

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

RE: [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 her own behalf and on behalf
) of [REDACTED]

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 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 both Appellants.

Chronology of Events Relevant to the Appellants' Claim

(i) The Appellants' Investments and Claim

4. The claim arises from the Appellants' investments in various First Leaside Group products for a total net claim of by [REDACTED] of \$324,184 and [REDACTED] of \$83,390. [REDACTED] advised that additional investments had been made with First Leaside; however, these preceded 2009 when investigations by the OSC into the First Leaside Group began. The Appellants had decided not to make claims with respect to those investments. The Appellants have received distributions from the insolvency with respect to their investments in the First Leaside Group.

5. The securities representing the Appellants' purchases were transferred to accounts in the names of the Appellants at Fidelity Clearing Canada ULC or delivered to their possession.

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 separate letters dated March 5, 2015, 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. 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.

Analysis

7. [REDACTED] described how, following an initial solicitation from FLSI, the Appellants performed due diligence with respect to the First Leaside Group. They attended an annual meeting and spoke with other investors who all spoke highly of First Leaside. They noted the IIROC and CIPF logos on the First Leaside marketing materials; they considered these memberships a key factor in making their investments. They queried the process for redeeming their investments and were told that it would require a notice period of 30 days, contrary to the information in the Offering Memorandum. In 2010, they did request a redemption and received their funds, which gave them confidence to make further investments.

8. [REDACTED] explained that following the insolvencies of the First Leaside Group, she had done more research with respect to the nature of CIPF coverage and now understood its limitations with respect to off-book investments and market value. She also understands the limitations of

information regarding proprietary products and how their values rely upon information supplied by the issuer.

9. [REDACTED] also queried the regulatory surveillance of the First Leaside Group. It was her view that the IIROC disciplinary decision against Messrs. Phillips and Wilson showed misconduct even prior to 2009. She was disappointed that the regulators had not taken steps earlier. She was particularly distressed about the disclosure in the various Offering Memoranda for First Leaside Group products, stating that they were largely incomprehensible. She couldn't understand how the regulators would allow the marketing of these products. At the end of the day, she observed, there was no regulatory protection and the investment in the First Leaside Group was a matter of trust, which had been betrayed by the First Leaside principals.

10. 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 in the same way as a regulator. CIPF is not a regulatory body; it has no powers to investigate or to discipline member firms. That authority lies within IIROC or the OSC.

11. It is of great concern and disappointment to the CIPF Board of Directors that its coverage has been misrepresented to investors by FLSI. Efforts have been, and continue to be undertaken to promote a proper understanding of CIPF coverage within the investment industry. A review of CIPF's communication with investors through its website and brochures is also being undertaken.

12. [REDACTED] also commented on the fees paid by dealers to CIPF. She felt that, ultimately, these fees were passed onto investors. She didn't believe that any value was being received by investors for those fees as CIPF's coverage policy is so narrow that she wondered if any investors ever benefited from it.

13. Counsel for CIPF Staff expanded upon the origins of the CIPF and the restrictive nature of CIPF coverage. 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. It is most unfortunate that the value of the property is uncertain; 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”.

14. The October 27, 2014 decision deals extensively with the Appellants’ written arguments and the reasoning in the October 27, 2014 decision is adopted by this Appeal Committee. As in the October 27, 2014 decision, while expressing considerable sympathy for the position of 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

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

Dated at Toronto, this 9th day of December, 2015.

Brigitte Geisler