

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

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

**Heard: January 25, 2016, by teleconference**

**HEARD BEFORE:**

ANNE W. LA FOREST

Appeal Committee Member

**APPEARANCES:**

Graeme Hamilton

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)

Counsel for Canadian Investor  
Protection Fund Staff

[REDACTED]

)

On his own behalf  
and on behalf of [REDACTED]  
and [REDACTED]

**DECISION AND REASONS**

**Introduction and Overview**

1. [REDACTED], [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 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 January 25, 2016, 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 took place by way of teleconference. The Appellant, [REDACTED], was in attendance by teleconference and made submissions on his own behalf as well as on behalf of [REDACTED] and [REDACTED].

### **Chronology of Events Relevant to the Appellants’ Claim**

#### *(i) The Appellants’ Investments and Claim*

4. The Appellant, [REDACTED], claims the amount of \$432,168.26 with respect to its purchases of various First Leaside Group products purchased between June 2, 2009 and September 23, 2010. The Appellant, [REDACTED], claims the amount of \$120,994.94 with

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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”.

respect to his purchases of various First Leaside Group products purchased between May 4, 2009 and July 29, 2010. The Appellant, [REDACTED], claims the amount of \$101,979.80<sup>2</sup> with respect to her purchases of various First Leaside Group products purchased between December 24, 2009 and July 29, 2010. Many of these products were purchased by the Appellants during the period after the OSC began investigating FLSI in the fall of 2009.

5. Certificates representing the corporate Appellant [REDACTED]'s purchases were delivered to the corporation's possession. 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 Clearing Canada ULC ("Fidelity") in December 2012. Certificates representing the Appellant [REDACTED]'s purchases were either delivered to her possession or the units were transferred to an account in her name at Fidelity in December 2012. The materials filed before me establish this and statements made by the Appellant, [REDACTED], during the teleconference hearing 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 August 1, 2014, the Appellants were advised that CIPF Staff were unable to recommend payment of their claims. The relevant parts of the letter to the corporate Appellant [REDACTED] read as follows:

Regarding the 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 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 the investments and not a loss resulting from the insolvency of FLSI or the conversion of the property. Losses

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<sup>2</sup> [REDACTED] claims a total of \$101,980.10 on her claim form. However, the total amount of the investments claimed is \$101,979.80, resulting in a difference of \$0.30.

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, 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.

The letters to the other two Appellants were substantially the same but also included the following paragraph:

With respect to the securities that you purchased and which [were held on book] 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 Dealer Member subsequent to February 24, 2012.

## **Analysis**

7. The Appellants made a number of submissions in writing that were provided in advance of the teleconference. These included arguments to the effect that:

- a) the CIPF brochure referred to the insolvency of IIROC members and did not explicitly exclude fraud;
- b) what had transpired in this case was in effect a Ponzi scheme;
- c) while the CIPF utilized the date of February 24, 2012 as the date of the bankruptcy, the bankruptcy had occurred at a much earlier date;
- d) the regulatory agencies including CIPF had failed to take action;
- e) the Appellants in making their investments were told that their investments were in real estate whereas in fact the funds were utilized to pay distributions to other investors and to support Messrs. Phillips and Wilson; and
- f) the language in the Coverage Policy was ambiguous and that in interpreting the Coverage Policy, the Appeal Committee should adopt a broad interpretation of unlawful conversion or exercise the discretion provided for in the Coverage Policy.

These arguments are identical to those that were made in the October 27, 2014 hearing and in subsequent hearings before the Appeal Committee and I rely on the reasoning in the October 27, 2014 decision and in the Appeal Committee's subsequent decisions to reject these arguments.

8. In their written submissions and at the hearing, the Appellants focused on two arguments, one relating to the loss of value of the investments and the second relating to unlawful conversion. The Appellants also raised questions of bias in their written submissions and counsel for CIPF Staff responded to these arguments both in writing and at the hearing.

9. In terms of loss of value, the Appellants argue that their loss was not caused by a change in the market value of the investments but rather was a loss caused by insolvency that was the result of the actions of those who, through fraudulent actions, failed to properly manage the Appellants' investments and who were engaged in a Ponzi scheme. As to unlawful conversion, the Appellants submit that the money they invested was not used as directed by the Appellants but rather was used to refinance mortgages, to pay distributions to other investors who had invested earlier, or to support Messrs. Wilson and Phillips. The Appellants' expectation was that the CIPF would cover their loss in these circumstances particularly since, in their submission, the CIPF website refers to coverage in relation to fraudulent schemes.

10. The difficulty for the Appellants is that the loss they have suffered must be caused by the insolvency of FLSI and must result from a failure to return their property to them including "property unlawfully converted" (this phrase comes directly from the Coverage Policy dated September 30, 2010). As to causation, there is a distinction between FLSI and the issuers, being the First Leaside Group, in which the Appellants' investments were made. Here, the loss of value is in the issuers in which the Appellants invested. The documents associated with these investments, outlined the risks associated with, and the allowable business, of the investments. As to unlawful conversion, the relevant property is the securities representing the Appellants' investments. These securities are with the Appellants either in certificate form or accounted for in statements showing that the units are currently held by Fidelity. Where property is not returned to investors whether as a result of a fraudulent scheme or otherwise, the Coverage Policy applies. But that is not this case.

Here, all the property belonging to the Appellants - the securities in which they invested - have been accounted for. Like other clients of FLSI, the Appellants were likely induced to purchase these investments through misconduct, fraud, material non-disclosure and/or misrepresentation by FLSI. But this fact does not assist the Appellants as the Coverage Policy only covers the situation where there is a failure to return property.

11. Finally, the Appellants alleged in their written submissions that the outcome of this appeal has been pre-determined and as such the Appeal Committee is biased in its response to their appeal. Bias is a state of mind that is in some way predisposed to a particular result or that is closed with regard to a particular issue. As I indicated during the course of the teleconference, each case is reviewed on its own facts and members of the Appeal Committee have no involvement in or discussions with CIPF Staff in relation to these appeals. My role is limited to reviewing the facts of each case and the arguments made by the Appellants against the wording of the Coverage Policy of September 30, 2010 that was in effect at the time of the insolvency of FLSI. Members of the Appeal Committee have no motivation to find claims ineligible for compensation. Indeed, I have considerable sympathy for the Appellants, and appreciate the fact that they have suffered significant losses.

### **Disposition**

12. 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