Ontario's Divisional Court confirms regulatory rules do not create fiduciary duties

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Like other participants in Canada's financial sector, investment advisors are often named as defendants in proposed class actions. However, such cases are not always certified, in part because of the idiosyncratic nature of client-advisor relationships. The Divisional Court's recent decision in *Boal v. International Capital Management Inc.*, 2022 ONSC 1280 (*Boal*) continues this trend, and serves as a reminder that investment advisors do not automatically owe fiduciary duties to their clients, notwithstanding the strict regulatory rules that apply to advisors.

What you need to know

- In *Boal*, the Divisional Court affirmed a decision of Justice Perell that refused to certify a proposed class action against investment advisors and a mutual fund dealer.
- A majority of the Divisional Court stressed that determining whether investment advisors owes fiduciary duties to their clients is not a "one-size-fits-all" exercise.
- *Boal* is a reminder that strict regulatory rules, including a "best interests of the client" standard and a duty to deal "fairly, honestly and in good faith", are not dispositive of whether investment advisors owe fiduciary duties to their clients.

Investment advisors and fiduciary duties

In Canada's common law provinces, the relationship between clients and financial professionals such as investment advisors and stockbrokers is not presumed to be fiduciary in nature. Instead, based upon the facts of a particular case, clients may be owed *ad hoc* fiduciary duties. The existence of an *ad hoc* fiduciary duty is determined under a contextual, multi-factor analysis. The relevant factors of the analysis include a client's vulnerability, the degree of discretionary power exercised by the alleged fiduciary and applicable professional rules or codes of conduct.

Background

The representative plaintiff, Ms. Boal, commenced a proposed class action in February 2017 arising from her purchase of a high-interest promissory note from her investment advisor.

In her claim, Ms. Boal alleged that her investment advisor, his colleague, and their mutual fund dealer had failed to properly disclose that the promissory notes were issued by a company that was controlled by the investment advisors and their family members. Ms. Boal, who was an accredited investor, sought to represent a class of at least 170 clients and asserted numerous causes of action against a number of defendants, including the investment advisors and mutual fund dealer.

By the time of certification motion in December 2020, the proposed class members had not suffered any investment losses, and it appeared unlikely that they would do so in the future. Accordingly, at certification, Ms. Boal focused solely on causes of action that do not require proof of loss, such as breach of fiduciary duty.

The certification motion

In January 26, 2021, Justice Perell of the Superior Court dismissed the certification motion in its entirety.

Although the two investment advisors and the mutual fund dealer conceded that there was a legally-tenable breach of fiduciary duty against them, Justice Perell rejected this concession. In concluding that the breach of fiduciary duty claim "does not have a reasonable chance of success on a class wide basis", Justice Perell stressed that the pleaded claim was at odds with the *ad hoc* nature of fiduciary duties that investment advisors may owe their clients.

In Justice Perell's view, Ms. Boal's argument that the defendants' regulatory obligations grounded a fiduciary duty owed in common to all proposed class members turned "the law of fiduciary duties for investment advisors backwards, upside down, and inside out". After observing that the existence of an *ad hoc* fiduciary duty in the investment advisor context depends on the particular factual circumstances of each advisor-client relationship, Justice Perell concluded that: "in each individual case, it is contestable whether the relationship with the investor was a fiduciary relationship, and in each individual case the breach of any fiduciary duty is idiosyncratic and not common."

Because Justice Perell concluded that the breach of fiduciary duty claim was not certifiable, he refused to certify accessory claims for knowing assistance and knowing receipt that Ms. Boal asserted against certain other defendants.

The Divisional Court dismisses the appeal

Ms. Boal appealed to the Divisional Court, seeking to overturn Justice Perell's refusal to certify the breach of fiduciary duty, knowing assistance and knowing receipt claims. In a decision released on March 1, 2022, the Divisional Court upheld the decision of Justice Perell, albeit in a split decision.

In a lengthy dissent, Justice Sachs concluded that Justice Perell had erred in principle regarding the breach of fiduciary duty claim. According to Justice Sachs, Justice Perell

failed to appreciate the significance of the strict regulatory standards to which the defendants were subject to as registrants of both the Mutual Fund Dealers Association and the Financial Planning Standards Council. As Justice Sachs noted, these regulatory rules impose strict obligations to deal fairly, honestly and in good faith with clients and to address conflicts of interest in the "best interest of the client".

In her brief majority reasons, Justice Kristjanson (joined by Justice McWatt) upheld Justice Perell's decision. According to Justice Kristjanson, recognizing a class-wide fiduciary duty based upon the pleaded claim would have "inappropriately" turned one factor (*i.e.* regulatory rules) into "the sole factor in determining whether an *ad hoc* fiduciary duty exists", thereby distorting the multi-factor analysis. Justice Kristjanson also expressed concern that imposing fiduciary duties on investment advisors based solely on regulatory rules would be antithetical to the *ad hoc* nature of such duties, and "could have a significant impact on elements of the capital markets including those with restricted advice business models (like many mutual fund dealers), and could have significant negative effects on both investors and capital markets." As the knowing assistance and knowing receipt claims required a viable underlying breach of fiduciary duty claim, Ms. Boal's appeal of these claims was also dismissed.

Further implications

Although the appeal heard by the Divisional Court dealt solely with the legal viability of the breach of fiduciary duty claim asserted by Ms. Boal, Justice Perell also concluded that there was insufficient evidence that the common issue and preferable procedure criteria of the *Class Proceedings Act* were met.

It bears noting that future proposed class actions against investment advisors in Ontario will face an additional hurdle in light of the recently-enacted requirements (which we have previously summarized) that common issues "predominate" over individual issues and that a class action be "superior" to all other "reasonably available means" as a means of adjudicating proposed class members' claims. The "predominance" and "superiority" requirements may be especially difficult to establish in cases such as *Boal* due to the idiosyncratic nature of client-advisor relationships.

By

Adrian Pel

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BLG Offices

Calgary

Centennial Place, East Tower
520 3rd Avenue S.W.
Calgary, AB, Canada
T2P 0R3

T 403.232.9500
F 403.266.1395

Ottawa

World Exchange Plaza
100 Queen Street
Ottawa, ON, Canada
K1P 1J9

T 613.237.5160
F 613.230.8842

Vancouver

1200 Waterfront Centre
200 Burrard Street
Vancouver, BC, Canada
V7X 1T2

T 604.687.5744
F 604.687.1415

Montréal

1000 De La Gauchetière Street West
Suite 900
Montréal, QC, Canada
H3B 5H4

T 514.954.2555
F 514.879.9015

Toronto

Bay Adelaide Centre, East Tower
22 Adelaide Street West
Toronto, ON, Canada
M5H 4E3

T 416.367.6000
F 416.367.6749