

**IN THE MATTER OF AN APPEAL TO THE APPEAL COMMITTEE
OF THE CANADIAN INVESTOR PROTECTION FUND**

RE: [REDACTED]; [REDACTED]
[REDACTED]

Heard: 2 February 2015

PANEL:

ANNE WARNER LA FOREST

Appeal Committee Member

APPEARANCES:

[REDACTED]

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[REDACTED]

James Gibson

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Counsel for Canadian Investor
Protection Fund Staff

DECISION AND REASONS

Introduction and Overview

1. [REDACTED] and [REDACTED] (the “Appellants”) were clients of First Leaside Securities Inc. (“FLSI”), an investment dealer through which over 1200 customers made investments in various affiliated companies, trusts, and limited partnerships (collectively the “First Leaside Group”). FLSI was registered with the Ontario Securities Commission (“OSC”) and was a member of the Investment Industry Regulatory Organization of Canada (“IIROC”). It was also a member of the Canadian Investor Protection Fund (“CIPF” or the “Fund”) until it was suspended by IIROC on February 24, 2012, the same date FLSI sought protection under the *Companies' Creditors Arrangement Act*. The relevant history leading up to these events and the role of CIPF with respect to claims to the Fund are set out in detail in the Appeal Committee's decision dated October 27, 2014.¹

2. FLSI was declared to be insolvent on February 24, 2012. The following investments were made by the Appellants:

- i [REDACTED] purchased 50,000 units of First Leaside Universal Limited Partnership on July 16, 2010 for a total investment of \$50,000 and received a distribution of \$3,052 from the insolvency proceedings for a net claim of \$46,947.95; and
- ii [REDACTED] made investments in a number of First Leaside products between May and September 2011 for a total investment cost claim of \$321,344.06.

3. The Appellants sought recovery from the CIPF on the basis that FLSI was a Member of CIPF and as such the Appellant was entitled to protection through the Fund, which was established to provide coverage in the event of insolvency. CIPF Staff made a decision denying compensation

¹ This decision is available on the CIPF website and will be referenced throughout as the “October 27, 2014 decision”.

to the Appellant on the basis that the Appellant's losses did not arise as a result of the insolvency of FLSI and thus were not covered under the CIPF Coverage Policy dated September 30, 2010.

4. On February 2, 2015, an Appeal Committee Member of CIPF's Board heard the Appellants' appeals. The main issue in each appeal was whether to depart from the decision of CIPF Staff that denied compensation for losses suffered by the Appellant. The appeals were scheduled to be heard together at Neeson Arbitration Chambers in Toronto, Ontario but because inclement weather prevented the Appellants from being physically present and with the Appellants' consent, the hearing proceeded instead by means of teleconference.

Chronology of Events Relevant to the Appellants' Claims

5. As noted above, [REDACTED] had purchased 50,000 units in First Leaside Universal Limited Partnership in May 2010. This investment was held off book and was delivered out to the Appellant on July 19, 2010.

6. [REDACTED] personally became an investor with FLSI in 2011. His investments are listed, in summary as follows:

- i 151,603 units of First Leaside Wealth Management Fund purchased May 12, 2011 (60,460 units), July 21, 2011 (30,580 units) and August 10, 2011 (60,563);
- ii 845 units of First Leaside Flex Fund (Class B) on September 8, 2011;
- iii 100,000 units of Special Notes Limited Partnership on September 8, 2011; and
- iv 100,000 units in First Leaside Holdings Limited Partnership on June 9, 2011.

7. The total value of these investments was \$352,448.00. Mr. [REDACTED] received distributions of \$31,103.94 through the insolvency proceedings in relation to his investments in First Leaside Holdings Limited Partnership. His net claim is \$321,344.06. His investments in the investments in the First Leaside Wealth Management Fund and Flex Fund (Class B) were held on book in a registered retirement account and were transferred to Fidelity in December of 2012 following

FLSI's insolvency. His investments in the Special Notes Limited Partnership and the First Leaside Limited Partnership were held off-book and were delivered out to Mr. [REDACTED] on September 9, 2011 and June 9, 2011 respectively.

8. The investment made by [REDACTED] was made in the period following which the OSC had begun to investigate FLSI and Mr. [REDACTED]'s investments were all made following the retention of the firm of Grant Thornton Limited who was responsible for reviewing, reporting on, and making recommendations in relation to the First Leaside Group's business, assets, affairs, and operations. The Appellants were not aware of the investigation or the review or report of Grant Thornton at the time that their investments were made.

The Appellants' Application for Compensation

9. The Appellants applied to CIPF for compensation for their losses in investments made through FLSI prior to the October 12, 2013 deadline for submitting claims that was set by the CIPF Board of Directors. The Appellants also provided additional information regarding the claim and specifically, on claim forms dated March 15, 2012, the Appellants indicated that the amount claimed was due to the default of an issuer of securities.

10. By letters dated January 30, 2014, the Appellants were advised that CIPF Staff was unable to recommend payment of their claims. The relevant parts of the letter read as follows:

[REDACTED]: At the date of insolvency, the security [in First Leaside Universal Limited Partnership] was not held by, or in the control of, FLSI. As an indication of this, you provided a copy to CIPF of the security that you held in certificate form. Since the security was not held by, or in the control of, the insolvent Member at the date of insolvency, the loss is not one that is eligible for CIPF coverage.

In addition, you indicated that your loss, or part of it, was a result of "the default of the issuer of securities". As mentioned above, losses resulting from the default of an issuer of securities are not covered by CIPF.

[REDACTED]: With respect to the securities that you purchased [in First Leaside Wealth Management Fund and First Leaside Flex Fund (Class B)], they were properly recorded in the books and records of FLSI at the date of insolvency. These securities were transferred to an account in your name at another IIROC Dealer Member subsequent to February 24, 2012.

At the date of insolvency, the securities [in Special Notes Limited Partnership and First Leaside Holdings Limited Partnership] were not held by, or in the control of FLSI. As an indication of this you provided copies to CIPF of the securities that you held in certificate form. Since the securities were not held by, or in the control of, the insolvent Member at the date of insolvency, the loss is not one that is eligible for CIPF coverage.

In addition, you indicated that your loss, or part of it, was a result of "the default of the issuer of securities". As mentioned above, losses resulting from the default of an issuer of securities are not covered by CIPF.

11. The Appellants provided a written response to the decision of the CIPF staff on May 18, 2014.

Analysis

12. The Appellants made arguments in their correspondence mentioned above. Many of the arguments raised by the Appellants are similar to those that were addressed in the October 27, 2014 decision and in this regard, we rely upon our analysis in that decision at paragraphs 27 through 49. The Appellants emphasized certain arguments in relation to their own circumstances.

13. First, the Appellants stated that their understanding was that the funds they invested would be invested in products for the primary purpose of funding the acquisition and/or development of various real estate products. They argued that their investments were not used for the intended investment purpose, but rather were unlawfully converted by the First Leaside Group for its own uses during a period when there was an OSC investigation and review by Grant Thornton Limited. As we have indicated in other decisions, the Appeal Committee is of the view that the Appellants' claim is really one of fraud, material non-disclosure and/or misrepresentation and does not fall within the meaning of the phrase "including property unlawfully converted".

14. In their submissions, the Appellants write as follows:

In the result, between January 2009 (by which time First Leaside was well aware of its untenable financial position and significant regulatory concerns regarding the inappropriate use of customer's funds) through to November 2011, FLSI solicited and accepted and proceeded to use the Claimed Funds for its own purposes in a manner which was contrary

to my rights in and to that money-all the while intentionally misleading me as to why First Leaside actually acquired, and how it intended to use my money.

This is in effect a claim for misrepresentation and providing coverage therefore would amount to creating a new head of coverage in the Coverage Policy.

15. Second, the Appellants' submissions focussed on the fact that FLSI had marketed itself to customers as being a CIPF member since 2004. As we indicated in the October 27, 2014 decision, the CIPF brochure does outline limitations on coverage. Furthermore, any misrepresentations in relation to CIPF were made by FLSI and oversight of members is within the jurisdiction of IIROC.

16. Third, the Appellants objected to the statement on their claims summary that their assets had no value. In their view, the "N/A" in relation to values means "not available". I would agree with the Appellants on this matter. Since the investments made in the First Leaside Group were in unlisted securities, their valuation was supplied by that Group and were not determined independently. When the First Leaside Group was placed into insolvency, there was no further information available as to the value of the investments.

17. For its part, CIPF Staff submitted that the Coverage Policy provides for custodial protection and that the question for the Appeal Committee is whether Appellants' property was returned to them. In this case the Appellants acknowledged that they were in possession of the certificates representing their off-book investments and the Appellants' units in other investments had been transferred to another IIROC Member after the insolvency of FLSI. Thus, even though the OSC and IIROC had found that the principals of FLSI had engaged in misleading representation and induced the investment of funds, there has not been a loss of property.

18. The Appeal Committee has considerable sympathy for the Appellants. Unfortunately, their submissions do not give rise to a successful claim for compensation from CIPF.

Disposition

19. The appeal is dismissed. The decision of the CIPF Staff is upheld.

Dated at Toronto, this 6th day of March, 2015.

Anne Warner La Forest