

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

**RE: [REDACTED] AND [REDACTED]**

**WRITTEN APPEAL CONSIDERED BY:**

ANNE W. LA FOREST

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 (“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 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.<sup>1</sup>

2. FLSI was declared to be insolvent on February 24, 2012. The Appellants sought recovery from CIPF on the basis that FLSI was a Member of CIPF and as such the Appellants were entitled

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

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. 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*

4. The Appellant, [REDACTED], claims the amount of \$16,796.00 with respect to her purchases of two First Leaside Group products purchased on April 13, 2010 and September 9, 2011. All of these purchases were made after the date that OSC began investigating FLSI. The Appellant, [REDACTED], claims the amount of \$784,788.43 with respect to his purchases of various First Leaside Group products purchased between October 21, 2005 and October 3, 2011. The claim also includes stock dividends and stock exchanges. More than half relates to investments purchased by the Appellant [REDACTED] before the OSC began investigating FLSI in the fall of 2009.

5. Units representing the purchases made by the Appellant [REDACTED] were transferred to an account in her name at Fidelity Clearing Canada ULC ("Fidelity") in December 2012. Certificates representing the Appellant [REDACTED]'s purchases were either delivered to his possession or the units were transferred to an account in his name at Fidelity in December 2012. The materials filed before me establish and confirm these matters.

(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 December 29, 2014, the Appellants were advised that CIPF Staff were unable to recommend payment of their claims. The relevant parts of the letter to the Appellant [REDACTED] 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. 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 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.

In addition, with respect to the securities that you purchased, 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 Deal Member subsequent to February 24, 2012. Therefore, the loss is not one that is eligible for CIPF coverage, as indicated above.

The letter to the Appellant [REDACTED] was substantially the same but also included the following paragraph:

In addition, at the date of insolvency, the securities [which were held off book] were not held by, or in the control of, FLSI. Therefore the loss is not one that is eligible for CIPF coverage, as indicated above.

**Analysis**

7. In their original claims submissions, the Appellants relied upon the arguments prepared by representative counsel arguing that their loss was as a result of the insolvency of FLSI and unlawful conversion. These arguments were fully raised at the October 27, 2014 hearing and were addressed in the October 27, 2014 decision.

8. For purposes of this written appeal, the Appellants made further submissions dated January 25, 2016. Their arguments fall under three headings. First, they argue that their losses arose solely as a result of insolvency. In this regard, they point out, as other investors have done, that an accounting insolvency occurred as early as 2008. They support this statement by reference to the Grant Thornton Report and its assessment of the First Leaside Group. Second, they argue that FLSI failed to return or account for their investments as a result of this accounting insolvency including unlawful conversion. Third, the Appellants argue that their losses were due to the fact that CIPF allowed itself to be recklessly marketed by FLSI and that the Coverage Policy has evolved without reference to how customers of members such as the Appellants rely on CIPF and IIROC coverage when choosing a private investment firm.

9. Finally, it is worth noting that the Appellants have focused on the investments they made during the period after the Grant Thornton Report was released in August of 2011 and cite the OSC decision in which a panel found that Messrs. Wilson and Phillips had acted contrary to the public interest by selling securities of the First Leaside Group during the period between August 22, 2011 and October 28, 2011 by not disclosing the Grant Thornton Report and instead representing that the state of the First Leaside Group was of a certain character, when in reality it was not.

10. While framed in different words from arguments that have been presented to the Appeal Committee in the past, the arguments are in effect identical to submissions the Appeal Committee have answered in previous decisions. The role of the Appeal Committee is to review the Coverage Policy that was in effect at the time of the insolvency of FLSI and assess whether the Appellants are entitled to coverage for their losses. This requires the establishment of a number of matters, some of which are not in dispute. For example, FLSI must have, at the time of the insolvency been a member of IIROC and, the Appellants must have been clients of FLSI. Both of these matters are established. However, the loss must also have been caused by the insolvency of FLSI and must relate to a failure to return the Appellants property. The difficulty for the Appellants is that there is a distinction to be drawn between the insolvency of issuers within the First Leaside Group and FLSI itself. More importantly, there must be a failure to return property. Through the claims

confirmation material and the evidence before me, it is clear that all of the investments made by the Appellants are accounted for either through certificates that were delivered out or in account statements in relation to the units now held by Fidelity.

11. There is no doubt that the OSC panel determined, as the Appellants point out, that Messrs. Wilson and Phillips failed to disclose the Grant Thornton Report to investors and that they represented that the First Leaside Group was of a certain character. The Appellants in their own submissions state that there is no doubt that they would not have invested in September of 2011 had they been aware of the Grant Thornton Report. If they had been aware of the Report they would have withdrawn their funds from FLSI. Even accepting for the purposes of this decision that this is true (since this is not an adversarial process and there is no means available to the Appeal Committee to assess the matter) the fact remains that the Appellants were induced to purchase their investments and did not withdraw them because of misrepresentations made to them by the principals of FLSI. The question for the Appeal Committee is whether the Coverage Policy in effect on September 30, 2010 covers that particular wrongdoing. As the Appeal Committee stated in the October 27, 2014 decision, it does not and the Appeal Committee does not have the jurisdiction to add a new head of coverage to the policy.

12. Finally, the Appellants have raised concerns about the use of the CIPF logo and the public's understanding of its coverage. 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 as a regulator. CIPF is not a regulator and has no power to investigate or discipline members. That authority rests with the OSC or IIROC. Rather, CIPF is a fund providing coverage in accordance with the relevant coverage policy in effect at the time of insolvency of an IIROC member. It is of concern to the CIPF Board of Directors that its coverage has been misrepresented and that members of the public may misunderstand it. As has been noted in other decisions of the Appeal Committee, a review of CIPF's communication with investors through its website and brochures is being undertaken.

**Disposition**

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

Dated at Toronto, this 4<sup>th</sup> day of February, 2016

Anne Warner La Forest