

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

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

Heard: January 14, 2016

PANEL:

PATRICK J. LESAGE) Appeal Committee Member

APPEARANCES:

[REDACTED]) In person
[REDACTED]) In person

Nicolas Businger) Counsel for Canadian Investor Protection
) Fund Staff

DECISION AND REASONS

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” of “FLG”). 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”) 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 CIPF was established to provide certain limited coverage in the event of losses arising from dealer insolvency. 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, released on December 17, 2014.¹

BACKGROUND

2. For the three years preceding July 2011, [REDACTED] was an employee of First Leaside Wealth Management Fund (FLWM). In March 2011, he invested \$11,000 in that Fund. During 2009 and 2010, [REDACTED] invested almost \$43,000 in First Leaside Series II preferred shares.

3. The Appellants submitted that their losses flowed directly from the Cease Trade Order and/or the FLSI insolvency. Their position is that the Cease Trade Order led to FLSI's insolvency, which in turn led to the insolvencies of the FLG entities in which they had invested. The insolvencies occurred, they submit, because those entities were then unable to access operating funds. Thus, they submit, they suffered losses for which they are entitled to be compensated by CIPF. They also submit that they were misled into believing and in fact did believe that the CIPF coverage extended to losses such as they suffered. [REDACTED] also submits that he knew from his experience working for three years at FLWM, that all the FLG entities including FLSI were really only one company that was run by David Phillips.

ANALYSIS

4. Before addressing the Appellants' arguments, it is important to understand the nature of CIPF coverage. CIPF provides coverage arising from the custodial relationship between the investor client and the IIROC regulated dealer, FLSI, including for unlawful conversion. It does not provide broad coverage for fraud, misfeasance, malfeasance or diminution of the value of the investments.

5. FLSI and the FLG entities, as the Appellants submit, appear to have been operated as one single operation. However FLSI is at law a separate and distinct entity from the myriad of other FLG entities and must be treated as such.

6. The diminished value of the Appellants' investments occurred because the entities in which they had invested lost their value. When the Cease Trade Order was put in place, the companies could no longer operate what had become, in effect, a Ponzi scheme. The diminished value came

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

about, not because of the insolvency of FLSI, but rather because the FLG entities were no longer able to continue the Ponzi scheme. The Appellants' losses simply result from or reflect the value of the entities in which they invested.

7. Any remaining cash in the Appellants' accounts at FLSI, and the certificates or other indicia of their investments, were returned to them. Accordingly, the Appellants claim against the "custodial" coverage provided by CIPF cannot succeed.

8. While I have sympathy for the Appellants' losses, in essence this appeal does not meet the requirement of establishing a valid legal claim for coverage under the terms of the CIPF policy.

RESULT

9. The appeal must therefore be dismissed. The decision of the CIPF Staff is upheld.

Dated at Toronto, this 29th day of February, 2016



Patrick J. LeSage