial amounts of monies in these investments. Unknown to Hodgkinson, Simms was acting for the developers regarding the structuring of the MURB projects and received fees from the developers. Hodgkinson sued for breach of fiduciary duty, breach of contract and negligence-this was not a case of fraud or deceit. The decision is a leading decision

---

[110] (1974), 45 D.L.R. (3d) 456

[111] [1994] 3 S.C.R. 377

because of its statement of general principles regarding fiduciary duty. The decision is also important in terms of what it has to say about calculation of damages, however.

The trial judge awarded the plaintiff damages, based on the theories of breach of fiduciary duty and breach of contract, in the amount of $350,507.62. This was calculated based on the principle that Hodgkinson was entitled to be put in the position he would have been in had he never been induced to make the investments in the MURBs. Thus he was awarded the capital invested in the four projects, minus the tax benefits received, plus an additional amount paid by way of arrears on income tax reassessments and consequential damages of legal and accounting fees. This was varied by the British Columbia Court of Appeal and disgorgement was in effect ordered The damages were set at an amount equal to the fees received by Simms from the developers on account of the four MURB projects, prorated as between the various investors in the projects. The Supreme Court of Canada restored the damage award of the trial judge.

The Supreme Court of Canada per La Forest J. for the majority first noted that the proper approach to damages for breach of a fiduciary duty was restitutionary-the plaintiff was entitled to be put in as good a position as he would have been but for the breach. La Forest then referenced the leading decision *of Rainbow Industrial Caterers Ltd.* v. *Canadian National Railway Co.*[112] per Sopinka J. with respect to the measure of damages resultant from misrepresentation. In the *Rainbow* case Sopinka J. had adopted the following passage from Fridman, *The Law of Torts*:[113]

---

[112] [1991] 3 S.C.R. 3

[113] at p. 136

> "What sort of economic loss is recoverable in an action for negligent misrepresentation is still to be resolved conclusively, although the accepted test seems to be restoration of the plaintiff to the position in which he would have been if the negligent misrepresentation had never been made. Some cases suggest that what the plaintiff can recover is what might be termed "out of pocket expenses". In other words, he is entitled to be reimbursed for those costs and expenses which he has incurred and has expended in reliance on the misrepresentation."

In *Hodgkinson* v. *Simms*, La Forest J. stated:

> "Thus, where a party can show that but for the relevant breach it would not have entered into a given contract, that party is freed from the burden or benefit of the rest of the bargain; . . . In short, the wrong party is entitled to be restored to the pre-transaction status quo."

La Forest J. reviewed *Waddell* v. *Blockey* and noted that it was an aged case which predated the court's modern approach to fiduciary relationships. La Forest then noted the case of *Allan* v. *McLennan*, which stated that the measure of damages was to be the difference in the value of the shares at the time of the discovery of the misstatement and what was paid for them. After discussing the American cases regarding securities fraud, he concluded:

> "From a policy perspective it is simply unjust to place the risk of market fluctuations on a plaintiff who would not have entered into a given transaction but for the defendant's wrongful conduct. I observe that in *Waddell*, *supra*, Bramwell L.J. conceded, at p. 680, that if *restitutio in integrum* had been possible, the plaintiff could probably have recovered in full. Indeed counsel for the appellant argued that the proper approach to damages in this case was the monetary equivalent of a rescissionary remedy. I agree. <u>In my view the appellant should not suffer from the fact that he did not discover the breach until such time as the market had already taken its toll on his investments.</u> This principle, which I take to be a basic principle of fairness, is in fact reflected in the common law of mitigation, itself rooted in causation . . ." (Emphasis added.)

La Forest J. then further justified the trial judge's award of damages on the basis of the fiduciary relationship between the parties. He noted that the wrong complained of went to "the heart of the duty of loyalty that lies at the core of the fiduciary principle." He further stated: "In redressing a wrong of this nature, I have no difficulty in resorting to a measure of damages that places the exigencies of the market-place on the respondent. Such a result is in accordance with the principle that a defaulting fiduciary has an obligation to effect restitution in specie or its monetary equivalent."

It is to be noted, however, that La Forest wrote of the plaintiff not being penalized by market fluctuations if ". . . he did not discover the breach until such time as the market had already taken its toll on his investments". Thus this decision, on the face of it, would not seem to undermine those decisions such as *Burke* v. *Cory* which assess damages by subtracting the market value of the shares as of the date the plaintiff became aware of the true situation from the purchase price on the principle that the plaintiff has a duty to mitigate damages by selling the shares after disclosure of the misrepresentation. La Forest J. also referenced *Allan* v. *McLennan*,[114] in which the full purchase price of shares purchased following a misrepresentation in a prospectus was not awarded, but only the difference between the purchase price and the value of the shares as of the date of disclosure of the misrepresentation. La Forest particularly emphasized that the trial judge's award of damages should be upheld in order to "put special pressure on those in positions of trust and power over others in situations of vulnerability." Thus, notwithstanding the Supreme Court's criticism of *Waddell* v. *Blockey*, *Hodgkinson* v *Simms* would not seem to be clear authority that the full purchase price should be given in situations of misrepresentation in a prospectus. This decision is further subject to being distinguished as being relevant only to breach of fiduciary relationship situations.

[114] (1916), 31 D.L.R. 67

In England a recent case has articulated circumstances in which the full purchase price paid for shares should be awarded in circumstances of misrepresentation in a prospectus. In *Smith Newcourt Securities Ltd.* v. *Scrimgeour Vickers and Citibank N.A.,*[115] a decision of the House of Lords, Roberts, who was an employee of the second defendant Citibank N.A., which was acting as broker for the first defendant Scrimgeour Vickers, made fraudulent misrepresentations which induced the plaintiff Smith New Court Securities Ltd to buy shares in a public company, Ferranti. Roberts stated that the plaintiff would be competing with two other bidders, that Roberts would disclose the competing bids after Smith had made its bid and that two other named companies had made bids. The plaintiff Smith bought 28,141,424 shares in the company at 82 pence each on July 21, 1989 for a total of £23,141,424, with a view to holding them as a "market making risk" and selling them when an appropriate opportunity arose. It then became apparent that a fraud had been perpetrated on the company, (the "Guerin fraud"), prior to the date of the purchase transaction, which was not revealed until the directors made an announcement on September 11, 1989. Trading in the shares was suspended. Trading resumed on October 3, 1989 and the plaintiff subsequently sold the shares in small parcels over a period of approximately six months. By April 30, 1990 Smith had sold all of the Ferranti shares and had recovered just over £11 million. Smith first learned of the Roberts fraud on December 5, 1989. The plaintiff sued for damages and the court considered what the proper measure of damages was to be.

The trial judge found that the plaintiff was entitled to the difference between the price paid for the shares and the "true" value of the shares as of the date of the purchase transaction, July 21, 1989. He assessed the value of the shares as of the date of the purchase transaction as being that as if the market known of the underlying Guerin fraud, and valued the shares at 44 pence per

---

[115] [1996] 3 W.L.R. 1051

share. He then awarded the difference between the contract price and the "true" value of the shares as of the date of the purchase transaction, for a total award of £12,382,226.

The English Court of Appeal took the view that it was only legitimate to depart from the market value of the shares as of the date of the purchase transaction if the price was falsified by the defendant's misrepresentation, ie. the Roberts fraud, and not by an underlying fraud. The appellate court therefore held that the correct measure of damages was the difference between the price paid per share, 82 pence, and the price that Smith would have been prepared to pay on the transaction date but for the Roberts misrepresentations, 78 pence, and thus reduced the damages to £196,000.

The House of Lords in effect restored the judgement of the trial judge. The House of Lords noted the general principle that ". . . where a fraudulent misrepresentation has induced the plaintiff to enter into a contract of purchase, the measure of damages is, in general, the difference between the contract price and the true open market value of the property purchased, *valued as at the date of the contract of purchase*". It then noted the exception to the rule being where the open market at the transaction date was a false market because the price was inflated due to the misrepresentation of the defendant-in such cases the "true" value at the transaction date has to be ascertained with the benefit of hindsight. The court then examined whether the rule that required damages to be assessed as of the date of the contract of purchase should be strictly adhered to.

After stating that *Doyle* v. *Olby (Ironmongers) Ltd.*[116] correctly stated the law, Lord Browne-Wilkinson stated:[117]

> *Doyle* v. *Olby (Ironmongers) Ltd.* establishes four points. First, that the measure of damages where a contract has been induced by fraudulent misrepresentation is reparation for all the actual damage directly flowing from (ie. caused by) entering into the transaction.

116 [1969] 2 Q.B. 158

117 at pp. 1058, 1059

Second, that in assessing such damages it is not an inflexible rule that the plaintiff must bring into account the value as at the transaction date of the asset acquired; although the point is not adverted to in the judgments, the basis on which the damages were computed shows that there can be circumstances in which it is proper to require a defendant only to bring into account the actual proceeds of the asset provided that he has acted reasonably in retaining it. Third, damages for deceit are not limited to those which were reasonably foreseeable. Fourth, the damages recoverable can include consequential loss suffered by reason of having acquired the asset.

Lord Browne-Wilkinson then concluded:[118]

“In the light of these authorities the old 19th century cases can no longer be treated as laying down a strict and inflexible rule. In many cases, even in deceit, it will be appropriate to value the asset acquired as at the transaction date if that truly reflects the value of what the plaintiff has obtained. Thus, if the asset acquired is a readily marketable asset and there is no special feature (<u>such as a continuing misrepresentation or the purchaser being locked into a business that he has acquired</u>) the transaction date rule may well produce a fair result. The plaintiff has acquired the asset and what he does with it thereafter is entirely up to him, freed from any continuing adverse impact of the defendant’s wrongful act. The transaction date rule has one manifest advantage, namely that it avoids any question of causation. <u>One of the difficulties of either valuing the asset at a later date or treating the actual receipt on realization as being the value obtained is that difficult questions of causation are bound to arise. In the period between the transaction date and the date of valuation or resale other factors will have influenced the value or resale price of the asset. It was a desire to avoid these difficulties of causation which led to the adoption of the transaction date rule. But in cases where property has been acquired in reliance on a fraudulent misrepresentation there are likely to be many cases where the general rule has to be departed from in order to give adequate compensation for the wrong done to the plaintiff, in particular where the fraud continues to influence the conduct of the plaintiff after the transaction</u>

118 at pp. 1060-1061

> is complete or where the result of the transaction induced by fraud is to lock the plaintiff into continuing to hold the asset acquired . . .
>
> In sum, in my judgement the following principles apply in assessing the damages payable where the plaintiff has been induced by a fraudulent misrepresentation to buy property: (1) the defendant is bound to make reparation for all the damage directly flowing from the transaction; (2) although such damage need not have been foreseeable, it must have been directly caused by the transaction; (3) in assessing such damage, the plaintiff is entitled to recover by way of damages the full price paid by him, but he must give credit for any benefits which he has received as a result of the transaction; (4) as a general rule, the benefits received by him include the market value of the property acquired as at the date of acquisition; but such general rule is not to be inflexibly applied where to do so would prevent him obtaining full compensation for the wrong suffered; (5) although the circumstances in which the general rule should not apply cannot be comprehensively stated, it will normally not apply where either (a) the misrepresentation has continued to operate after the date of the acquisition of the asset so as to induce the plaintiff to retain the asset or (b) the circumstances of the case are such that the plaintiff is, by reason of the fraud, locked into the property. (6) In addition, the plaintiff is entitled to recover consequential losses caused by the transaction; (7) the plaintiff must take all reasonable steps to mitigate his loss once he has discovered the fraud." (Emphasis added.) [119]

---

[119] S.M. Waddams in *The Law of Damages* (Looseleaf Edition) (Canada Law Book Inc., Toronto, 2001) has summarized these cases by stating at pp. 5-23:

> ". . . *Waddell* v. *Blockey* was, however, disapproved by the Supreme Court of Canada in *Hodgkinson* v. *Simms*, where La Forest J. said that a plaintiff "should not suffer from the fact that he did not discover the breach until such time as the market had already taken its toll on his investments". In *Smith Newcourt Securities Ltd.* v. *Scrimgeour Vickers (Asset Management) Ltd.*, the House of Lords held that the rule stated in *Waddell* v. *Blockey* was generally "practical and just" but the rule was not inflexible, and should yield to the "overriding compensatory rule" and would not apply when the plaintiff was locked into the transaction by reason of the fraud.
>
> The value of the property at a later date than the date of transfer may be relevant evidence of its value at the date of transfer itself (citing *Derry* v. *Peek* and *Twycross* v. *Grant*)."

In John G. Fleming, *The Law of Torts* (9d) (The Law Book Company Limited, Sydney, Australia, 1998), in discussing damages for deceit, it is stated at p. 703:

> "Liability covers all direct damage, not only foreseeable damage, in token of the heinousness of fraud and as a measure of deterrence. Ordinarily, the value of any property acquired as a result of the fraud must be assessed as at the time of the purchase. But where the plaintiff was locked into the property, the correct measure may exceptionally be the difference between the price paid and the amount subsequently realized on sale. Such extra loss,

In *Kerr* v. *Danier Leather Inc*.,[120] a decision of Cuming J. of the Ontario Superior Court of Justice, the long established principles set out above seem to have been applied, without express reference to the preceding authorities.

In *Kerr* the proposed representative plaintiffs brought an action under the Ontario *Class Proceedings Act* and Cuming J. considered an application for certification of the class proceeding. The action claimed damages resultant from misrepresentation in a prospectus in reliance on the disclosure provisions of the Ontario *Securities Act*. The proposed representative plaintiffs were individual investors who had purchased shares in Danier Leather Inc. during the period of distribution pursuant to an initial public offering. Danier issued a prospectus on May 6, 1998 and the price per share was set at $11.25. The date of the contract of purchase was May 20, 1998. The case indicates that one of the representative plaintiffs, Mr. Kerr, continued to hold the shares at the time of the application.

One of the things to note is that the Ontario *Securities Act* s. 130 is different than Alberta *Securities Act* s. 203 in that the Ontario Act provision stipulates that liability from misrepresentation in a prospectus is to be assessed on the basis of the misrepresentation <u>at the time of purchase</u>. S. 203 does not explicitly state at which time the misrepresentation is to be assessed. The

---

however, must not be "causal", nor accidental or extrinsic, and subject to the duty to mitigate. . . "

[120] [2001] O.J. No. 4000

foregoing review of the common law and more particularly the case of *McConnel* v. *Wright* clearly states that misrepresentation in these situations is to be assessed as of the time of purchase, however, and it is therefore arguable that the Ontario statute does nothing more than codify the common law on this point.

The issue became important in *Kerr* v. *Danier Leather Ltd.* because the misrepresentation made at the time of the issue of the prospectus had in effect corrected itself at the time of the trial (as was the case in *McConnel* v. *Wright*). In *Kerr* the prospectus disclosed Danier's financial condition and operating results for the first three quarters of the fiscal year to March 29, 1998 and projected future revenue, profit and other financial information with respect to the fourth quarter of fiscal 1998. The forecast for the fourth quarter was that the total revenues would be 19.3% of the total revenues for the 1998 fiscal year. An increase in revenue of $5 million was projected over that of the 1997 fourth quarter, for total revenues of $17,410,000. The actual sales in the fourth quarter, May and June of 1998, did not meet the expectations in the forecast. This was attributed to a prolonged period of unseasonably warm weather.

The Amended Amended Statement of Claim asserted that the prospectus contained misrepresentations with respect to the future oriented financial information, including the projected revenue for the fourth quarter. The plaintiffs claimed that there were misrepresentations in that the Danier directors, on the basis of daily sales receipts, knew almost eight weeks into the fourth quarter that the sales projections would not be met.

On June 4, 1998, Danier's Board of Directors issued a press release containing a "Revised Forecast" which reduced the projected earnings for the fourth quarter from $17,410,000 to approximately $12,600,000, a decline of 27.5%. A net loss of $1.15 million was projected for the fourth quarter. The projected net earnings of fiscal 1998 were reduced from $4,000,500 to $3,000,700.

In fact, however, there was colder weather for the balance of June 1998 and sales of the product increased. Danier also made use of certain “reserves” in its manner of financial reporting. Thus the actual results for the fourth quarter in overall fiscal 1998 were only marginally less than the projections in the forecast in the prospectus. However, the share price remained depressed for some time. With the June 4, 1998 “Revised Forecast” the market price for Danier’s shares had dropped some $2 to $3 per share. On June 1, 1998 the shares traded at $11.65 per share; on June 9, 1998 they traded as low as $8.25 per share. On July 20, 2001, the date of the hearing of the application, the share price was $12.50 per share.

In assessing whether the action should be certified as a class action, Cuming J. seemingly concluded that it was arguable that the known results to May 20, 1998, based on the daily sales report, would be material information to investors and should have been included in the prospectus. Thus there was a misrepresentation.

The defendants apparently argued that because the forecast for the fourth quarter contained in the prospectus was ultimately substantially achieved, there was no misrepresentation. Cuming J. dismissed this argument by stating that s. 130(1) of the Ontario *Securities Act* clearly said that the misrepresentation was to be assessed “at the time of purchase”. “The fact that a misrepresentation contained in a prospectus might later become accurate is irrelevant”.

Cuming J. then considered whether there was a common issue in respect of damages. The plaintiffs asserted that the damages were suffered as of the date of purchase, being May 20, 1998. The plaintiffs would quantify the damages as the difference between the amount paid ($11.25) and the price that would have been paid had the price not been based in part upon a misrepresentation. (The plaintiff’s submission on this point seems to be a clear summary of the common law.)

Cuming J. summarized the argument of plaintiff’s counsel as follows:

> "Counsel for the proposed representative plaintiffs advances the theory that where there is a misrepresentation as to the value of shares the measure of damages will be the purchase price paid less the actual value of the shares at the time the shares were allotted. He argues that the claim of a class member crystallizes at the point of discovery of the misrepresentation and that any decline or increase in value thereafter should not impact upon the claim."

Apparently counsel only referenced general texts, and not case law to support this position.

Cuming J. noted that those persons who had sold their shares into the secondary market before the date of the "Revised Forecast" on June 4, 1998 would not have suffered damages. "It is not the misrepresentation per se that causes the damages. Rather, it is the change in position to one's detriment because of reliance upon the representation that constitutes the loss or damages."

Cuming J. stated:

> "The normative measure for the quantification of damages in tort for a negligent misrepresentation is to compensate for the loss resulting from change of position due to the reliance by the innocent victim upon the misrepresentation. That is, the reliance interest of the victim is protected. The plaintiff seeking damages in an action for negligent misrepresentation is entitled to be put in that position he or she would have been in if the misrepresentation had not been made. *Rainbow Industrial Caterers Ltd.* v. *C.N.R. Co.* . . .
>
> Section 130 of the *Securities Act* does not prescribe a measure of damages. In my view, the measure for damages for a misrepresentation under s. 130 is of the same nature as a misrepresentation in tort. Thus, the question must be - what did a given shareholder lose by purchasing a share for a given price in the IPO premised upon a misrepresentation. For example, an investor who purchased shares in Danier on May 20, 1998 and who then sold just after the June 4, 1998 Revised Forecast would have incurred a loss. <u>Arguably, the loss due to the misrepresentation would be quantified as a fall in market price due to the corrected forecast for the fourth quarter</u>. A share is a bundle of rights constituting a chose-in-action. The shareholder purchased an intangible property in becoming a shareholder. That property arguably had a lesser value as

> determined by the market when the facts contained in the Revised Forecast become public knowledge in the marketplace.
>
> The defendants submit there is no common issue in respect of damages. They say the Court must make an inquiry in respect of every individual shareholder as to what the person would have done had the misrepresentation not been made . . . However, I query the nature of the inquiry necessary when the subject matter is publicly traded shares. <u>If it can be proven on a balance of probabilities that the misrepresentation diminished the price of the shares in the market place then arguably the difference between the issue price and the diminished price reflects accurately the loss of shareholders who are deemed to have relied upon the misrepresentation</u>." (Emphasis added.)

Thus, again, Cuming J. seems to articulate the common law principles, without reference to cases.

Cuming J. then went on to red-flag the difficulties in damage assessment in this case, in that the fourth quarter projections were substantially met, and thus it could be argued by the defendants that the fall in value of the Danier shares could not be attributed to the misrepresentation once the actual fourth quarter results were known. Moreover, the issue price of $11.25 per share may not have been an accurate reflection of the value of the shares if the Danier directors had had the actual results for the fourth quarter at the time of setting the IPO price.

Cuming J. further red-flagged the difficulty presented by the fact that some of the shareholders continued to hold their shares, including Kerr, and the price of the Danier shares had increased. It was his view that those shareholders who continued to hold the shares may have problems in assessing damages, presumably because the value of the shares had risen. He suggested that there might not be any damages in fact.

In the result Cuming J. held that there were common issues of damages such that this criteria for certification of the class action was met.

In *Dixon* v. *Deacon Morgan McEwen Easson et al.*,[121] a decision of the British Columbia Court of Appeal, the president and the chief financial officer of the defendant company NBS falsified the company's records and the president issued a press release which represented a false picture of the company's financial affairs. The appellant, knowing of the press release, purchased shares in the company at approximately $12.50 per share. When the misconduct was discovered and the true state of the company's affairs became public, the share price dropped and the appellant sold his shares for about $1.65 each. He sued for fraud and misrepresentation. The trial judge held the company was not guilty of fraudulent misrepresentation, but was guilty of negligent misrepresentation. However, he also held that the appellant failed to prove his damages. The appellant appealed and the appeal was allowed. It was held that, having proved the market price and the price at which he sold the shares, the appellant was entitled to recover the difference between them in damages. McEachern C.J.B.C., writing for the court, stated, after summarizing the defendant's argument that the plaintiff had failed to prove the "real" value of the shares at the time of the purchase:

> "I am unable to accept this submission. In my view the market value of the shares was some and probably the best evidence of their "real" value. It is true that that value may be too high or low when compared with other methods of ascertaining value, such as book value, discounted cash flow, asset appraisal or on an earnings basis. But these are matters of evidence and in the absence of any such evidence, I do not agree that a court should reject an apparently valid market price and dismiss the action. The position is well stated in *McGregor on Damages*, 14th ed. paras. 1466-7:
>
> > "Since the price paid by the plaintiff for the shares can be ascertained without difficulty, the courts have had to concern themselves only with a calculation of the

[121] (1993), 102 D.L.R. (4th) 1

> actual value of the shares transferred. On this several points have been decided.
>
> (1) The most important point, being peculiar to shares, is that care must be taken not to assess the value of the shares at the price at which they stand in the market, since such a price may be a false and artificial one induced by the very deceit of which the plaintiff is complaining . . .
>
> The actual value is, therefore, the price the shares would fetch in the market if the truth was revealed and all the facts were known."

Employing this analysis, it is apparent that the defendant, if it wished, could have attempted to show that the market price was not reliable, but I reject the suggestion that the market price was no evidence at all and I think that the onus was on the defendant to show that the market price was unreliable for this purpose. <u>In this context I think market price after disclosure of the true facts was the best evidence of value</u> because it represented an amalgam of a great many investment opinions. If the market price at the time of purchase was inflated because of the suppression of the Company's difficulties known to its officers, as must have been the case, then it is obvious that the plaintiff proved some loss. In other words, it was open to the defendant to rebut the evidence of market value to show that the plaintiff got actual value for his money.

> For these reasons, it is my view that the learned trial judge erred in concluding that the plaintiff had not proved any loss. I wish to say a word about another basis upon which the learned trial judge reached his conclusion. He mentioned that by the time the trading was resumed in February, 1988, there was other bad news that had become known to investors that was entirely unrelated to the false statements in the press release. He particularly referred to the fact that the president and treasurer had both been removed under a cloud of suspicion; that there had been an unauthorized removal of $10 million from the company's treasury subsequent to the last fiscal period, and that it later became known that the company had lost an important contract with Citibank, a major customer. The trial judge said those matters, which had nothing whatsoever to do with the misrepresentation upon which the plaintiff relied, made the share value on resumption of trading an unreliable indicator of the amount of loss actually suffered by the plaintiff. In argument these matters were described as "investors risks".
>
> The test to be applied in these matters is what compensation should the plaintiff recover for having been misled into purchasing shares which had less value than the purchase price. It is appropriate to consider his position as it would be if he had never purchased the shares. Looked at in this way, it follows that he should not have been subjected to investors risks such as those described above, and it is not necessary to examine what contribution each of these risks made to the lessened value of the shares." (Emphasis added.)

These basic principles have also been applied in situations in which the shareholder has been induced to sell the shares for much less than their real value because of misrepresentation on the part of the purchaser of the shares. A recent example of such a case is *Baxter* c. *Biotech Electronics Ltd.*[122] In this decision of the Quebec Court of Appeal the minority shareholders of Biotech Electronics Ltd., a closely held corporation, sold their shares to the majority shareholders. The minority shareholders then took action against the purchasers to annul the sale on grounds of fraud and further sued for damages. The Quebec Superior Court concluded that the purchasers had failed to disclose certain material facts which they had a duty to disclose and maintained the action against them. A month after the purchase of the shares from the plaintiff shareholders, Biotech made

[122] [1998] A.Q. No. 48; leave to appeal to the Supreme Court of Canada dismissed at [1998] S.C.C.A. No. 1119

a public offering of its shares at a price equivalent to $150 per share. It was found that the plaintiffs had been kept in ignorance of a proposal by Midland Doherty to underwrite the public offering for an amount of $100 to $180 per share. In assessing damages, however, the Superior Court judge awarded damages equivalent to the difference between the price at which they sold their shares to the purchasers ($25 per share) and what he considered to be the "fair value" of the shares on April 19, 1984, the date of the transaction, which was $33.75 per share. Thus the judgement was for the amount of $206,062.60.

On appeal, the plaintiffs argued that they should be granted damages in the amount between the price the shares were sold for and the price that the purchasers eventually sold the shares for on the open market, which was $150 per share.

Rothman J. stated: "The basic principle to be applied in the evaluation of damages caused by fraud through misrepresentation or concealment, as in the case here, is that the plaintiffs are entitled to be put in the position they would have been in had the misrepresentation or concealment not occurred: "*restitutio in integrum*". . . *Canadian National Railway Company* v. *Rainbow Industrial Caterers Ltd.* . . .".

He then concluded: "I can see no valid reason why the measure of plaintiff's damages should not be the difference between the price of $25 they received and the price of $150 on the public issue: their loss of profit was $125 per share."

Rothman J. referenced *Dixon* v. *Deacon Morgan McEwen Easson* as authority, *inter alia*.

The case of *NIR Oil Ltd.* v. *Bodrug*[123] is also of interest. This case involved an action for damages for insider trading. The plaintiff Cohen was active in the oil and gas industry and

[123] (1983), 47 A.R. 127; affirmed at (1985), 18 D.L.R. (4^{th}) 608

incorporated the plaintiff NIR Oil Ltd. as a private oil and gas producing company in Alberta. He met the defendant Bodrug, who had a small propane marketing company called Canadian Hidrogas Resources Ltd. The two parties discussed a form of merger which resulted in Cohen joining Bodrug's company, Hidrogas. Hidrogas bought all producing properties from NIR Oil Ltd. for $600,000, payable in installment over six years. Cohen entered into employment with Hidrogas for a period of three years and it is implicit in the decision that he acquired shares in Hidrogas. Over this period of time NIR Oil Limited acquired the right to purchase shares in Hidrogas.

In 1975 Cohen voiced dissatisfaction with the way in which Bodrug was running the company. He decided to leave Hidrogas. Various lawsuits ensued and eventually a settlement agreement was reached. Pursuant to this settlement, Cohen sold his shares in Hidrogas to Bodrug. Unknown to Cohen at this time, however, was the fact that Bodrug was negotiating to sell the shares of Hidrogas to Norcen Energy Resources Ltd. Thus, following the transfer of Cohen's shares in Hidrogas to Bodrug, Bodrug then sold the shares for substantially more than what was to be paid by Bodrug to Cohen pursuant to the settlement agreement.

Cohen and NIR sued for damages, alleging active concealment of material fact, which amounted to fraudulent misrepresentation and thus deceit. They further asserted that the defendants were liable pursuant to the insider trading provisions of the Alberta *Companies Act* and the Alberta *Securities Act*.

This reliance on the Alberta *Companies Act* and Alberta *Securities Act* insider trading provisions is significant with respect to the measure of damages in that both of these sections provided for the recovery of "any direct loss" resultant from insider trading. In considering the measure of damages, McDonald J. found that Cohen and NIR were entitled to recover compensation from the estate of Bodrug for the direct losses suffered. He then noted that the statutory measure of damages of direct losses was not in step with the common law development which required that losses be reasonably foreseeable to be awarded. McDonald J. then awarded damages to the plaintiffs in the amount that they could have received for the Hidrogas shares had they sold them to Norcen In the case of NIR this amount was reduced to the amount that it could have sold the Hidrogas shares for in the open market following the press release of the deal with Norcen, $14.25 per share. McDonald J. then determined the price that Cohen was prepared to take from Bodrug to settle the claims, $7 per share, and assessed the direct loss of NIR as being the difference between $7 per share and $14.25 per share, for a total damage award of $2,247,500. Cohen was awarded the difference between $7 and $15 per share.

This damage calculation was affirmed in the result by the Alberta Court of Appeal per McDermid J.A.

What Happens If the Price of the Shares Goes up after the Misrepresentation?

Cuming J. in *Kerr* v. *Danier Leather Inc.* suggested that there may not in fact be damages if the price of the shares goes up after the date of the misrepresentation. This is a view taken by the early case of *Uncle Ben's Tartan Holdings Ltd.* v. *Northwest Sports Enterprises*,[124] a decision of Anderson J. of the British Columbia Supreme Court, but it has subsequently been called into question.

In *Uncle Ben's* the plaintiff bought shares and debentures in the defendant Northwest Sports Enterprises Ltd. for a total sum of $675,000 on December 17, 1970. Following notice in June of 1971 of certain irregularities in the conduct of the company's affairs, the plaintiff demanded a meeting to inquire into these matters and issued a statement of claim, claiming damages for fraud and/or negligence. As of June 1971 the shares were worth somewhat less than the plaintiff had paid for them but the plaintiff held them until November 1973, when it sold the shares and debentures for a total of $707,934.12. Thus between the date of the purchase and the date of the sale the plaintiff received a profit of $119,148.25.

[124] (1974), 46 D.L.R. (3d) 280

It was argued that the plaintiff should nonetheless receive damages in the amount of the difference between the amount paid for the shares and the value that they were on the transaction date, but for the fraud/negligence. The authorities of *McConnel* v. *Wright*, *Derry* v. *Peek*, *Hepting* v. *Schaaf* and others were reviewed, including the English case of *Doyle* v. *Olby (Ironmongers)*. In the result Anderson J. concluded:

> "While I would be prepared to follow the reasoning of Lord Denning [in *Doyle*], in proper circumstances, I have reached the conclusion that the principles enunciated by Lord Denning are not applicable here. I am inclined to the view that a plaintiff, who has been defrauded, cannot say: I will keep the shares and endeavour to make a capital gain, but at the same time, I am going to hold the defendant liable for interest on the monies I have invested, until I decide to sell my shares.
> If I am wrong in concluding that interest or "cost of the use of the plaintiff's monies" is not payable by the defendants and that I am bound to follow the judgement of our Court of Appeal in *Allan* v. *McLennan, supra*, it appears that Tartan cannot succeed. The following calculations, utilizing the most favourable version of the *Allan* v. *McLennan* formula, namely: "the difference between the value of the shares at the time Tartan allegedly discovered the fraud and what they paid for them with interest", make it quite apparent that even if Tartan is entitled to a "fair" return on the monies which it invested, there has been no loss . . ."

These cases were reviewed in some detail and an opposite result reached in *Secord* v. *Global Securities Corp.*,[125] a decision of Smith J. of the British Columbia Supreme Court. In this case the plaintiff Mary Secord was the owner of the plaintiff Sailview Ventures Ltd. She had a substantial portfolio of investments and she placed her holdings and accounts with the defendant Global Securities Corp., with whom the defendant investment advisors were employed. She was not employed and relied on her investments for her income. Some of the plaintiff's funds were used for options trading which eventually resulted in losses. She then transferred her accounts to another broker and by the time of the trial some of the shares in the accounts, which had been acquired under

---

[125] (2000), 81 B.C.L.R. (3d) 235

the auspices of the defendants, had greatly appreciated in value. She sued for damages for breach of fiduciary duty, breach of contract and negligence on the basis that the advisors engaged in unauthorized trading and unsuitable investments. The action was allowed and she was awarded $50,000 Cdn. and $107,500 US in damages. It was held that the appropriate time for assessment of the measure of damages was the date of transfer of the accounts. The plaintiff had the ability and duty to mitigate her losses and, as such, would have had difficulty claiming damages from the defendants for losses beyond the market value on the date of the transfer. Accordingly, on the same principle, she should not have her subsequent gains offset against her damages.

Smith J. noted the defendant's position that the plaintiff had not suffered a loss. Where an act of negligence also causes profit, such profit must be characterized as part of a continuous transaction and deducted from the damages claimed. He further noted the plaintiff's position that when they closed out their accounts with Global Securities they took responsibility for those accounts. They could have sold all of their securities and recovered damages for the difference between the value of the accounts at the beginning and at the end of the period. They chose not to and chose to take the risk from that point on. If the value of the securities had declined, they would not have been able to pursue the defendants for further losses. By the same token the fact that the securities increased in value should not go to the defendant's credit.

Smith J. placed great emphasis on *Jamal* v. *Moola Dawood, Sons & Co.,*[126] a decision of the Privy Council. In this case the buyer breached a contract to purchase shares from the plaintiff vendor, resulting in a loss to the plaintiff of the difference between the contract price and the lower market price as of the date of the breach. In the following six months the plaintiff sold the shares into the market. Although he realized less than he would have under the breach of contract, his overall loss was less than his date-of-breach loss thanks to improving marketing conditions. The Privy Council refused to give the defendant the benefit of the plaintiff's later sales and awarded the plaintiff the full date-of-breach loss.

---

[126] [1916] 1 A.C. 175

As Smith J. then further noted, the rule that losses are to be ascertained at the date of the breach is not absolute, the plaintiff is subject to a duty of mitigation. If the plaintiff has a duty to mitigate his or her losses, he or she will be given a reasonable time to do so and if, during that period, the plaintiff takes steps in mitigation which in fact avoid losses, the plaintiff is only permitted to recover for the losses he or she has actually experienced.

Smith J. then sought to reconcile the conflicting cases, and concluded:

> "Looking at the cases overall, it appears that: (1) gains earned from the use of superior equipment or licenses purchased after the original equipment or licensed vendor's breach of contract are to be set-off against the plaintiff's loss . . .; (2) gains earned from the use of replacement structures acquired after the original developer's negligence and/or breach of contract are to be set off against the plaintiff's loss . . .; (3) gains earned at an employer's liquidation sale are to be set-off against damages for wrongful dismissal where that dismissal was the result of the employer's bankruptcy . . .; but (4) gains earned from the sale of shares into an improved market following the original buyer's breach of contract are not to be discounted from the plaintiff's loss. . .
>
> The apparent inconsistency can be explained. Shares or other securities are so readily transferable that the period for mitigation of loss following a tort or breach of contract in respect of those shares will generally be very brief. Assets that have a substantial physical bulk or lack an active market (such as structures and heavy equipment) will carry a more lengthy mitigation period; and gains that are made by dealing with the assets following the defendant's wrongful conduct in respect of those assets will be accounted for where they occur within that period . . ."

American Application of an Econometric Formula

A review of the American literature indicates that the Americans essentially apply the same legal principles to assess damages as a result of misrepresentation in a prospectus as is applied in English and Canadian jurisprudence, but have articulated a specific formula for calculating damages within the context of a class action proceeding. A difficulty arises with respect to the application of this formula to a Canadian context in that the American formula arises from the "fraud on the market theory" which has been specifically stated not to be applicable as a basis of liability in Canada. The Canadian court's difficulty with the "fraud on the market theory" appears to stem from the removal of the need to prove reliance. Although it can be noted at the outset that the Alberta *Securities Act* s. 203 deems reliance on a misrepresentation in a prospectus, it can further be argued that the measure of damage assessment resultant from the application from the fraud on the market theory is of value in a Canadian context.

The Fraud on the Market Theory

The fraud on the market theory is well summarized in the recent article by John A. Campion, "Misrepresentation in Class Proceedings: The Cardozo Nightmare?"[127] as follows:

> "The fraud on the market theory is a misnomer. It is in fact a way of proving reliance through a fiction of "market reliance", which assumes that every statement made in the market place affects the price of a stock and that therefore every purchaser of a stock has relied on every statement through this market impact. The integrity of the market establishes a fair and current price on openly traded securities. The defendant is presumed to have been misled in that the market was unable to correctly value the security due to the misrepresentation of the defendant. The price therefore diverged from its true value and caused damage to the plaintiff who sold at a price too low or purchased at a price too high. In these circumstances of a presumption of reliance, the investor is said to be relying upon the statement complained of because the price paid reflects each and every statement made about the stock in the marketplace.
>
> In fact, the investor will likely never have heard of the statement or the maker. The doctrine represents a form of deemed reliance and a

[127] (2001), 24 Advocates' Quarterly 129 at pp. 164, 165

> mechanism to prove aggregate damages through experts opinions on the impact of each statement on the market price.

And further paraphrasing from Joseph de Simone, "Should Fraud on the Market Theory Extend to the Context of Newly Issued Securities?":[128]

> The "fraud on the market theory" in the United States stems from the seminal case of *Basic Inc*. v. *Levinson* 108 S .Ct. 978, 1988 U.S. LEXIS 1197 (Supreme Court of the United States, 1987). In this case Basic Inc., a publically traded company on the New York Stock Exchange, was involved in merger negotiations with Combustion Engineering from September 1976 through December 1978. Rumours of a possible takeover caused the price and trading volume of Basic stock to increase throughout this period. During this period, however, Basic issued three statements denying knowledge of any reason for the stock's upward activity and specifically denying the existence of the merger negotiations. In December 1978, Basic notified the NYSE that it had been approached concerning a merger: it approved Combustion's tender offer the next day. The plaintiff class consisting of stock holders who had sold their shares during the class period alleged that defendant Basic and its directors artificially depressed the price of Basic stock throughout the class period, thereby injuring the plaintiffs who had sold their stock at depressed prices. The Supreme Court of the United States addressed the issue of whether the preliminary merger discussions were material and whether the district court properly applied the presumption of reliance supported by the fraud on the market theory.

In an oft-applied passage in *Basic* v. *Levinson*, Blackmun J., for the majority, stated:

[128] (1993), 61 Fordham Law Review 151

> "The fraud on the market theory is based on the hypothesis that, in an open and developed securities market, the price of a company's stock is determined by the available material information regarding the company and its business . . . Misleading statements will therefore defraud purchasers of stock even if the purchasers do not directly rely on the misstatements . . . The causal connection between the defendants' fraud and the plaintiffs' purchase of stock in such a case is no less significant than in a case of direct reliance on misrepresentations. "[129]

Canadian Rejection of the "Fraud on the Market Theory" as a Basis of Liability

The "fraud on the market theory" was rejected as a basis of liability by Winkler J. of the Ontario Court (General Division) in *Carom et al.* v. *Bre-X Minerals Ltd. et al.*[130] The plaintiffs were shareholders or former shareholders in Bre-X Minerals Ltd. and commenced class action proceedings under the Ontario *Class Proceedings Act*. They suffered losses when the value of Bre-X shares collapsed following the announcement that the alleged gold resources on the properties of Bre-X Minerals Ltd. were unsubstantiated due to fraud. The actions were brought against Bre-X, its officers, directors, and other insiders, two securities brokerages, stock analysts and the engineering companies which had analysed the alleged gold resources. The plaintiffs moved before Winkler J. to amend their statements of claim to add the "fraud on the market theory" as a basis of liability, and this application was dismissed. Winkler J. noted that the "fraud on the market theory" created a rebuttable presumption of reliance on the misrepresentations, thus obviating the need to prove such reliance on an individual basis.

Winkler J. concluded:

> "The adoption of the fraud on the market theory by an Ontario court cannot be justified when neither the statutory duty, the cause of action

[129] Applying *Peil* v. *Speiser* 806 F. 2d (C.A. 3, 1986)

[130] (1998), 41 O.R. (3d) 780

> founded upon this breach, nor the predominance test as a procedural barrier to class proceedings exist. More so, the plaintiffs seek to apply the theory to common law causes of action, to which it would not be applicable in the United States, and in a wholesale fashion, without the restrictions which circumscribe it there. Simply put, the proposition advanced is ill conceived.
>
> The torts of fraudulent and negligent misrepresentation are neither novel nor undeveloped in Canada. Both have been canvassed by the Supreme Court of Canada and the pronouncements of that Court on the elements of each must be considered to be settled law. In my view, the presumption of reliance created by the fraud on the market theory can have no application as a substitute for the requirement of actual reliance in either tort. In the context of the torts of fraudulent and negligent misrepresentation a presumption of the nature advocated for by the plaintiffs does not exist in Canadian common law. Indeed, to import such a presumption would amount to a redefinition of the torts themselves."

It should be noted that Winkler J. had further denied the right to proceed pursuant to negligent misrepresentation. This was upheld on appeal to the Ontario Superior Court of Justice Divisional Court[131] but overturned by the Ontario Court of Appeal.[132] Although the Ontario Court of Appeal allowed the claim for negligent misrepresentation to proceed within the context of the class action proceeding, however, it did not comment on the fraud on the action theory.

---

[131] (1999), 46 O.R. (3d) 315

[132] (2000), 51 O.R. (3d) 236

John A. Campion in "Misrepresentation in Class Proceedings: The Cardozo Nightmare?", summarized the reasons why the fraud on the market theory was rejected in *Carom*[133] as follows:

> "In coming to its conclusion, the Ontario court first observed that actual reliance was a necessary component under Canadian law where negligent or fraudulent misrepresentation was pleaded. The court went on to review the American law and concluded that the fraud on the market theory was a "rebuttable presumption of reliance on certain misrepresentations, obviating the need to prove such reliance on an individual basis". The court concluded that the theory was developed in a unique context of complaints founded on a breach of a statutory provision in American securities law, which provision was strictly limited to actual fraud and where there were no punitive damages and a shortened limitation period.
>
> The Canadian court in *Carom* v. *Bre-X* emphasized that the United States courts had refused to apply the doctrine in common law actions in the United States. The Ontario court observed that the Canadian legislation did not contemplate anything similar to the American legislation. The plaintiffs argued that the *Competition Act* was legislation similar to Rule 10b-5 in the United States, which thereby justified the use of the doctrine in Canada. The Ontario court found that any analogy between the *Competition Act* and the Rule 10b-5 was "flawed". In particular, the *Competition Act* was not restricted to fraudulent misrepresentation and the court therefore rejected any application of the theory to a cause of action relying upon the *Competition Act*.
>
> Finally, the Ontario court also noted that the fraud on the market theory had been developed under American Federal Rule 23, Class Action Requirements, where the common issues had to predominate over the individual issues. The Ontario court noted that the *Class Proceedings Act* in that jurisdiction expressly rejected the "predominance of common issues" test and the certification considerations in Ontario. As a result, class actions were not easily certified in Ontario and the theory was therefore not necessary to enable class actions in that context."

---

133 at pp. 165, 166

An earlier case which had not allowed the fraud on the market theory to be applied within a Canadian context is *Kripps* v. *Touche Ross & Co.,*[134] a decision of Boyd J. of the British Columbia Supreme Court (In Chambers). In this case the defendant prepared an audit report in respect of certain debentures offered by a corporation to the public. In the report the defendant expressed opinions without reservation or qualification to the effect that the financial statements for the periods noted complied with generally accepted accounting principles. In fact the financial statements failed to make provision for certain anticipated losses to the mortgage receivable portfolio. The plaintiff invested in the debentures and suffered loss. He sued the auditing firm, alleging that it was negligent in preparing the financial statement. He further sued the Superintendent of Brokers, alleging that it was negligent for not diligently scrutinizing the statement before approving the sale of the debentures. The defendant sought to strike out the pleadings on the ground that it disclosed no reasonable cause of action, and this application was allowed in part. The allegations of deemed reliance pursuant to the British Columbia *Securities Act* were rejected, an argument for deemed reliance at common law was rejected and a theory based on the US "fraud on the market theory" was also rejected. The court concluded that the "fraud on the market theory" was uniquely applied to a "nominate tort of breach of statutory duty" which was not available in Canada.

This was upheld by the British Columbia Court of Appeal, with Taylor J.A. stating with respect to an argument that there was presumed reliance pursuant to s. 141 of the British Columbia *Securities Act*:

> "It would be decidedly unusual that the legislature should establish a presumption without saying against whom it is raised, or for what purpose it is to have effect. When the words establishing the presumption are followed, as they are here, by words creating a right of action against a specific class of persons, a natural reading of this

---

[134] (1992), 52 B.C.L.R. (2d) 291

> section leads, in my view, to the conclusion that the presumption operates in actions against those persons. There then remains, in my view, no basis for applying the presumption in actions against anyone else."
>
> With respect to the "fraud on the market theory", Taylor J.A. stated:
>
> "The plaintiffs next invoke a doctrine said to be known in the United States as: "Reliance on the Integrity of the Market", or a variation on that doctrine contemplating reliance on the regulatory system. As I understand it, these doctrines obviate the need for proof of reliance on a particular defendant in stock market cases so long as it can be said that securities of the sort in question would not get on to the market without scrutiny, and that the security in question would not have passed scrutiny had the defendant acted carefully. For reasons which I have given in dealing with the present statutory scheme, it appears to me that there can be no basis for such reliance in this case because the scheme was not intended to assure buyers that only securities of a particular quality, or which meet particular criteria, will be put on the market. Reliance on the "integrity of the market" or the regulatory system by a potential lender, as an insurance that a proposed loan will be adequately secured, would in the circumstances of this case be unreasonable."

Cuming J. of the Ontario Superior Court of Justice implicitly rejected the American fraud on the market theory in *Mondor* v. *Fisherman*.[135] This case involved a class action proceeding under the Ontario legislation wherein the plaintiffs claimed on behalf of every person who had dealt in shares of YBM Magnex International Inc. and had suffered a loss as a result. They claimed on behalf of persons who had suffered losses through purchases of YBM shares in the secondary market. The plaintiffs alleged that YBM had been used to carry out a multi-layered conspiracy and fraud with several objectives, including the objective of laundering funds and obtaining improper gains from the sale of shares of YBM to the public for prices predicated upon a misrepresentation. The plaintiffs alleged that the innocent shareholders of YBM were misled because YBM circulated funds, in ever increasing amounts, through YBM, its sham suppliers and its customers.

---

[135] [2001] O.J. No. 4620

Cuming J. reviewed the law of misrepresentation and held that proof of reliance was a necessary ingredient in actions based upon negligent misrepresentation. The defendants argued that the plaintiff was implicitly arguing a fraud on the market theory, which was not a part of Canadian law.

Cuming J. referred to the cases of *Carom* v. *Bre-X Minerals Ltd.* and *Kripps* v. *Touch Ross & Co.* and stated: "The "fraud on the market theory" has been expressly rejected by Canadian courts because, *inter alia,* Canadian securities legislation does not include a similar concept, and that actual reliance is a necessary component under Canadian law concerning negligent and fraudulent misrepresentation."

The fraud on the market theory was also implicitly rejected by MacAulay J. of the British Columbia Supreme Court in *Collette* v. *Great Pacific Management Co.*[136]

The American Econometric Measure of Damages

Given the Canadian rejection of the "fraud on the market theory", one can anticipate strong objection to the application of the American econometric formula used to measure damages resultant from misrepresentation in a prospectus in a class action proceeding. This formula is based on the "fraud on the market theory". If one can overcome these objections, however, the formula is arguably very helpful. The legal principles underlying the application of the formula are the same as the common law principles which have already been reviewed.

An excellent overview of the general underlying principles is set out in Janet Cooper Alexander in "Rethinking Damages and Securities Class Actions".[137] She states:

---

[136] (2001), 86 B.C.L.R. (3d) 92

[137] (1996), 48 Stan. L. Rev. 1487

"1. The Measure of Damages in Rule 10b-5 Class Actions

In cases brought under Rule 10b-5, the generally accepted rule is that damages are calculated by the out-of-pocket method used in fraud cases. Purchasers are entitled to recover the difference between the price paid for the shares and the "true value" of the shares at the time of purchase. The "true value" or "intrinsic value" of the securities is taken to mean the price at which they would have traded in the absence of fraud - ie, if the true information had been disclosed.
In individual (non-class) actions, the calculation of damages is relatively straightforward. The number of shares and the date of the transaction are known with certainty, and the amount of the loss attributable to the violation, while not free from doubt, does not pose unusual problems of proof.

The problems of determining damages in class actions are different not just in degree, but in kind. The class damages are supposed to consist of the sum of the individual damages of each member of the class. Calculating the total class damages is a two-step process. The first step is to determine the "per-share damages", the amount of the actual market price attributable to the non-disclosure on each day of the class. The second step is to determine the aggregate damages of the class. To determine per-share damages, an expert economic witness constructs a "value line" which represents the "true value" of the stock - what purchasers would have been willing to pay if they had known the undisclosed information - on each day of the class period. The damages sustained by any particular member of the class can then, in theory, be determined by comparing the price actually paid with the value line for the date of the transaction.

The value line is a hypothetical construct. The most common method of estimating per-share damages is to start with the share price after disclosure of the relevant information, and then, through an event study, to isolate the effects of the withheld information from other factors, unrelated to the litigation, that may have affected the stock price between the time of the purchase and the time of the disclosure. Determining the value line is the least problematic aspect of the class action damages calculation, but it is subject to serious difficulties. The event study methodology depends on various debatable factual assumptions. As a result, the value line calculations of the experts for the two sides can differ greatly, even when they are using the same methodology. Moreover, even at its best the event study methodology can only calculate the price effect of the disclosure, which is not

> necessarily the same as the price effect of the information that was withheld. From the value line, one can determine each class member's damages. A member of the class who bought shares during the class period and held them until the close of the class period (typically the date when the bad news was finally disclosed) suffered damages of the difference between the price paid and the value line, multiplied by the number of shares purchased. If a plaintiff resold the shares during the class period, however, both the purchase price and the selling price were inflated by the non-disclosure. The windfall the plaintiff received on the sale must therefore be offset against the loss incurred on the purchase. If the value of the undisclosed information remained constant during the class period, these amounts would cancel each other out, and those who bought and sold during the class period ("in-and-out traders") would have no damages. If the value of the information fluctuated during the class period, in-and-out investors' damages would depend on the dates of their transactions.
>
> Related to this issue is the question of the number of shares in the class. Because some shares are bought and sold, often repeatedly, within the class period, the number of shares in the class is not simply the sum of the daily volume of trading during the class period. Indeed, the total daily trading volume may exceed the total number of shares outstanding. The methodology for calculating aggregate class damages must therefore include a procedure to account for in-and-out traders and to net out their windfalls against their losses . . ."

The formula to be used is suggested in the detailed article by Jon Koslow "Estimating Aggregate Damages in Class-Action Litigation Under Rule 10b-5 for Purposes of Settlement."[138] There are other key articles on damage calculation, including Bradford Cornall and R. Gregory Morgan, "Using Finance Theory to Measure Damages and Fraud in Fraud on the Market Cases";[139] Jared Tobin Finkelstein, "Rule 10b-5 Damage Computation: Application of Financial Theory to Determine Net Economic Loss";[140] Barry Reder, "Measuring Buyer's Damages in 10b-5 Cases";[141]

---

[138] (1991) 59 Fordham L. Rev. 811

[139] (1990), 37 UCLA L. Rev. 883

[140] (1983), 51 Fordham L. Rev. 838

[141] (1976), 31 The Business Lawy*er* 1839

Jared Specthrie and Zachary Starr, “Measuring Damages in Securities Class Actions”;[142] and Power C. Snow, Jr., Mary Lou Carp, Mary K. McEachron, “Damages in Securities Cases”.[143]

---

142 Practising Law Institute, *Securities Litigation, Prosecution and Defence Strategies* (1985)

143 Practising Law Institute, *Securities Litigation Prosecution and Defence Strategies* (1985)

Conclusion

As has been seen, section 203 of the Alberta *Securities Act*, which provides a civil remedy for damages for misrepresentation in a prospectus, has a long pedigree dating back to 1890 and the *Directors Liability Act* of England. The Alberta Act has also been influence by the "blue sky" legislation in the United States. There is much judicial authority to help us to interpret the civil liability provision over the years and with the aid of this case law general principles can be deduced to construct a thesis with respect to the measurement of damages for a misrepresentation in a prospectus. Complexities are introduced in measuring damages within the context of class action proceedings, but there is a wealth of American literature and jurisprudence which recommends the application of an econometric formula to this end. The authors hope that the distillation of the general principles and construction of a thesis with respect to measurement of damages for misrepresentation in a prospectus will be of aid to those practitioners seeking to measure damages under section 203 of the Alberta *Securities Act* and in analogous contexts.