Ontario Securities Commission | Commission des valeurs mobilières de l'Ontario | 22nd Floor, 20 Queen Street West, Toronto ON M5H 3S8 | 22e étage, 20, rue Queen Ouest, Toronto ON M5H 3S8

Citation: Caldwell Investment Management Ltd. (Re), 2018 ONSEC 50
Date: 2018-10-12
File No. 2018-36

IN THE MATTER OF
CALDWELL INVESTMENT MANAGEMENT LTD.

REASONS AND DECISION ON A DISCLOSURE MOTION

Hearing:	September 27, 2018	
Decision:	October 12, 2018	
Panel:	D. Grant Vingoe	Vice-Chair and Chair of the Panel
Appearances:	Derek Ferris Raphael Eghan	For Staff of the Commission
	Rene Sorell Shane D'Souza	For Caldwell Investment Management Ltd.

TABLE OF CONTENTS

REASONS AND DECISION ON A DISCLOSURE MOTION

I. BACKGROUND

A. Introduction

[1] On June 14, 2018, Staff of the Ontario Securities Commission (the **Commission**) commenced an enforcement proceeding against Caldwell Investment Management Ltd. (**CIM** or the **Respondent**) by issuing a Statement of Allegations.

[2] Staff have alleged that, among other things, CIM failed in its obligation to provide best execution of equity and bond trades for its clients contrary to section 4.2 of National Instrument 23-101 *Trading Rules* between January 1, 2013 and November 15, 2016 (**Relevant Period**) by sending to its affiliated dealer trades of securities with excessive commissions or mark-ups.

[3] On September 17, 2018, CIM brought a motion for an order that Staff disclose:

i. documents and information in Staff's possession as to what procedures are followed and what reasonable efforts are typically taken by OSC-regulated advisors to achieve best execution of orders, including the foregoing in relation to:

(a) discussions between Staff and witnesses or potential witnesses, experts and potential experts or other third parties;

(b) researching and preparing Concept Paper 23-402 *Best Execution and Soft Dollar Agreements*, OSC Staff Notice 33-748 *Annual Summary Report for Dealers, Advisors and Investment Fund Managers* (page 63 to 65), and OSC Staff Notice 33-734 *2010 Compliance and Registrant Regulation Branch Annual Report* (pages 24 and 25);

(c) performing compliance reviews of OSC-regulated advisors during the Relevant Period and responses from such advisors, redacted in each case to protect confidentiality; and

ii. documents and information in Staff's possession concerning the comparative commission rates as between affiliated and unaffiliated dealers, including the foregoing in relation to:

(a) commissions or bond spreads charged by unaffiliated dealers; and

(b) best execution practices, including quantitative information, and written policies and procedures, redacted for confidentiality.

B. Chronology of Events

[4] On July 3, 2018, Staff provided CIM with some disclosure at the first attendance. The disclosure consisted primarily of documents provided by CIM to Staff during Staff's investigation.

[5] By Commission Order, dated July 5, 2018, Staff was ordered to file and serve a witness list and serve a summary of each witness' anticipated evidence on CIM and indicate any intention to call any expert witness by no later than October 11, 2018.

[6] On July 31, 2018, CIM requested from Staff, among other things, information known to Staff as to what procedures are followed and what reasonable efforts are typically taken by OSC-regulated advisors to achieve best execution, and materials cautioning advisors from sending orders to an affiliated dealer or prescribing the terms upon which such orders can be sent.

[7] On August 23, 2018, CIM requested information about fixed income spreads or charges.

[8] On August 24, 2018, Staff responded to CIM's requests for information. Staff indicated that it would not provide information as to what procedures are followed and what reasonable efforts are typically taken by OSC-regulated advisors to achieve best execution of orders for bond and equity trades when acting for clients. They took the position that this information is not directly relevant to Staff's allegations, and that the request is overly broad and objectionable on the basis of confidentiality.

[9] Staff also provided a binder of materials to CIM including:

i. Concept Paper 23-402 *Best Execution and Soft Dollar Arrangements*

ii. Comment Letters received for Concept Paper 23-402

iii. Mutual Fund Governance – Cost Benefit Analysis – Final Report prepared for the OSC by Keith A. Martin, July 2003

iv. OSC Staff Notice 33-748 *Annual Summary Report for Dealers, Advisors and Investment Fund Managers*

v. OSC Staff Notice 33-734 *2010 Compliance and Registrant Regulation Branch Annual Report*

vi. In the Matter of Staff's Recommendation to Impose Terms and Conditions on the Registration of Acker Finley Asset Management Inc.

[10] On August 30, 2018, Staff advised CIM that it plans to call an expert to testify concerning equity commission rates and bond spreads and that the name of any expert and the issues to which the expert is expected to testify will be provided in accordance with the Commission's *Practice Guideline*[1]. Staff further indicated that any information obtained to date from third parties concerning commission rates and bond spreads is privileged and falls outside Staff's disclosure obligations.

[11] On September 10, 2018, in response to further communications between CIM and Staff, Staff advised CIM that it had retained one expert, and spoken to others.

[1] *Ontario Securities Commission Practice Guideline* (2017), 40 OSCB 9009.

[12] On September 21, 2018, Staff advised CIM that Vidis Vaiciunas (**Vaiciunas**) has been retained as an expert and provided the issues upon which he is expected to testify. Staff also advised that they intend to call a bond expert but that no bond expert has been retained and they would provide the information to CIM if an expert is retained.

[13] Staff's Factum filed with respect to the Motion, dated September 26, 2018, indicates that Staff had caused the relevant branches of the Commission to seek to retrieve the information and materials underlying Staff reports described in sub-paragraph i.(b) of paragraph [3] above that is potentially relevant to the allegations against CIM or responsive to the request for procedures to achieve best execution.

[14] Staff provided a confidential binder of documents (**Disclosure Binder**) to the Panel at the motion hearing related to discussions with Vaiciunas and potential experts so that I could assess whether each of these documents needed to be disclosed to CIM. This binder was accompanied by a log (**Disclosure Log**) identifying each numbered document by date, description and reason for non-disclosure, which was provided to CIM's counsel. Aside from the retainer agreement with Vaiciunas included after Tab 1 in the Disclosure Binder (**Retainer Agreement**), where Staff indicated that they will consider whether this document needs to be provided when an expert's report is delivered, Staff refused to provide any of the documents in the binder to CIM's counsel based upon an assertion of litigation privilege.

[15] It appears from the Disclosure Log that the only third-party witnesses or potential witnesses that Staff has had discussions with that may be responsive to the Respondent's disclosure demands are Vaiciunas and potential experts that Staff have considered retaining.

II. THE ISSUES

[16] The issues to be decided are:

i. Does litigation privilege apply to the materials related to discussions with Vaiciunas and potential experts set out in the Disclosure Binder or are they required to be disclosed to the Respondent in order to enable the Respondent to make full answer and defence?

ii. Does Staff have to disclose materials to the Respondent related to the best execution practices and procedures of other OSC registrants obtained through the Commission's regulatory programs, including such information for firms that use affiliated dealers to execute orders on behalf of their clients, in order to enable the Respondent to make full answer and defence, or are such materials either irrelevant to the allegations against CIM and/or subject to confidentiality considerations making disclosure of such materials inappropriate in the public interest?

iii. Should an order be issued to require Staff to produce the materials underlying Staff reports described in paragraph [13]?

III. THE POSITIONS OF THE PARTIES

[17] The parties agree that Staff's disclosure obligation is set out in *R v Stinchcombe*[2] and that Staff is obligated to take a "generous view" of relevance[3].

[18] There was also general agreement that if an expert or potential expert provided relevant facts to Staff that, if disclosed to the Respondent, would assist the Respondent in its defence, such factual information would need to be disclosed. A clear example would be if it turned out that the expert or potential expert had direct knowledge of CIM's commission rates for a particular client not otherwise in Staff's possession, this factual information would have to be disclosed.

A. CIM

[19] CIM submits that Staff is obliged to provide CIM with the views, opinions and analysis of others it has approached, even potential experts it has not retained. CIM submits that there are several cases, including *Stinchcombe*, that support that the right to make full answer and defence can overcome litigation privilege.

[20] CIM further submits that to defend itself (on the merits or at a sanctions hearing) and to make tactical decisions, it is critical to know what best execution procedures and reasonable efforts were undertaken by other OSC-regulated advisors to achieve best execution and the actual execution charges of OSC-regulated advisors during the Relevant Period, as well as all of the information in Staff's possession that speaks to the best execution standards applicable to advisors during the Relevant Period.

[21] CIM submits that pursuant to *Stinchcombe* standards and *Deloitte*, Staff's disclosure obligation includes material that has a "reasonable possibility of being relevant" to a respondent's ability to make full answer and defence. This includes material that can be used to rebut the case presented by Staff, advance a defence, or material that may assist them in making tactical decisions.[4] Further, CIM submits that Staff must err on the side of disclosure unless the information is "clearly irrelevant", as expressed in *Re Biovail Corp*[5].

[22] CIM expressed that they need the requested information to assess whether its procedures were consistent with industry standards during the Relevant Period. CIM submits that this information is central to the allegations against them and is needed to make a defence. CIM submitted that this is especially true where the proceeding involves the first time a violation is asserted in a Commission enforcement proceeding involving an industry practice since such practice could be relevant to both a determination of whether a violation occurred or in the consideration of sanctions.[6]

[23] CIM submits that confidentiality concerns with regard to information received by Commission staff through its examinations of its registrants or otherwise can be

---

[2] [1991] 3 SCR 326.
[3] *Deloitte & Touche LLP v Ontario (Securities Commission)*, [2002] OJ No 2350 (Ont Ca) aff'd 2003 SCC 61, at para 41 (***Deloitte***).
[4] *Deloitte*, at paras 40-41.
[5] 2008 ONSEC 14, (2008), 31 OSCB 7161, at paras 15 and 32.
[6] CIM cites *R. v. Hudson*, 2016 NUCJ 7 (***Hudson***), a decision of the Nunavut Court of Justice, not binding upon this panel, as an example where a court ordered disclosure of observations by a prosecuting agency as to whether the gear of other fishing vessels drifted into prohibited fishing waters during prior years as potentially relevant to a due diligence defence by the accused.

dealt with by appropriate redactions of identifying information and undertakings by the Respondent.

B. Staff

[24] Staff submits that disclosure of privileged documents are not captured under Rule 27 of the Commission's *Rules of Procedure and Forms*[7]. Staff considers the notes of discussions with Vaiciunas and potential bond experts to be the subject of litigation privilege and therefore expressly excluded from Staff's disclosure obligation.

[25] Staff submit that the two conditions for litigation privilege are that the communication with third parties must have been specifically made with existing or contemplated litigation in mind and the privilege only attaches if the dominant purpose of the third-party communication is to assist in possible forthcoming litigation. Staff cites the Supreme Court's decision in *Lizotte v Aviva Insurance Company of Canada*[8] which emphasized the importance of litigation privilege as fundamental to the functioning of our legal system and concluded that litigation privilege cannot be abrogated without clear, and explicit legislative language to that effect.

[26] Staff submit that the zone of privacy in adversarial proceedings is fully engaged with respect to initial dealings with Vaiciunas, and it continues to be engaged now that he's been asked to prepare an expert report. They submit that early communications and dealings pre-Statement of Allegations cannot be distinguished from the post-Statement of Allegations and that the same principles apply across the board and apply to all notes regarding communications with Vaiciunas.

[27] Staff submit that Vaiciunas and the potential bond experts are not fact witnesses and that any notes from meetings or telephone calls evidencing preliminary views or opinions are more akin to preliminary views or opinions from a draft report.

[28] Relying on *Moore v Getahun*[9], *Simons v Canada (Minister of Public Safety and Correctional Service)*[10], *Maxrelco Immeubles Inc v Jim Pattison Industries (c.o.b. Pattison Sign Group)*[11], and *2060619 Ontario Inc. v Durham (Region Municipality)*[12], Staff's position is that in the same manner that litigation privilege prevents draft reports from being generally disclosed, litigation privilege also applies to prevent any preliminary opinions or views expressed by Vaiciunas from being disclosed.

[29] Staff further submits that the best execution procedures of other OSC-regulated advisors identified during compliance reviews are irrelevant to the allegations made against CIM and its ability to make full answer and defence to those allegations since the circumstances of each firm in relation to the services it offers its client base are highly fact specific.

---

[7] (2017), 40 OSCB 8988.
[8] 2016 SCC 52, at para 65.
[9] 2015 ONCA 55.
[10] 2018 ONSC 3741.
[11] 2017 ONSC 5836.
[12] 116 LCR 39.

[30] Staff submits that the policies and procedures of other advisors are irrelevant in a vacuum and must be viewed in conjunction with a particular advisor's conduct and specific business model, including size, nature, and number of funds and/or accounts it may manage.

[31] Staff also submits there are public interest considerations that support its position that the documents should not be provided, namely, (i) the need to preserve third party confidentiality; (ii) the need for transparency between Compliance and Registrant Regulation Branch Staff and registered firms; and (iii) ensuring proceedings are conducted in a just, expeditious and cost-effective manner.

[32] With respect to CIM's request for documents and information related to Concept Papers and Staff Notices, Staff submits that this issue is premature as the request for this information is recent and Staff is in the process of determining what information, if any, they have and whether the information is relevant.

IV. ANALYSIS

1. Information and materials related to Vaiciunas and potential experts

[33] Having reviewed the Disclosure Binder, I find, with one exception, that the materials that were included do not contain facts requiring disclosure by Staff. They contain background information related to the qualifications and experience of Vaiciunas and the potential experts who are identified in these materials, and information regarding the general approaches to best execution considered by these individuals.

[34] These documents came into existence when an enforcement proceeding was within reasonable contemplation. These documents form a very partial outline of considerations that may be reflected in an expert report. They are properly regarded as materials constituting partial draft expert reports, which are within the scope of litigation privilege. Such materials are within the zone of privacy necessary to enable Staff to prepare its case within and are subject to litigation privilege.

[35] Since an expert report, if relied upon by Staff, will be provided to the Respondent, there is no compelling reason to subordinate the privilege to a need to disclose to allow for full answer and defence.

[36] Paragraphs (4) to (6) of Rule 27 of the Commission's *Rules of Procedure* prescribe the requirements related to disclosure of the intention to rely on expert evidence and experts' reports. The Respondent is asking us to rewrite these rules to provide earlier and much more extensive disclosure concerning expert and potential expert evidence on the asserted constitutional ground that it would be helpful to the Respondent in making full answer and defence.

[37] The Respondent takes issue with Rule 27 in a very general sense. However, this Rule was designed to provide fair disclosure to enable respondents to meet the case against them, while preserving an appropriate scope for Staff to assert litigation privilege and to have discussions with its experts and potential experts and be involved in reviewing successive drafts of expert reports without the entire process of producing an expert report being open to scrutiny by a respondent. Except for the one instance described below, nothing in the

Disclosure Binder revealed relevant facts of the kind described in the example in paragraph [18] that would require disclosure.

[38] If the Respondent wished to challenge the constitutional efficacy of Rule 27, this would be a matter of general importance requiring compliance with Rule 31 requiring notice of the constitutional question to the Attorneys General of Canada and Ontario. They did not provide this notice, so the broader question of the constitutionality of Rule 27 is not before this panel.

[39] The one exception, where I find that Staff must make disclosure, is the last handwritten notation, consisting of four lines of text, in Tab 24 beginning with "CSL" at the left margin in which the notes reflect that certain facts were imparted outside of the person's role as a potential expert. This is directly relevant factual information involving a recollection of events occurring when the person was performing other responsibilities and when the expert role was not in contemplation.

2. Information and materials related to other OSC registrants

[40] I am persuaded by Staff's argument that data related to commission rates and mark-ups arising from individual examinations by OSC Staff of other registrants are not relevant to the case against CIM.

[41] At issue based upon the Statement of Allegations are CIM's best execution practices measured against the applicable regulatory standard. Business models, services that are either included or not included in these compensation metrics, range of securities, markets and client types will all vary among firms. Firm practices will also evolve over time and will be subject to the exercise of discretion in administering these practices within each firm and for reasons that may be very specific to individual circumstances or clients. Without such accompanying analysis and history, raw data and written policies will be factually irrelevant to the case against CIM. There is no principle that would require Staff to afford such an accompanying detailed analysis to the Respondent to accompany any factual data that is produced.

[42] In the absence of such analysis, the raw materials demanded by the Respondent will not be helpful in its defence and it is highly speculative whether such material could ever be helpful to the Respondent even if all the surrounding facts were known for each firm whose materials would be disclosed.

[43] In addition, based on the Respondent's very broad demand, this information would likely involve the entire universe of OSC-registered portfolio managers. In addition to a lack of relevance, this production would be a very onerous task that would adversely affect the efficiency of a proceeding of this kind.

[44] The need for the overlay of detailed analysis necessary to make the requested information of any potential utility to the Respondent distinguishes this case from *Hudson* where the fact at issue was whether fishing gear merely crossed a fishery border, a matter requiring limited cartographical analysis.

[45] In addition, the disclosure of commission and mark-up data and procedures for the entire universe of Ontario-regulated portfolio managers would undermine registrants' expectations of confidentiality in the examination process. While firms may understand that such documents may, in appropriate cases, have to be disclosed pursuant to discovery obligations, it would be highly unexpected

that this extensive disclosure, of no practical utility to the Respondent without an overlay of analysis, would be an anticipated use of their regulatory information.

[46] Disclosure in these circumstances would have a negative effect on the candor expected of registrants in the examination process and would therefore undermine the ability of the Commission to carry out its mandates of investor protection and fair and efficient capital markets.

[47] The Respondent itself is an experienced player in the Canadian portfolio management business. It knows who its competitors are. It also knows that it would likely face loud objections from those firms if it asked for their information by name. Those firms are very much the parties in interest if their information may be disclosed, and yet they are not parties to the proceeding in which the need for such disclosure and the practicality of confidentiality restrictions are assessed. The confidentiality of this examination information and the fact that the affected parties whose information would be disclosed are not heard on this motion are additional reasons for denying disclosure in this case.

[48] This again is very distinct from *Hudson* where the conduct at issue was physical conduct occurring in the open, capable of being assessed by any vessel in the area whose personnel wished to make those observations.

3. Information and materials underlying Staff Reports

[49] Since Staff is seeking to retrieve from off-site locations and assess whether it will provide additional information or materials as described in paragraph [13] above, and the results of these efforts and Staff's position with regard to any materials retrieved are not yet known, this matter remains hypothetical at this stage, with no need for urgency since the merits hearing has not yet been scheduled.

[50] I also find that it is premature to address the Retainer Agreement pending Staff's consideration of whether it will be disclosed in connection with the delivery of an expert report.

[51] If these issues require consideration of a disclosure order in the future following a new motion, the potential timing involved can then be considered by the panel at that time in relation to what is transpiring in the proceeding at that stage.

V. CONCLUSION

[52] For the foregoing reasons, the Respondent's motion is denied with the exception of the one item described in paragraph [39].

Dated at Toronto this 12th day of October, 2018.

"D. Grant Vingoe"
D. Grant Vingoe