SIPA
SMALL INVESTOR PROTECTION ASSOCIATION

A Voice for the Small Investor

February 14, 2010

Mr. Robert Day rday@osc.gov.on.ca

Manager, Business Planning
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, Ontario M5H 3S8

Re: COMMENTS REGARDING STATEMENT OF PRIORITIES FOR FISCAL YEAR ENDING MARCH 31, 2011

Dear Mr. Day;

The Small Investor Protection Association (SIPA) was founded in 1998 because we felt investor protection was lacking. Although regulators claimed investor protection was important, a great number of Canadians were losing their savings due to systemic investment industry practices of fraud and wrongdoing. It seemed that the "written rules" were simply treated as guidelines and industry continued to follow established practices that to consumer/investors seemed contrary to the rules.

A year later SIPA was incorporated as a national non-profit organization with a mission:

1. to aid public awareness of how the investment industry operates;
2. to provide guidance to members who have a complaint about investments with a bank, broker, financial advisor, or other seller of financial products;
3. and to pursue improvement of industry regulation and enforcement.

Since the days when Jack Geller was Acting Chair of the OSC, and during the time David Brown was Chair, SIPA liaised with the OSC and met regularly with the Chair to act as a voice for consumer/investors. We realized that the Chair was buffered from the consumer/investor issues by an industry that has its own cultures that seemingly overrides the norms of morality common amongst the majority of Canadians. So in 2004 SIPA issued a report "The Small Investors' Perspective of Investor Protection in Canada to help raise awareness of the issues impacting Canadians' savings and investments.

In our early years SIPA organized public meetings in our community and invited speakers from the OSC, the SROs, OBSI as well as other stakeholder to make presentation and respond to questions. In later years SIPA began liaising with other groups to raise awareness. A few years ago SIPA joined with several other organizations in the Common Front for Retirement Security, which now comprises some 21 organizations representing two million Canadians.

In 2005, SIPA participated with the OSC, the Self Regulatory Organizations (SROs), and the Ombudsman for Banking Services and Investments (OBSI) to provide a public forum where consumer/investors could dialogue directly with the regulators and OBSI. The OSC Town Hall was an astounding success with approximately 500 people in attendance, and sustained interest that exceeded the allotted time. The event was available on the internet to enable many others to participate. A transcription of the audio cast is available of the SIPA website.

Sadly, this promising OSC initiative faltered and was abandoned with no subsequent events of that nature. The OSC Investor Advisory Committee established after the Town Hall Event was also subsequently quietly disbanded after two years without any report on its workings.

These events raise the question whether the objective was simply to bolster a perception, or whether there is intent to improve the regulatory regime's approach to investor protection.

Nevertheless, we offer our comments on the OSC Statement of Priorities for your consideration.

SIPA's top priority with regard to investor protection is restitution. The OSC should have its mandate revised, if necessary, so they can provide restitution as other provinces have already done. It should be able to not only order, but also pay the restitution as does the Autorité des marchés financiers in Québec.

Granted there is good and bad in all industries. Corporate greed is certainly not uncommon. However, an industry that deals with the very lifeblood of our society should be held to a higher moral standard not dissimilar to our healthcare facilitators. Canadians' life savings are often essential for their well-being and survival; those in whom consumer/investors place their trust should be deemed to have a fiduciary responsibility. Canadians see the dispute resolution mechanisms as ineffectual an question why regulators allow this to happen. Yet we see

"The fact that there are so many Financial Advisers in Canada that are dishonest and are allowed to handle Canadians' Investments knowing that the system will not protect the investors is inexcusable.

The whole complaint process that the financial institutions present is nothing more than a sham as far as I am concerned"

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a corporate culture that seems to have more of a “rape and pillage” mentality, with a cavalier attitude towards consumer/investor savings and trust, rather than a “just and caring society” mentality.

From interviewing hundreds of consumer/investors and speaking with dozens of groups and thousands of people, we have by observation formed an opinion of the issues faced by investors. From time to time SIPA makes unsolicited submissions to represent consumer/investors but with limited resources the investors’ voice is often overwhelmed by industry’s seemingly unlimited resources.

We believe the financial market meltdown of the last couple of years has raised awareness to a whole new level as many of the frauds and scams that survived for many years in a rising market environment could not survive the onslaught of a falling market that was if not precipitated at least accentuated by these very frauds and widespread wrongdoing on which a rapacious industry fed their greed to achieve rewards that were beyond the norm.

The OSC claims that investor protection is part of their mandate. If the OSC is to continue to be responsible for investor protection, the mandate should make clear that this part of its mandate should not be compromised so that trade-offs are made. The fact the OSC delegates investor protection to SROs simply passes down a conflict of interest.

While the regulators should ensure investor protection is a fundamental right of Canadians, there must be an oversight body to ensure that consumer/investors are being adequately protected. The OSC acknowledges they understand the problem of innovative products created to circumvent regulations and being packaged and sold to unsuspecting investors with a lack of transparency and disclosure. The issue really is industry culture. As long as there is intent to create an illusion, consumer/investors will suffer loss of their savings at the hands of industry. The OSC mandate should make provision for new developments and not be limited by lack of prescriptive rules for new developments created to circumvent rules. There need to be room for some wise judgements by those who know right from wrong.

To provide proper investor protection there must be restitution. The current inability, or unwillingness, of regulators to order restitution must be changed. This has happened in Quebec and a couple of other provinces. It is one of the priorities in the Expert Panel recommendations. It may be that new legislation and a revised mandate is the most important issue with regard to the OSC. Fiddling with rules and regulations while consumer/investors continue to lose their life savings, and then simply admonishing the industry participants for breaching rules, providing the regulators deem there is sufficient evidence of rule breaching, does not help victims of financial abuse.

For many victims being told they can resort to civil litigation to resolve their dispute is akin to saying there is no hope for them to recover their loss. To direct them to industry processes does not provide justice for the victims as the system is adversarial and few victims can achieve more than a partial payment of what would seem a fair settlement, and even at that they must sign a confidentiality agreement (Gag Order) so the victim can not speak out and Canada remains unaware of the magnitude of this hidden problem.

Investor education alone will not resolve the issue of consumer/investors losing their savings due to industry fraud and wrongdoing. The issue is probably best illustrated by the Madoff scam in the United States and the Earl Jones scam in Canada. Both of these scams spanned a period of more than 20 years. What were the regulators doing?

It should be a requirement for anyone selling financial products to be registered and regulators should ensure that registrants are qualified.

While it may be that consumer/investors should realize they have some responsibility, and it may be an INVESTOR BEWARE society, we would like to think our aspirations are higher than that.

On May 31st, 2008, SIPA made an unsolicited submission to the Expert Panel on Securities Regulation entitled “Because They Can” to reflect the fact that the industry is not restricted from systemic practices that erode consumer/investor savings when regulators are fully knowledgeable of their actions. The report stated:

> “Recognizing the mandate of the Expert Panel is to recommend reform to securities regulation we are submitting our recommendations with regard to improving investor protection which we believe the current system is failing to provide. Lip service is paid to the need for investor protection but the regulators believe they are providing preventative investor protection rather than remedial investor protection. The result is investors’ savings are being stolen by industry fraud and wrongdoing at a rate exceeding $20 billion per year.”

The complete recommendations are included at the end of this submission.

From time to time we see what appear to be good intentions from regulators, like the OSC Town Hall Event and the Investor Advisory Committee referred to above. More recently the CSAs published an alphabetical list of persons that at first seemed to be a positive step forward.

A decade ago SIPA published an alphabetical list of persons disciplined or reported in the media for fraud and wrongdoing. Shortly afterwards the British Columbia Securities Commission also published an alphabetical list of disciplined persons. It is

essential for consumer/investors to have access to information when they are attempting to source help for their investment needs.

Unfortunately, other Canadian Securities Regulators were slow to respond. Only recently the CSA Secretariat published an alphabetical list of persons and the OSC has finally joined in although the OSC provides data going back only to 2005, while the BCSC provides data going back to 1987. That is 18 years more. If the OSC had investor protection as a priority they should consider extend the database back as far as possible.

A fundamental weakness of the CSA List is that it does not include persons disciplined by the SROs. We suspect that more persons who have taken advantage of consumer/investors would be disciplined by the SROs. Therefore it would seem essential that if this tool is to be of value to consumer/investors the CSA List should be comprehensive and include all registered representatives.

The lack of a national regulator means that even a comprehensive list form provincial regulators would not include federally regulated insurance companies and banks.

There seems little doubt that there is regulatory capture of our regulators. There have been many studies over the last decade and more. Although a national regulator for Canada seemed most appropriate, the industry was not a supporter for such a move, and so the call for a national regulator languished. It seemed that when the Wise Persons Committee was established there was very little left to study. They reviewed prior studies and concluded that it was time for Canada to have a national regulator in their report entitled “It’s Time.” It still hasn’t happened, although the Canadian Securities Transition Office is working towards that objective.

SIPA is quite aware of the impact of regulatory capture on Canadian consumer/investors. As a voluntary organization funding is a continuing issue. Several years ago SIPA made an application for funding to the OSC in response to being advised by a senior OSC executive that they had a mechanism in place so they could provide funding and sent an application form which he said he hoped would not be too onerous. A month later, with assistance from the OSC, the application was submitted. Although the application was presented and supported by two senior executives, it was turned down by the board.

The current approach of regulators “inviting comments” to guide them inevitably leads to an overwhelming submission by industry with paid researchers and services and resources enabling them to provide detailed credible submissions. Effectively it results in industry guiding the regulators.

This is one of the many reasons why SIPA recommend in 2004 that Government establish an Investor Protection Agency to represent consumer/investor interests. This is described in detail in the CARP/SIPA Mutual Fund Report issued in September 2004 and available on the SIPA website.

There are many issues that need to be addressed; but unless investor protection includes provision for restitution when preventative measures fail and fraud and wrongdoing result in investor loss, the other issues seem remarkably less important for consumer/investors.

Yours truly

Stan I. Buell
Founder & President

CC Hon. Dwight Duncan, Minister of Finance
Douglas Hyndman, Chair CSTO

8. Recommendations

Recognizing the mandate of the Expert Panel is to recommend reform to securities regulation we are submitting our recommendations with regard to improving investor protection which we believe the current system is failing to provide. Lip service is paid to the need for investor protection but the regulators believe they are providing preventative investor protection rather than remedial investor protection. The result is investors' savings are being stolen by industry fraud and wrongdoing at a rate exceeding $20 billion per year.

Although we fully support a national securities regulator we believe it should be a national financial services regulator similar to the Québec model. We also believe that it is unlikely to come to fruition in the near future. There is considerable effort towards harmonization and uniform securities laws as securities regulation remains a provincial jurisdiction. With the advance made in Québec with the formation of the Autorité des marchés financiers and the forward looking decisions of the Québec courts it will likely take years for the rest of Canada to reach the enlightened position of Québec with regard to investor protection and restitution of the victims of industry wrongdoing. Nevertheless we believe that Canada could make progress towards a national regulator by encouraging Uniform Securities Laws and harmonization amongst the provinces and territories and recognizing and reinforcing some of the good initiatives of the regulators and self regulatory organizations.

Two examples of such initiatives which we believe should be inherent in a national approach to regulation are:

1. The IDA's ComSet database. This database was initiated to record all complaints received by members of the IDA and settlements made with aggrieved investors. Recently the IDA has taken some disciplinary action against registered representatives reported by the firms. This is a system that should be adopted by a national regulator and expanded to apply to all firms selling investment products.
2. The BCSC initiated an alphabetical list of individuals and firms disciplined by the BCSC shortly after SIPA had introduced a "Hall of Shame" on our website that listed alphabetically registered representatives and firms that had been disciplined by the regulators or reported in the media. We believe the BCSC is the only CSA to provide such an alphabetical list. Other regulators offer to provide information on disciplines but it is not available as an alphabetical list, and search mechanisms are not always user friendly. As an example, if you do not have the exact spelling of the registered name a search will not produce results.

The Expert panel should carefully review the Autorité des marchés financiers and consider how the Québec model for regulation could be applied on a national basis.

We believe that investor protection must be paramount in any regulatory system. Ralph Goodale, former Minister of Finance, wrote to SIPA on May 31, 2004;

> "I share your view about the importance of investor protection. Indeed, one of the fundamental objectives of securities regulation is to protect investors from unfair practices. It is imperative that any reforms to our current system of securities regulation measure up to this objective."

Having witnessed events for the last ten years and read many report from experts and various recommendations we would recommend the following:

1. A National Regulator for Financial Services (NRFS) similar to Québec's Autorité des marchés financiers. The website of the Autorité states: The Autorité des marchés financiers administers different laws and regulations applicable to Québec's entire financial sector. For each of four sectors of activity, the laws, regulations, guidelines, and all other legal texts concerning the organizations merged into the Autorité. The Securities Sector, the Distribution of Financial Products and Services Sector, the Financial Institutions Sector, and the Compensation Sector are all incorporated in the Autorité des marchés financiers. The NFRS should work with an enforcement agency such as the RCMP/police or Attorney General depending upon revised securities legislation.
2. A National Investor Protection Authority (IPA) with a mandate for investor protection in all financial sectors. The IPA would be independent from the industry regulators and empowered to investigate or order investigations by police or regulators. The IPA would be established by statute and funded by Government. It could report to the Auditor General. The IPA would incorporate a special tribunal to hear investment complaints from small investors and pronounce judgment in timely fashion. When industry is found to have committed fraud or wrongdoing by the IPA, the IPA would also be empowered to order restitution to the victims from an Investor Protection Fund. These funds would be recovered from industry and supplemented with punitive fines against firms who commit wrongdoing or employ representatives who do. The IPA would also have Financial Services Victims Assistance Unit that will be staffed by specialists that can assist victims to deal with their situation and provide guidance on how to proceed. There are cases where victims need counseling and there should be provision for gaining exemption from limitation periods for those who proceed to civil litigation.
3. A Financial Services Investor Protection Fund (FSIPF) that would respond to the IPA. This fund would be available to make payments to victims of financial wrongdoing including fraudulent acts, deceptive practices, or embezzlement, and would be paid out upon instruction from the IPA. Payments made to victims would be recoverable from the industry. The firms would be responsible for repayment for any wrongdoing by the firm or their representatives. In the event of bankruptcy of the firm the industry would be responsible through insurance or the regulators to compensate the FSIPF. The Government would provide initial funding to be recovered from the industry and/or regulators.
4. A Financial Services National Registration Database (FSNRD) to record all Complaints and Settlements in the Financial Sector. This NRD would be similar to the ComSet database established by the IDA but would be accessible to the public to enable investors to determine is a registered representative is disciplined. This database would have an alphabetical list of representatives and firms similar to that

provide by the BCSC and NOT accessible only be a search mechanism as some other regulators provide.

5. National Financial Services Legislation that will govern the financial services industry. It should be written to accommodate the new reality and be forward looking to cope with new developments. It should ensure that protection is provided for TruthTellers to enable witnesses to come forward without fear of persecution. It should make provision for enforcement of rules and regulations and establish financial penalties for financial wrongdoing such as disgorgement of profits, payment of losses plus interest plus expenses plus moral and punitive damages. It should prohibit gag orders in settlements and other forms of cover-up to enable the truth to be exposed, and call for principles based regulation.
6. A Special Court for Financial Crime with a judiciary schooled and experienced in securities litigation and white collar crime to hear cases involving financial crime that are not suitable for resolution by the IPA tribunal. This could include major fraud, systemic practices, large institutional investors or pension funds, or complex cases requiring court resolution.

During the transformation period Government should establish an special implementation office that would initially research the issues raised so that the shortcomings of the present regulatory system can be rectified to ensure the new financial services regulator is structured to be able to monitor financial services activities and root out corruption and unsavory practices that are decimating seniors savings and eroding their retirement security.