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No Need to Disclose "Unsolicited, Inexpert, Premature and Unreliable" Opinions

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Overview

The Court of Appeal for Ontario has confirmed that a public company acted properly and lawfully when it decided not to disclose to the investing public an opinion received from an external consultant that questioned the economic viability of the company's main asset, in circumstances where the company honestly and reasonably believed the consultant was incorrect.

In *Wong v Pretium Resources* (*Wong*, 2022 ONCA 549), the Court of Appeal upheld a 2021 decision of the Superior Court of Justice (2021 ONSC 54) that dismissed a securities class action against Canadian mining company Pretium Resources Inc.

The 2021 decision of the Superior Court was the first-ever merits determination in an action brought under the secondary market liability misrepresentation provisions of the Ontario *Securities Act* or equivalent provisions of securities legislation in other Canadian provinces and territories. A "misrepresentation" is defined in the *Securities Act* as (i) an untrue statement of "material fact" or (ii) an omission to state a "material fact" that is required to be stated or that is necessary to make a statement not misleading in the light of the circumstances in which it was made. A "material fact" is defined as a fact that would reasonably be expected to have a significant effect on the market price or value of the securities. Cases of this nature therefore frequently turn on the "materiality" of information that supposedly ought to have been disclosed.

The plaintiff's claims of misrepresentation related to Pretium's decision not to disclose concerns raised by one of its external consultants, Strathcona Mineral Services, regarding negative mineral sampling results at Pretium's flagship Brucejack Project. Pretium honestly and reasonably believed that the concerns raised by Strathcona were premature and unfounded, and that the sampling results were unrepresentative and inaccurate. Strathcona had proffered an unsolicited and clearly erroneous opinion concerning matters that were outside "its own lane." The company's board of directors and principal external mineral resource consultant concurred that the opinion was wrong. In these circumstances, Pretium decided not to disclose Strathcona's concerns.

Strathcona subsequently resigned over Pretium's decision not to disclose its concerns. Pretium had no choice but to issue a news release announcing the resignation, and within days the share price of Pretium had declined by more than 50%. Class action litigation against Pretium was promptly commenced and was pursued even though Pretium was ultimately proven right when the complete sampling results became available months later. Those results confirmed that Strathcona's concerns were misplaced.

Key Takeaways

- A plaintiff's success in obtaining leave of the Court to proceed with secondary market misrepresentation claims under the *Securities Act* is not determinative of the ultimate disposition of the case on a motion for summary judgment or at trial. The test for leave to proceed involves a preliminary assessment of the merits of the case; a plaintiff need only establish a reasonable possibility of prevailing at trial. That is a different standard from the "balance of probabilities" standard that a plaintiff must ultimately satisfy to prove liability.
- The objective reliability of a concern or opinion expressed by an external consultant can be central to the assessment of the materiality, and therefore "disclosability," of the concern or opinion. Courts may, however, view with skepticism after-the-fact

proclamations of unreliability. Reporting issuers should consider documenting contemporaneously their assessment of important reports and opinions received from external consultants.

- Materiality must not be assessed with the benefit of hindsight. Although Pretium was ultimately correct in its determination that Strathcona's concerns had no merit, what mattered was the objective unreliability of those concerns at the time they were expressed (rather than the results of processing the entire bulk sample).
- When assessing the materiality of information, public companies should understand that courts will not defer to the business judgment of executives concerning disclosure obligations. The Supreme Court of Canada made clear in *Kerr v Danier Leather Inc.* (2007 SCC 44) that the business judgment rule "should not be used to qualify or undermine the duty of disclosure." Here, however, the Court of Appeal rejected the argument that the Motion Judge had effectively adopted the business judgment rule in determining that Strathcona's concerns were unreliable and did not need to be disclosed.
- Although the definition of "material fact" in the *Securities Act* refers to the impact of a fact on the market price or value of an issuer's securities, issuers should also consider and apply the "reasonable investor" test when making disclosure decisions.

The Decision Raises an Important Issue

At the heart of the Court of Appeal's decision is a question that cuts to the core of securities legislation in Canada: What test should companies apply when making important decisions about the materiality of information and their disclosure obligations, particularly when the information in question consists of a negative opinion concerning key assets or aspects of the business?

Background

In 2011, Pretium began a mineral exploration program at the Brucejack Project, an underground gold mining project located in northwestern British Columbia. In November 2012, Pretium retained Snowden Mining Industry Consultants to review the initial results of the mineral exploration program and to conduct a mineral resource estimate for the Brucejack Project. Another third-party consultant then used that estimate to prepare a Feasibility Study, which was issued in June 2013. The Feasibility Study concluded that the Brucejack Project contained enough gold to support an underground bulk-mining operation.

Given that the validity of the Feasibility Study depended on the accuracy of the underlying mineral resource estimate, Snowden recommended that Pretium test a 10,000 tonne bulk sample to verify the findings of the mineral resource estimate. Pretium hired Strathcona to oversee and report on the bulk sample program. When the custom mill that was going to be used to process the bulk sample proved unavailable, Pretium agreed to use a sample tower testing method as an additional and interim method of evaluating the bulk sample. Notably, the sample tower required testing of only a tiny fraction of the entire 10,000 tonne bulk sample that was intended to be tested in the bulk sample program. The remainder was shipped to a mill in Montana for processing.

Results from the sample tower testing were unfavourable to Pretium and did not support the mineral resource estimate that was the foundation of the Feasibility Study. In a series of emails and letters, Strathcona communicated to Pretium that the findings of the sample tower did not validate the mineral resource estimate and strongly urged Pretium to publicly disclose the sample tower findings that Strathcona believed rendered the mineral resource estimate, and therefore the Feasibility Study, "materially inaccurate" and "unreliable." Strathcona did so even though it was not retained to opine on the mineral resource estimate in this manner. As the Court of Appeal put it, Strathcona acted outside "its own lane" in providing its unsolicited opinion to Pretium.

Given both the small sample size used for purposes of the sample tower and the potential for a high degree of variability in the 10,000 tonne bulk sample, Pretium disagreed that the sample tower results were determinative. Pretium instead decided to defer public disclosure concerning the results of the bulk sample program until the final results from processing the entire 10,000 tonne bulk sample were available. The investing public was already taking a "wait-and-see" approach, because Pretium had made clear to the market that it would provide a report once the bulk sample program had been fully completed.

On October 7, 2013, Strathcona resigned from the bulk sample program in protest, which Pretium disclosed in a news release two days later. On October 22, 2013, Pretium issued another news release that summarized the reasons Strathcona had given for its resignation and explained the company's own view that Strathcona's concerns were baseless. During the 13 days between those two news releases, Pretium's share price fell by more than 50%.

Months later, Pretium was vindicated when the results of the sample tower were shown to be inaccurate. Upon completion of the bulk sample program, the findings of the mineral resource estimate were confirmed – in fact, more gold than expected was processed from the bulk sample. An updated Feasibility Study was prepared in 2014 and the mine ultimately entered into commercial production in 2017.

Leave to Proceed

Under the secondary market liability provisions of the *Securities Act*, claims of misrepresentation cannot be pursued absent leave of the Superior Court.

As described in a Davies bulletin, dated May 31, 2018, to the surprise of public company executives and advisers, the plaintiff's initial motion for leave to proceed was granted in 2017. The Ontario Superior Court of Justice found that there was a reasonable possibility that the action would be resolved in favour of the plaintiff. The action was subsequently certified as a class proceeding in 2019.

In 2020, the parties brought competing summary judgment motions. The same Justice of the Superior Court who had granted leave to proceed ruled in favour of Pretium and dismissed the class action in its entirety, concluding that (i) Pretium had committed no actionable misrepresentation; and (ii) in the alternative, Pretium conducted a reasonable investigation into Strathcona's concerns and had therefore made out the affirmative defence provided for in section 138.4(6) of the *Securities Act*.

The plaintiff appealed the dismissal of the action to the Court of Appeal.

The Positions of the Parties

On appeal, the plaintiff argued that the Motion Judge had erred in law in determining what constituted an actionable "misrepresentation." The plaintiff challenged the Motion Judge's conclusion that Strathcona's concerns did not constitute a material fact that was required to be disclosed because those concerns were "unsolicited, inexpert, premature, and unreliable."

Pretium argued that the Motion Judge correctly ruled that it had made no misrepresentation. Members of Pretium's senior management had discussed Strathcona's concerns internally and with Snowden, and had determined that those concerns were premature and unreliable such that they did not have to be disclosed.

The Decision

The Court of Appeal dismissed the plaintiff's appeal in its entirety.

The Motion Judge Did Not Err in Considering the Reliability of Strathcona's Opinion

In dismissing the action, the Motion Judge found as a fact that Strathcona's concerns were unreliable for two reasons. First, the sample tower findings were inherently unreliable because they were based on samples that were not necessarily representative of the mineral deposit. Second, Strathcona's testing methodology was not appropriate in view of the unique characteristics of the deposit. The Motion Judge held that the unreliable opinion of Strathcona was not a "material fact" that required disclosure.

The plaintiff argued that the reliability of information is not relevant to a determination of the materiality of that information, and that consequently the Motion Judge erred in considering the reliability of Strathcona's concerns. The Court of Appeal disagreed. It affirmed that, in the circumstances of this case, the objective reliability of those concerns was a relevant consideration. The Motion Judge's finding that Strathcona's opinion was unreliable was entitled to deference.

Importantly, both the plaintiff and Pretium agreed that the legal framework for assessing the materiality in a case of "misrepresentation by omission" is set out in the decision of the Supreme Court of Canada in *Sharbern Holding v Vancouver Airport Centre Ltd.*, 2011 SCC 23 (*Sharbern Holding*). That case stands for the proposition that the standard for materiality is whether a reasonable investor would consider the information in question important in making an investment decision. Materiality must be determined objectively from the perspective of a reasonable investor, rather than based on the subjective views of the company. Put somewhat differently, there must be a substantial likelihood that the reasonable investor would have viewed the omitted fact as significantly altering the total mix of information available.

The Court of Appeal acknowledged that there is some case law that suggests that a "market impact" test, rather than "reasonable investor" test, should be applied to assess materiality in secondary market misrepresentation cases. The Court left open the question of whether the two tests are the same or whether one or the other is appropriate in all or particular cases. Nothing turned on the distinction between the two tests, because both parties agreed that the materiality of an omitted fact is governed by the principles established in *Sharbern Holding*.

In *Sharbern Holding*, the requirement to disclose all material information does not impose on issuers an obligation to disclose all facts that would permit an investor to sort out what is material and what is not. On the contrary, such disclosure would overwhelm investors with information and impair their ability to make decisions.

The Court affirmed that it is inimical of the objectives of the *Securities Act* – which include investor protection – to require every marginal fact to be disclosed. The Court of Appeal was mindful of this in confirming that Strathcona's objectively unreliable opinion did not have to be, and indeed ought not to have been, disclosed.

The Motion Judge Did Not Defer Inappropriately to Pretium's Business Judgment

The Court of Appeal rejected the plaintiff's argument that the Motion Judge's decision was based on a *post hoc* evaluation of materiality and deferred inappropriately to Pretium's subjective opinions and business judgment. Rather, there was significant and contemporaneous evidence that Pretium, its board of directors and Snowden considered the concerns expressed by Strathcona to be highly dubious, premature and outside Strathcona's "own lane." The Motion Judge did not conduct his analysis through the distorted lens of hindsight.

The Motion Judge Did Not Err by Failing to Infer Materiality from the Share Price Decline

Finally, the Court of Appeal rejected the plaintiff's argument that the Motion Judge erred by failing to infer materiality from the decline in the market price of Pretium's shares following the announcement of Strathcona's resignation. Even where it is obvious that a misrepresentation has been "publicly corrected," the occurrence of a share price decline following the public correction is not determinative of materiality (though it is relevant). Here, there was no evidence that the decline in Pretium's share price was tied to disclosure of Strathcona's concerns. It is impermissible to reason backward from a share price decline to a finding of materiality.

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