

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

RE: [REDACTED] and [REDACTED]

Heard: November 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 and representing

[REDACTED]

DECISION AND REASONS

Introduction and Overview

1. [REDACTED] and [REDACTED] (“[REDACTED]”) (collectively, 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 November 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 Appellant, [REDACTED], representing himself and [REDACTED] (a sole proprietorship under the control of [REDACTED]), was in attendance by teleconference.

Chronology of Events Relevant to the Appellants’ Claim

(i) The Appellants’ Investments and Claim

4. The claim arises from the Appellants’ purchase of various First Leaside Group products, for a total net claim for [REDACTED] of \$445,445.30 and for [REDACTED], a total net claim of \$95,330.21. These amounts include a reduction representing distributions from the insolvency trustee.

5. Certificates representing the Appellants’ investments were either delivered into the possession of the Appellants or transferred to accounts in the name of [REDACTED] at Fidelity Clearing Canada ULC.

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 letters dated April 10, 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.....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.

██████████

Regarding your claim for unlawful conversion, it does not appear to us that any property held by FLSI for ██████████ was converted or otherwise misappropriated..... The securities that were 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, the 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. ██████████ advised that he had invested with FLSI in order to attain a specific rate of return. He was assured that the First Leaside entities were viable operations and that if their operations led to cash deficiencies, these would be satisfied by the company, rather than there being calls on investors. He took comfort from the fact that CIPF coverage was prominently displayed.

8. ██████████ advised that the two investments made by ██████████ were meant to be loans or promissory notes to FLSI, that he had not intended that they be investment in other entities which

were offered by Offering Memorandum. It is actually from these entities that he received the largest payment from the insolvency trustee. It must be noted that if [REDACTED] had intended that these investments be loans to FLSI, a claim for compensation would not qualify under the Coverage Policy. The first criterion for coverage is that the claimant be a customer of the member firm. Making a loan to the member would not give the lender the status of customer and accordingly, no coverage would be applicable.

9. [REDACTED] queried the application of CIPF coverage, in particular, with regard to coverage for fraud. Counsel for CIPF Staff explained the nature and purpose of CIPF's mandate and coverage which is custodial in nature; in other words, to ensure that the clients of an insolvent member have received their property. This custodial coverage is set out in CIPF's mandate, which is approved by the OSC and other provincial securities regulators. The mandate is restricted to this coverage, and does not extend to coverage for fraud, material non-disclosure and/or misrepresentation. The nature and extent of the coverage is discussed in full in the October 27, 2014 decision.

10. [REDACTED] expressed his view that the literature which describes CIPF coverage is inadequate in failing to clearly set out the limitations of its coverage. This opinion has been expressed by other claimants and is being taken seriously by the CIPF Board of Directors.

11. In the Appellants' written submissions, [REDACTED] 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.

12. 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.

13. 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

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

Dated at Toronto, this 16th day of November, 2015.

Brigitte Geisler