

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

RE: [REDACTED] and [REDACTED]

Heard: May 15, 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 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 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 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 heard on October 27, 2014 with its reasons released on December 17, 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 May 15, 2015, 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 at Neeson Arbitration Chambers in Toronto, Ontario. The Appellant, [REDACTED] was in attendance by teleconference and made submissions on behalf of both Appellants.²

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. At the hearing, the Appellant, [REDACTED] amended the claim to restrict it to the purchase on June 10, 2011, of 100,000 units of FLWM Holdings Limited Partnership for a cost of \$100,000.

5. All of the certificates for the securities purchased by the Appellants were delivered to the Appellants, pursuant to the documentation provided.

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

² Consequently, although this decision is in relation to the appeals brought by both Appellants, [REDACTED] is referred to below as the "Appellant".

(ii) The Appellants' Application for Compensation

6. The Appellants applied to CIPF on September 30, 2013 for compensation for their losses in investments made through FLSI. By letter dated November 3, 2014, the Appellants were advised that CIPF Staff were unable to recommend payment of their claims. The relevant parts of the letter 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.

In addition, at the date of insolvency, the securities described in the table below³ 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.

Analysis

7. The Appellant noted that inducements had been made by the principals of FLSI to encourage investment in First Leaside Group products. These inducements included assurances that there was CIPF coverage for their investments, which gave them more confidence in investing with FLSI. The Appellant stated that he had relied upon the CIPF brochure and statements that insolvency was rare in the securities industry. The Appellant also commented that he was reassured

³ The Appellant amended the claim to include only the single security noted in paragraph 4.

in that FLSI's board of directors included at least one prominent Canadian businessman. The Appeal Committee took note of the comments.

8. The Appellant submitted that the FLSI insolvency actually occurred in 2009 on the basis that this was when the events relating to the eventual insolvency originated and because this is when the investigation into the First Leaside Group began. The Appellant submitted that it was improper for FLSI to continue to show the value of the investment at the original cost price when it knew, or should have known, that the value was being eroded. In effect, by doing so, this constituted an "unlawful conversion" of the funds which the Appellants invested.

9. These arguments are similar to those addressed in the October 27, 2014 decision. This included interpretation of the phrase "including property unlawfully converted" in the Coverage Policy. The Appellant argued that the funds they invested were to have been invested in proprietary First Leaside products on the understanding that such funds would be invested in those products for the primary purpose of funding the acquisition and/or development of various real estate products. The Appellant submitted that the FLWM Holdings Limited Partnership investment was made in 2011, during the period in which the Ontario Securities Commission ("OSC") was investigating the First Leaside Group. The conclusion, the Appellant submitted, was that the funds invested were unlawfully converted by FLSI for their own use.

10. The adoption of these arguments suggests 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.

11. CIPF Staff addressed a comment by the Appellant that CIPF had been involved in the investigation of FLSI by the OSC. He advised that CIPF is not a regulator, nor does it have investigatory powers for possible securities violations; these are the purview of the OSC and IIROC. He noted the similarity of names of the entities and proprietary products involved in the First Leaside Group, which may have led to some confusion about which entity was a member of

CIPF, and which body, regulatory or otherwise, might have jurisdiction or interface with the various First Leaside Group entities.

12. Counsel for CIPF Staff noted that IIROC's regulatory function relates to the business and operations of FLSI. It does not have jurisdiction over the various proprietary products that were marketed by FLSI to various investors. Those products, or issuers, are under the jurisdiction of the OSC, which, having concerns over those operations, began an investigation into the First Leaside Group in the fall of 2009. The jurisdiction of IIROC, and by extension, CIPF, within the limits of its mandate, is confined to FLSI only.

13. 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. 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.

14. 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. As in the October 27, 2014 decision, 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

15. The appeal is dismissed. The decision of CIPF Staff is upheld.

Dated at Toronto, this 25th day of May, 2015

Brigitte Geisler

Brigitte Geisler