

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

RE: [REDACTED], [REDACTED]

and [REDACTED]

Heard: November 26, 2015

HEARD BEFORE:

BRIGITTE GEISLER

Appeal Committee Member

APPEARANCES:

Nicolas Businger

) Counsel for Canadian Investor
) Protection Fund Staff

[REDACTED]

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

DECISION AND REASONS

Introduction and Overview

1. [REDACTED], [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 26, 2015, an Appeal Committee Member of CIPF’s Board heard an appeal to determine whether to depart from the decision of CIPF Staff. The hearing was held at Neeson Arbitration Chambers in Toronto, Ontario. [REDACTED] was in attendance representing himself, [REDACTED] and [REDACTED], the corporate Appellant.

Chronology of Events Relevant to the Appellants’ Claim

(i) The Appellants’ Investments and Claim

4. The claim arises from the Appellants’ purchases of various First Leaside Group products for a total net claim by [REDACTED] of \$51,083.97; by [REDACTED] of \$30,804.98;² and by [REDACTED] of \$325,000.00. The claims by [REDACTED] and [REDACTED] include claims for stock dividends.

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

² [REDACTED] claim was originally for the amount of \$39,785.12, but was adjusted to \$30,804.98 upon review by CIPF Staff and confirmed by [REDACTED].

5. The securities representing [REDACTED] and [REDACTED] purchases were transferred to accounts in their names at Fidelity Clearing Canada ULC, and in the case of the corporate Appellant, [REDACTED], were delivered into the possession of [REDACTED].

(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 May 26, 2014 and October 20, 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:

CIPF does not cover customers' losses that result from other causes such as dealer misconduct, changing market values of securities, unsuitable investments or the default of an issuer of securities.

[REDACTED], [REDACTED]: 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 an account in your name at another IIROC Dealer Member subsequent to February 24, 2012. Therefore, the loss is not one that is eligible for CIPF coverage....

[REDACTED]: At the date of insolvency, the securities.....were not held by, or in the control of, FLSI. As an indication of this, you provided a copy to CIPF of the securities that Complete Freight Services Inc. held in certificate form. Since the securities were not held by, or in the control of, the insolvent Member at the date of insolvency, the loss is not one that is eligible for CIPF coverage.

Analysis

7. [REDACTED] described his meeting with Mr. Wilson of FLSI wherein he advised Mr. Wilson that the money he would invest were for his children's university educations and that he couldn't afford to lose it; he advised that he has taken a loan on his house in order to fund the university expenses.

8. There was some discussion at the hearing with respect to the investment by [REDACTED] of \$225,000 on June 19, 2009. [REDACTED] indicated that he had wanted to invest in T-bills and that this wasn't done, but he also agreed that he had not made any complaint to FLSI about this transaction. The records indicate that the funds were invested in First Leaside Fund (Series A)³ on his written instructions. He acknowledged that he had received the certificate and that he had received a monthly statement and confirmation which both showed this transaction.

9. Prior to the hearing, [REDACTED] filed the submissions of another CIPF Appellant ([REDACTED]) for consideration ("[REDACTED] submissions"). At the hearing, he primarily addressed the responding submissions of CIPF Staff counsel. He also filed the Brief of the Appellant which had been presented at the first Appeal Committee hearing.

10. [REDACTED] addressed the comments in the [REDACTED] submissions with reference to the securities, which, when delivered to an investor, would be considered off-book and not within the control of FLSI and accordingly no coverage would be applicable. The [REDACTED] submissions attempt to argue that the securities remained under the control of Mr. Phillips at FLSI as he was the controlling mind of FLSI (and also many, if not all, of the First Leaside Group entities). While it is certainly agreed that this control was exercised by Mr. Phillips, with respect, that is not the issue. Rather, the matter of control relates to the control of the stock certificate, not the control of the company.

11. The securities were held in the possession of the Appellants; those securities could not be transferred or disposed of without the Appellants' authorization. As such, they were the ones who had control over the certificates. Since they were not on the books and records of FLSI, no coverage would be available. However, it must be noted that the Appellants' ownership, like that of others who have received delivery of their stock certificates, is being acknowledged and their claims are being treated as valid claims by the insolvency trustee.

³ See Appeal Record, Volume 1, Tab C-1; Tab C-2; and page 178 of Tab C-7.

12. It is most unfortunate that the property has lost almost all of its value; 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”.

13. The [REDACTED] 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 argument is that funds which were intended to be invested in real estate projects were, through intercompany transfers, unlawfully converted by FLSI for its own use.

14. The [REDACTED] submissions further argue that the intercompany loans, which were made by many of the First Leaside Group entities, also constitute wrongful conversion of investors’ monies. It must be noted that the Offering Memorandum and the Declaration of Trust for the Appellants’ investments allows for loans to any First Leaside Group Member (Special Notes LP) and Wimberly Group Member (First Leaside Fund).⁴

15. 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.

16. Counsel for CIPF Staff described the role of CIPF vis-à-vis that of IIROC and the OSC; the latter bodies having regulatory and disciplinary authority over members and securities dealers. It is IIROC which primarily regulated FLSI and had the authority to bring disciplinary actions against its members and employees, as they did in the case of Messrs. Wilson and Phillips. The OSC has primarily authority over the principals and issuers of securities, such as the various entities in the

⁴ See Appeal Record Volume 2, pages 2 and 7.

First Leaside Group. In this regard, they implemented cease trade orders against entities in the First Leaside Group, and also took disciplinary action against Messrs. Wilson and Phillips.

17. In contrast, CIPF is not a regulator, but rather a not for profit entity which fulfills a specific role in the securities industry in the event of the insolvency of one of its members.

18. The First Leaside Group involved a very large number of separate entities, many of them having “First Leaside” as part of their name. This naming protocol, along with the fact that many of these entities entered into insolvency at about the same time as FLSI, has created confusion for FLSI customers. While investors have suffered losses because of insolvency, it has been the insolvency of the First Leaside Group entities that generated the loss, not the insolvency of FLSI. Only FLSI is a member of CIPF and only claims resulting from FLSI’s insolvency and not its related entities are eligible for compensation.

19. The kind of claim that is eligible for compensation from CIPF is one that arises from circumstances where customer funds have been diverted from their intended objective. 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.

20. I have considerable sympathy for the Appellants, however, 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

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

Dated at Toronto, this 10th day of December, 2015.

Brigitte Geisler