OSLER

Ontario Court of Appeal provides guidance on the meaning of 'material change' under the Securities Act

MAY 31, 2023 10 MIN READ

Related Expertise

- Capital Markets
- Corporate and Securities Disputes
- Mining and Natural Resources

Authors: Craig Lockwood, Jeremy Fraiberg, Alan Hutchison, Elie Farkas

On May 24, 2023, the Court of Appeal for Ontario released two decisions, *Peters v. SNC-Lavalin Group Inc* (*SNC*) and *Markowich v. Lundin Mining Corporation* (*Lundin*), that provide helpful guidance on what constitutes a "material change" for the purposes of the disclosure requirements under the Ontario *Securities Act*.

Unlike a "material fact", which is any fact that would reasonably be expected to have a significant effect on the market price or value of the issuer's securities, a "material change" must involve "a change in the business, operations or capital" of the issuer. Determining whether and when there has been a change in an issuer's business, operations or capital often proves challenging.

The Court of Appeal endorsed a two-step analysis in determining whether a material change occurred. First, a court must consider whether the issuer has experienced a "change", broadly defined, which includes a change in risk in an organization's business, operations or capital. This step does not involve an assessment of the magnitude of the change. The second part of the court's analysis, as prescribed by the Act, necessarily involves a consideration of whether the change would reasonably be expected to have a significant effect on the market price of the issuer's securities. The Court of Appeal clarified that it is only at this second stage of the analysis that the court considers the magnitude or materiality of the change.

The *SNC* decision: an expansive definition of 'change'

In *SNC*, the plaintiff sought leave to commence a secondary market claim based on SNC's alleged failure to disclose the content of a September 4, 2018, phone call with the Department of Public Prosecutions Services of Canada (PPSC). On this phone call, SNC was advised that it would not be invited to negotiate a remediation agreement[1] that would have a resolved a pending prosecution against SNC for fraud and corruption.

At first instance, the motion judge denied the plaintiff's leave motion, holding that there was no reasonable possibility that the September 2018 call constituted a "material change" as defined under the *Securities Act*.

Under the *Securities Act*, a "material change" is "a change in the business, operations or

capital of the issuer that would reasonably be expected to have a significant effect on the market price or value of any of the securities of the issuer".

The motion judge held that the call was not a change in SNC's business, operations or capital because there was not a change in SNC's risk at that time. SNC faced the prospect of prosecution before the call and it continued to face that prospect after the call. Moreover, SNC continued negotiating a remediation agreement with the PPSC for over a month until the PPSC confirmed on October 9, 2018, that it would not grant SNC's request for a remediation agreement. SNC promptly disclosed this on October 10, 2018.

The plaintiff appealed, arguing that the motion judge had erred in his interpretation of "change" and in finding that the September 2018 call was not a material change.

The Court of Appeal dismissed the plaintiff's appeal, finding that the motion judge had ultimately adopted a very broad definition of "change" and that, even under this broad definition, the September 2018 call could not be seen as a change in SNC's business, operations or capital.

Justice Favreau, writing for the Court of Appeal, found that the motion judge correctly held that the meaning of "change" is fact-specific.

Rightly, in the view of the Court of Appeal, the only limit that the motion judge placed on what could constitute a "change" under the Act was that a "change" does not include external circumstances that do not result in a change in the issuer's business, operations or capital, even if they might affect the issuer's share price. Unlike the motion judge in *Lundin* (as discussed below), the motion judge in *SNC* did not improperly read a "magnitude" element into the meaning of "change" under the Act.

The Court of Appeal also rejected the plaintiff's argument that the motion judge had failed to consider that a "change" could include a change in risk to an issuer's business, operations or capital. Rather, the Court concluded that the motion judge correctly considered this very issue and simply held, on the evidence before him, that there was no reasonable prospect of the September 2018 call being found at trial to constitute a change in the risk that SNC's business faced. The risk that SNC would be prosecuted was already known to investors at the time of the September 2018 call, and the call did not change that risk.

The *Lundin* decision: 'a change is a change'

As we discussed in our 2022 Legal Year in Review, in *Lundin*, the plaintiff sought leave to commence a statutory secondary market claim based on alleged delays in Lundin's disclosure of wall instability and an eventual rockslide at its copper mine in Chile. Lundin did not disclose these events until roughly one month after the rockslide occurred, following which its share price declined significantly. The plaintiff argued that these events constituted "material changes" requiring immediate disclosure.

As these issues arose in the context of a leave motion under the *Securities Act*, the plaintiff merely had to satisfy the court that there was a "reasonable prospect of success at trial". The motion judge ultimately held that the plaintiff had established a reasonable chance of proving that the impugned events were "material" because they would reasonably be expected to have a significant impact on the market value of Lundin's securities. However, the judge nonetheless held that they were not "material changes" as contemplated by the *Securities Act*.

The motion judge held that neither the pit wall instability nor the rockslide constituted a

"change" to Lundin's business, operations or capital because these were anticipated, inherent risks in Lundin's open pit mining operations that did not prevent Lundin from continuing to engage in its business of copper mining. The motion judge's narrow interpretation of the word "change" was premised on the term "material change" being defined more narrowly than the term "material fact" in the *Securities Act*.

The Court of Appeal reversed the motion judge's decision and granted the plaintiff leave to proceed with its statutory secondary market claim.

Justice Favreau, writing again for the Court of Appeal, held that the motion judge erred in interpreting the phrase "change in the business, operations or capital of the issuer" too narrowly, particularly in the context of a motion for leave where the plaintiff needed only to demonstrate a "reasonable possibility of success" based on a "plausible interpretation of the statute and the evidence."

In so doing, the Court of Appeal endorsed a two-step analysis for determining whether there has been a "material change". First, the court must determine whether the has been a "change in the business, operations or capital of the issuer". Second, the court must determine whether the change was "material" such that it would be expected to have a significant impact on the value of the issuer's shares. The Court held that the motion judge erroneously read a "magnitude" requirement into the first part of this test, when questions of magnitude should generally be left to the second part.

Relying on the Supreme Court's decision in *Kerr v. Danier Leather*, the Court of Appeal held that the distinction between a "material change" and a "material fact" does not focus on the magnitude of the change but instead focuses on whether the change was *external* to the company as opposed to whether the change was *internal* to the business, operations or capital of the company. A "material fact" can be external to the company, whereas a "material change" generally cannot.

In assessing whether the wall instability and rockslide constituted changes in Lundin's business, operations or capital, the Court ultimately concluded that the motion judge should not have limited his inquiry to whether Lundin had completely changed directions in its lines of business, stopped operating its mine or changed its capital structure. Rather, so long as the change was not "external to the company without a resulting change in the business, operations or capital of the company", the motion judge should have found the first part of the "material change" test to be satisfied.

The Court also held that the phrase "business, operations or capital" is broad. "Operations", for example, can refer to a broad range of changes within a company including, as was the case in *Lundin*, an interruption in production and a change in scheduling due to an accident or equipment failure.

Applying the correct interpretation, the Court held that the plaintiff had in fact satisfied its burden of showing a "reasonable possibility" of establishing that the wall instability and rockslide were "changes" in Lundin's "operations".

In allowing the plaintiff's appeal in *Lundin*, the Court endorsed the broad, fact-specific interpretation of "change" prescribed by the motion judge in the *SNC* case, emphasizing that "a change is a change and it should be defined broadly, especially in the context of a leave motion".

Key takeaways

The Court of Appeal's companion decisions in *Lundin* and *SNC* affirm the distinction between material facts and material changes. Certain disclosure documents, like a prospectus, must include disclosure of all material facts. The obligation to make timely disclosure is limited to the occurrence of a material change.

Issuers and their advisors often find it difficult to distinguish between a material fact and a material change. An example of a material fact that is typically not a material change is merger negotiations. While the fact that the merger negotiations are ongoing may reasonably be expected to have a significant effect on the price of the issuer's securities, there is generally not a change in the issuer's business, operations or capital until a decision is made to proceed with the transaction. In other cases, it is not as easy to make this distinction.

Other challenges can emerge when a change evolves over time. For example, the *Lundin* case involved an open pit mine. These types of mining operations illustrate the difficulties of identifying when a material change actually crystallizes. Mine pit walls in open pit mines are continuously monitored and where stability issues emerge, often it takes time to manifest into a full pit wall failure. Issuers are typically reluctant to publicly disclose until the situation is fully understood to ensure disclosure is full and complete when made, especially for changes that require technical analysis. Issuers will have to make decisions around when to make disclosure and whether it is better to make earlier disclosure — even if determination of materiality is incomplete — or wait until that determination is known and take the risk of claims for not disclosing earlier.

The Court of Appeal's decisions confirm that the two-part test for a "material change" under the *Securities Act* consists of two distinct inquiries — whether there has been a change and, if so, whether it is material — and that the term "change" should be given a broad interpretation.

This latest guidance from the Court of Appeal is also a reminder that issuers should closely monitor events that may bear upon their business, operations or capital, and must remain vigilant in ensuring that they comply with their continuous disclosure obligations under the *Securities Act*.

---

[1] As we discussed in a previous post, on September 19, 2018, the *Criminal Code* was amended to enact a remediation agreement regime, allowing prosecutors to negotiate agreements to resolve criminal prosecutions against organizations in exchange for compliance with certain conditions.