

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

RE: [REDACTED] and [REDACTED]

March 25, 2015

WRITTEN APPEAL CONSIDERED BY:

BRIGITTE GEISLER

Appeal Committee Member

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 1,200 customers made investments in various affiliated companies, trusts and limited partnerships (collectively the “First Leaside Group”). FLSI was registered with the Ontario Securities Commission 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 its suspension by IIROC on February 24, 2012, being the same date that FLSI was declared to be insolvent and 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

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

2. The Appellant [REDACTED] invested \$105,118 in various First Leaside Funds and Partnerships. He also received a stock dividend for a value of \$2,449 and submitted an undocumented claim amount of \$1,953.87 for a total claim of \$109,520.87. He is also claiming additional interest. The Appellant [REDACTED] invested \$11,613 and claimed a further \$68.29 as a credit balance, for a total claim of \$11,681.29 and interest.

3. The Appellants sought recovery from CIPF on the basis that FLSI was a Member of CIPF and as such the Appellants were entitled to protection through the Fund which was established to provide coverage in the event of insolvency. CIPF Staff made a decision denying compensation to the Appellants on the basis that the Appellants' 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. The Appellants requested that their appeal be considered on the basis of written materials which they provided.

Chronology of Events Relevant to the Appellants' Claim

(i) The Appellants' Investments and Claim

5. The claim arises from

- a. the Appellant [REDACTED]'s purchase of
 - i. 20,000 units of First Leaside Fund Series B Trust Units on February 3, 2009 in an RRSP account;
 - ii. 5,000 units of First Leaside Properties Class B Trust Units on May 1, 2009 in a TFSA account;
 - iii. 20,000 units of First Leaside Fund Series C Trust Units on December 21, 2009. Stock dividends were received for a total of 1,979 stock dividends on December 31, 2009 and April 15, 2011;
 - iv. 5,000 units of First Leaside Fund Series B Trust Units on December 23, 2009 and a further 5,000 units of February 1, 2010 in an RESP account;

- v. 5,000 units of First Leaside Fund Series C Trust Units on January 8, 2010 in a TFSA account. A stock dividend for 470 units was received on April 15, 2011;
 - vi. 1,087 units of FLEX Fund Class C Trust Units on October 5, 2011 in a TFSA account;
 - vii. 4,031 units of FLEX Fund Class C Trust Units on October 5, 2011 in an RRSP account; and
 - viii. 40,000 units of First Leaside Venture Limited Partnership on October 11, 2011.
- b. the Appellant [REDACTED]'s purchase of
- i. 5,000 and 5,000 units of First Leaside Fund Series B Trust Units in a TFSA account, on June 12, 2009 and February 24, 2010, respectively; and
 - ii. 1,613 units of FLEX Fund Class C Trust Units on October 5, 2011.

6. The total amount of the investments made, stock dividends and credit interest claim is \$109,520.87. The claim for interest is not specified. The Appellant's investments were transferred to accounts in the Appellants' names at Fidelity Clearing Canada ULC ("Fidelity") following FLSI's insolvency, with the exception of the certificate for 40,000 units of First Leaside Venture Limited Partnership which was delivered to the Appellant [REDACTED].

(ii) The Appellants' Application for Compensation

7. The Appellants applied to CIPF on June 20, 2012 for compensation for their losses in investments made through FLSI. By letters dated February 10, 2014, the Appellants were advised that CIPF Staff were unable to recommend payment of their claim. The relevant parts of the letters reads as follows:

[REDACTED] and [REDACTED]: CIPF does not cover customers' losses that result from other causes such as dealer misconduct, changing market values of securities, unsuitable investments or the default of an issuer of securities.

██████████: With respect to the securities that you purchased and which are described in Table 1 below², they were properly recorded in the books and records of FLSI at the date of insolvency. Those securities were transferred to accounts in your name at another IIROC Dealer Member subsequent to February 24, 2012. In addition, at the date of insolvency, the security described in Table 2 below³ was not held by, or in the control of, FLSO. Therefore, the loss is not one that is eligible for CIPF coverage, as indicated above.

██████████: With respect to the cash held in your account, and the securities purchased and which described in the table below⁴, they were properly recorded in the books and records of FLSI at the date of insolvency. Those cash and securities were transferred to an account in your name at another IIROC Dealer Member subsequent to February 24, 2012.

Analysis

8. The Appellants relied upon arguments which had been raised by Representative Counsel for the investors of FLSI. These arguments were dealt with in detail in the October 27, 2014 decision, in particular, in paragraphs 27 through 49. They also made further submissions.

9. The first argument focused on the interpretation of the phrase “including property unlawfully converted” in the Coverage Policy. The Appeal Committee is of the view that the adoption of these arguments suggests that the Appellants' claim is really one of fraud, material non-disclosure and/or misrepresentation which does not fall within the meaning of the phrase "including property unlawfully converted". CIPF coverage is custodial coverage, to provide assurances to the public that their securities will be returned to them in the event of the insolvency of a Member. To apply the suggested interpretation would, in effect, create a new head of coverage, one not contemplated in the CIPF mandate.

10. The other main argument raised in the Representative Counsel submissions related to the exercise of discretion by the Appeal Committee under the Coverage Policy. As was indicated in the October 27, 2014 decision, the Appeal Committee is bound to exercise its discretion within the

² See paragraph 5 (a) (i) to (vii) for details of the securities.

³ See paragraph 5 (a) (viii) for details of the security.

⁴ See paragraph 5 (b) for details of the security.

limits of the CIPF mandate which is to provide custodial coverage to customers in the event of the insolvency of a Member. While the Coverage Policy provides a residual discretion, it is limited to cases where the application of the Policy might result in an outcome that frustrates or defeats the purpose of the compensation scheme. It is not intended to use discretion to create a new head of compensation such as misrepresentation or the default of an issuer. The Appeal Committee's discretion is limited to the Coverage Policy which, in general terms, provides for the return of the Appellant's property. In this case, the Appellants' investments were held by FLSI at the date of insolvency and were subsequently transferred to Fidelity or had previously delivered to them a certificate representing their investment.

11. The Appellants submitted that their investments were made while the principals of FLSI were aware of the Grant Thornton Report and that to have done so was fraudulent conduct. In review of the dates of the investments, it appears that approximately two-thirds of their investments pre-dated the Grant Thornton Report. They further submitted that the Ontario Securities Commission should not have allowed this fraudulent conduct to happen. They noted that the public relies upon the regulations, especially when all of the documentation described FLSI as being IIROC and CIPF members. They were disappointed that the regulatory structure failed to protect their investments and indicated that they had lost faith in that structure.

12. As stated above, the purpose of CIPF coverage is limited to custodial coverage. As was indicated in the October 27, 2014 decision, the CIPF brochure outlines limitations on coverage. Furthermore, had any misrepresentations in relation to CIPF been made, they were made by FLSI. Oversight of members is primarily the jurisdiction of IIROC, with additional oversight by the Ontario Securities Commission.

13. As in the October 27, 2014 decision, while the Appeal Committee has considerable sympathy for the Appellants' position, I conclude that their submissions in this appeal are not persuasive and do not give rise to a successful claim for compensation from CIPF.

Disposition

14. The appeal is dismissed. The decision of CIPF Staff is upheld.

Dated at Toronto, this 25th day of March, 2015.

Brigitte Geisler

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