

# Ontario Court Of Appeal Releases Highly Anticipated Decision On Insider Trading In Finkelstein V Ontario Securities Commission

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The Ontario Court of Appeal has released its eagerly-awaited decision in the latest chapter of the Finkelstein et al. insider trading and tipping case saga, which has captured the attention of both the legal and investment industries since the allegations **first came to light**. In **Finkelstein v. Ontario Securities Commission**, the Court interpreted and clarified the application of the insider trading and tipping scheme in the Ontario Securities Act. However, the decision is equally important for its application of the law surrounding the role of the reviewing court when decisions are appealed.

The Ontario Securities Commission ("OSC") initiated administration proceedings against five individuals for breaches of the Act's insider trading and tipping provisions and acting contrary to the public interest. Specifically, the OSC alleged that material, non-public information ("MNPI") about Masonite International Corporation ("Masonite") flowed through a chain of five people, originating with Mitchell Finkelstein, a Toronto lawyer working on a takeover bid involving Masonite. Finkelstein informed an investment advisor friend in Montreal, Paul Azeff, of material facts about the bid. In turn, Azeff informed a Montreal accountant, L.K., who passed on the information to the appellant, Howard Miller, an investment advisor in Toronto, who then conveyed the information to his associate, Francis Cheng, an investment advisor of the same firm.

In its Merits Decision, the OSC hearing panel (the "Panel") found that Finkelstein, Azeff, Bobrow, Miller, and Cheng were in a special relationship with Masonite and had informed others of MNPI regarding Masonite, and that found Azeff, Miller, and Cheng each purchased Masonite securities with knowledge of MNPI. The Panel imposed administrative sanctions on the five individuals. All five appealed those decisions. The Divisional Court dismissed the appeals of Finkelstein, Azeff, Bobrow, and Miller, but allowed Cheng's appeal. Miller sought and obtained leave to appeal to the Court of Appeal, as did the OSC in respect of Cheng.

There was no dispute that Miller and Cheng received MNPI about Masonite, and that they did not have actual knowledge that their tipper was in a special relationship with Masonite or another person in a special relationship with Masonite. Rather, at issue on appeal was the Panel's interpretation and application of s. 76(5)(e) to find that Miller and Cheng "ought reasonably to have known" that their respective tippers stood in a special

relationship with Masonite.

The Ontario Court of Appeal's decision included the following findings:

1. The factors identified by the Panel in its decision can be used as a reasonable guideline when conducting an analysis under the "person connection" test in s. 76(5)(e) of the Act, which requires demonstrating that the recipient of MNPI "ought reasonably to have known" that the person who provided the information was in a special relationship with the issuer. These factors include, inter alia, the relationship between the tipper and tippee, the professional qualifications of the tipper and the tippee, the detail of information passed on, the time between the receipt of information and the initiating of a trade, and the presence or absence of intermediate steps to verify the information before executing a trade
2. The reasonableness of the factors in the "ought reasonably to have known" **inquiry turns on their relevance to the inference drawing process - an important** aspect of insider trading and tipping cases, given that these cases are decided primarily on circumstantial evidence. The Court gave a number of helpful examples of fact scenarios and the possible inferences that could be drawn based on the application of the factors.
3. The Divisional Court subjected the Panel's findings of fact against Cheng to "an intense parsing", leading that court to conclude the Panel had made three kinds of factual errors: (i) the Panel misstated certain evidence; (ii) the Panel drew inferences from the facts with which the Divisional Court took issue; and (iii) the Panel appeared to have not taken into account several pieces of evidence. Unfortunately, the Divisional Court succumbed to the "standing temptation" of a reviewing court conducting a reasonableness review to place itself in the position of the decision-maker. The Court of Appeal found that the Divisional Court overstepped the appropriate bounds of appellate review by engaging in its own inference-drawing exercise, and re-weighting the evidence against Cheng. The Panel's findings of fact were reasonable supported by the evidence, and the Divisional Court was not entitled to substitute inferences it would make for those reasonably available to the Panel.

The Court of Appeal ultimately dismissed Miller's appeal, and allowed the OSC's appeal. Having allowed the OSC's appeal with respect to Cheng's liability, the Court also considered whether Cheng's sanctions were reasonable. The Court rejected Cheng's argument that the sanctions against him were unreasonable.

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