

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

RE: [REDACTED] and [REDACTED]

Heard: December 11, 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

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 11, 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 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' investments in various First Leaside Group entities for a net investment of \$666,092.91, after allowing for a receipt of \$51,521.09 from the insolvency trustee.

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 letter dated January 30, 2014, the Appellants were advised that CIPF Staff were unable to recommend payment of their claims. The relevant parts of the letter reads 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. 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 investment and not a loss resulting from the insolvency of FLSI or the conversion of your property. 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.

Analysis

7. ██████████ advised that the funds invested in the First Leaside Group were retirement funds for himself and his wife. He had a bad experience with the 2008 financial crisis and had hoped for better results with First Leaside. He was disappointed in finding out that CIPF coverage was not what he had expected.

8. Counsel for CIPF Staff explained that CIPF's mandate and its coverage 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".

9. Counsel for CIPF Staff also noted that there was no relevance placed upon the reasons for the insolvency of FLSI, which may have been the result of bad business practices or even fraud. CIPF concerns itself only with ensuring that the property of customers is returned.

10. While the OSC and IIROC have found improper conduct on the part of the principals of FLSI, Messrs. Phillips and Wilson, such misconduct is within the purview of the regulatory authorities such as OSC and IIROC. Although the CIPF logo appears on FLSI documentation, as required by IIROC rules, it does not follow that CIPF represents or has a relationship with member firms in the same way as a regulator. CIPF is not a regulatory body; it has no powers to investigate or to discipline member firms. That authority lies within IIROC or the OSC.

11. The Appellants asked how they could recover their investments and how to protect themselves in the future. Counsel for CIPF Staff advised the Appellants that there was an action being brought by the insolvency trustee against Mr. Phillips and his wife, seeking to recover assets for the investors. He also noted that a class action has been brought by investors against the OSC. He further noted that some of the Appellants' investments were in entities that had not become insolvent and consequently, there may be some recovery.

12. The Appellants' written submissions raised arguments similar to those advanced at the October 27, 2014 hearing. This included interpretation of the phrase "including property unlawfully converted" in the Coverage Policy, with particular application to investments made after the OSC began investigating the First Leaside Group in 2009. The Appellants argued that they intended the funds they invested be applied to the proprietary First Leaside products for the primary purpose of funding the acquisition and/or development of various real estate projects; instead, these funds were unlawfully converted by FLSI for its own use.

13. These written arguments suggest that the Appellants' claims are really of fraud, material non-disclosure and/or misrepresentation which does not fall within the meaning of the phrase "including property unlawfully converted" as was discussed fully in the October 27, 2014 decision. Such an interpretation would in effect create a new head of coverage.

14. The October 27, 2014 decision deals extensively with the Appellants' arguments and the reasoning in the October 27, 2014 decision is adopted by this Appeal Committee. While I have considerable sympathy for the Appellants, 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 appeal is dismissed. The decision of CIPF Staff is upheld.

Dated at Toronto, this 22nd day of December, 2015.

Brigitte Geisler