

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

RE: [REDACTED] and [REDACTED]

Heard: December 9, 2015, by teleconference

HEARD BEFORE:

BRIGITTE GEISLER

Appeal Committee Member

APPEARANCES:

Nicolas Businger

)

Counsel for Canadian Investor
Protection Fund Staff

)

[REDACTED]

)

On his own behalf

)

On her own behalf

)

On behalf of [REDACTED]

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 (“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 its suspension by IIROC on February 24, 2012, being the same date that FLSI was declared to be insolvent and the day after

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 in relation to an appeal heard on October 27, 2014.¹

2. 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.

3. On December 9, 2015, an Appeal Committee Member of CIPF's Board heard an appeal to determine whether to depart from the decision of CIPF Staff. The appeal hearing was held by teleconference. The Appellants and [REDACTED] were in attendance and made submissions.

Chronology of Events Relevant to the Appellants' Claim

(i) The Appellants' Investments and Claim

4. The claim arises from the Appellants' purchases of securities through FLSI for a total net claim of \$59,133 by [REDACTED] and \$197,595.76 by [REDACTED]. These claims include claims for stock dividends and a reduction of \$15,331.24 by [REDACTED] with respect to her purchase of 150,000 units in First Leaside Progressive Limited Partnership. At the hearing, the Appellants removed their claim for 90 King St. East MPOC 6% 16Feb16, thus reducing their claim to \$43,460 by [REDACTED] and \$187,595.76 by [REDACTED].

5. Certificates representing the Appellants' purchases were transferred to accounts in the names of the Appellants at Fidelity Clearing Canada ULC or were delivered to their possession.

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

(ii) *The Appellants' Application for Compensation*

6. The Appellants applied to CIPF for compensation for their losses in investments made through FLSI. By separate letters dated April 25, 2014, the Appellants were advised that CIPF Staff were unable to recommend payment of their claims. The relevant parts of the letters read as follows:

Regarding your claim for unlawful conversion, it does not appear to us that any property held by FLSI for you was converted or otherwise misappropriated. In addition, as a basis for explaining your claim, you stated: "Suffered a financial loss solely as a result of the insolvency of FLSI." While you have not provided evidence of the truth of all of the assertions in support of your claim, losses caused by dealer misconduct, compliance failures or breaches of securities regulatory requirements in respect of the distribution of securities are not covered by CIPF. The securities that you purchased were subject to the disclosure of an offering memorandum or other offering documentation which, among other things, disclosed the risks relevant to the purchase and the investment. These investments, like any securities, were subject to market forces and, unfortunately, your loss appears to have been a loss caused by a change in the market value of your investments and not a loss resulting from the insolvency of FLSI.

Analysis

7. [REDACTED] spoke on behalf of the Appellants indicating that they wanted a clearer understanding of why CIPF Staff had denied their claim. He noted that in 2011, the regulatory bodies were aware that there was insufficient capital in the First Leaside entities to sustain their existence without the input of additional funds and wanted to understand why steps were not taken earlier to protect investors. He queried why CIPF Staff was taking the position that the Appellants' losses were as a result of a change in market value, rather than the insolvency of FLSI.

8. Counsel for CIPF Staff explained that CIPF is not a regulatory body; it has no powers to investigate or to discipline member firms. That authority lies within IIROC and/or the OSC. IIROC's regulatory function relates to the business and operations of FLSI. It does not have jurisdiction over the various proprietary products that were marketed by FLSI to various investors. Those products, or issuers, are under the jurisdiction of the OSC, which, having concerns over those

operations, began an investigation into the First Leaside Group in the fall of 2009. The jurisdiction of IIROC, and by extension, CIPF, within the limits of its mandate, is confined to FLSI only.

9. CIPF's relationship to its Members is the collection of fees, which are calculated on the basis of the amount of equity in customer accounts on the books and records of the Members. Some oversight of the audit and supervisory function of IIROC is performed; however, the responsibility for enforcement of compliance with industry rules lies primarily with IIROC, and in the case of the First Leaside Group entities, also with the OSC.

10. Counsel for CIPF Staff described the origins of CIPF and the restrictive nature of CIPF coverage. CIPF's mandate is to provide coverage that is custodial in nature; in other words, to ensure that the clients of an insolvent member have received their property. The Appellants have received their property; accordingly the issue of CIPF coverage is not applicable. It is most unfortunate that the value of the property is uncertain; however, the Coverage Policy clearly states that CIPF does not cover "changing market values of securities, unsuitable investments, or the default of an issuer of securities".

11. As stated above, CIPF does not guarantee the value of an investment. We have heard from many appellants who have stated that they were told that their investments were safe because there was CIPF coverage. It is correct that they were safe, in that they would be returned to the investors in the event of an insolvency, but it seems that it was implied and believed by many investors that the coverage extended far beyond a return of property and included a "guarantee" of the principal of their investment. It does not.

12. [REDACTED] queried as to the protection for investors in the event of fraud or improper conduct. Counsel for CIPF Staff advised that while regulatory bodies can discipline securities industry registrants, they do not have the power of granting restitution. To recover funds, it would be necessary to sue the firm and/or the investment advisor; in this case, the chances of recovery against FLSI are slim in that the firm has become insolvent. Counsel noted that Quebec has a

government regime which provides some limited compensation to investors in the event of fraud; however, this is unique to Quebec and not available elsewhere in Canada.

13. [REDACTED] stated that all of the marketing documentation for the First Leaside Group had included CIPF logos, which led them to believe that they had insurance coverage. They now feel that the coverage was not in fact for investors, but for the Member firms. I assured them that the Board of Directors of CIPF is examining the nature and content of the disclosure of CIPF coverage and appreciates the insight of investors such as the Appellants.

14. [REDACTED] was particularly gracious in her comments about CIPF, especially in light of the considerable hardship that has been suffered by her family. I have considerable sympathy for the Appellants; however, I conclude that the Appellants' submissions in this appeal are not persuasive and do not give rise to a successful claim for compensation from CIPF.

Disposition

15. The appeals are dismissed. The decisions of CIPF Staff are upheld.

Dated at Toronto, this 21st day of December, 2015.

Brigitte Geisler