SIPA Sentinel

January 2006

SIPA has a mission:

- **to aid public awareness of how the investment industry operates;**
- **to provide guidance to those who have a complaint about investments with a bank, broker, financial advisor, or other seller of financial products;**
- **and to advocate improvement of industry regulation and enforcement.**

Small Investor Protection Association - A voice for the small investor

The **SIPA Sentinel** offers articles and re-prints with opinions SIPA may not share.

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Protect Your Savings

Many Canadians have lost their savings when they placed their trust in their Investment Advisor (IA) and failed to monitor their account or to question the IAs activity. In some cases the investors did monitor their accounts and questioned the activities but were misled.

Sometimes investors lost their savings due to incompetence but in most cases it was due to deliberate wrongdoing by IAs who were most influenced by the amount of money they were making rather than what was best for the investor.

Some of the reasons for substantial loss are:

- Discretionary trading without proper authority
- Unsuitable investments
- Leveraging
- Lack of diversification
- Deceit and Fraud

Most victims of substantial loss were concentrated in unsuitable investments, had insufficient diversification and were leveraged. Whatever the reason for loss it is very difficult to get even a portion back after your savings are lost.

So what can you do to protect your savings?

- Only invest with companies that are registered with the regulators and that are insured against bankruptcy. Contact your provincial regulator to verify that your Investment Advisor and the company he works for are properly registered.
- Do not trust your savings to someone to invest in an investment that you do not understand.
- Find out how much you will pay your I.A., and if there are any fees to be paid when you want to cash out.
- If there are guarantees find out who provides the guarantee and if there are conditions. (i.e. you may need to hold the investment for an extended period of time and there may be a possibility of bankruptcy)

- Unless you control all investment decisions you should not borrow money to invest (home mortgage, bank loan, or dealer margin loan). Many financial institutions promote leverage. It is good for them. It significantly increases your risk of substantial loss.
- Diversify your investments so that no more than 15% is in one investment product. There is always some risk in investments. G.I.C.s and government bonds are low risk but the returns are modest. Mutual funds, income trusts, principal protected notes and other innovative products have varying degrees of risk and some are simply unsuitable.
- Be careful about "innovative products" and promises of high returns that are much above the returns paid on secure investments. Be wary of Business Trusts, PPNs, Limited Partnerships, special financing and any other products offering high returns.
- If you are over 50 years of age make sure a substantial portion of your savings are in secure investments. Do not risk your savings for higher returns if you risk major loss.
- Before you invest in anything ask yourself "How much can I afford to lose?" Discuss this with your I.A. and make your plans accordingly.
- Ask for monthly statements and monitor them to ensure that you are in tune with the general investment market and there is no trading activity of which you are not aware.
- If there is activity in your account that you have not approved report immediately to the Compliance Officer of the company.
- If the company does not provide a satisfactory response immediately, contact the regulators and get some independent expert advice as quickly as possible.

Be aware that the regulators will not get your money back. The industry offers the Ombudsman for Banking Services and Investments to recommend settlements and the IDA Arbitration Program. Feedback suggests that these processes will provide only partial recovery.

Victims who resort to civil action to gain restitution must be prepared for a tough battle that could take many years. Several provinces have reduced the limitation period from six years to two years. This means that victims now have only two years from the cause of action within which to initiate action, so you can't waste a lot of time trying to resolve your dispute through the industry's complaint handling processes. If you do have a problem get some expert advice as soon as possible.

Fund companies face lawsuit - From Tdalerts@globeinvestor gold.com

TORONTO - Mutual fund companies that allowed "market timing" trades face a class-action lawsuit organized by a Toronto law firm specializing in such litigation.

Rochon Genova LLP said Wednesday the claim filed in Ontario Superior Court names IG Investment Management Ltd., CI Fund Management Inc., Franklin Templeton Investments Corp. and AGF Funds Inc.

IG, CI and AGF reached settlements last December with the Ontario Securities Commission under which $97.7-million was distributed to fund investors hurt by market timing. Franklin Templeton followed with a $49.1-million OSC settlement in March.

The Rochon Genova claim alleges those amounts drastically understate the losses to long-term unitholders caused by market-timed trading & high-speed in-and-out buying and selling of mutual fund units to take advantage of transient price staleness on foreign holdings in other time zones.

The lawsuit states that the management companies breached their fiduciary duties and were negligent in allowing market timing between September 1998 and September 2003.

Joel Rochon, a partner at Rochon Genova, said AIC Inc., which settled with the OSC last December for $58.8-million, and other fund operators may be added to the action.

He said 17 Canadian mutual fund companies were implicated in the market-timing scandal.

Mr. Rochon did not specify the amount of damages being sought, but said it would be in the "hundreds of-millions of dollars".

Pushing parties for investor protection - From the Toronto Star

Jan. 10, 2006
JAMES DAW

A lobby group for seniors and investors is calling for some pre-election commitments on such issues as jail time for financial advisers and other market participants who defraud investors.
Leaders of the Concerned Canadian Seniors and Investors, or CCSI, say votes of some 300,000 Ontario members, and possibly 10 million investors across Canada, could be swayed by investor-protection issues.
"Investors and seniors are concerned enough for this issue to influence the way they vote in the coming general election," the group said in a news release yesterday.
The appeal for parties to make election promises on issues important to investors came as leaders were preparing for last night's debate leading up to the Jan. 23 federal election.
Opposition parties have made a lot of mileage by criticizing the Liberals for their handling of the Nov. 23 announcement about the tax treatment of income trusts and dividend-paying stocks.
The announcement of a police investigation into whether information was leaked to certain market participants has put the government on the defensive, even though no one has yet been named in the investigation.
But the complicated area of regulation and enforcement in the financial sector has not been treated as a potential vote magnet, even though abuse of investors can have dire consequences for their financial and psychological well-being.
"Widespread and well-documented corruption in the financial-services industry is only the tip of the iceberg," the lobby group claims.
"The larger problem is inadequate enforcement by governments and regulators of laws already on the books."
"The situation will get worse until perpetrators begin to be sent to jail rather than sent on their way with a friendly reprimand," argues the CCSI, a coalition of the Small Investor Protection Association and the United Senior Citizens of Ontario.
Some financial advisers are convicted and jailed for fraud each year, but few receive sentences as stiff as those issued in the United States.
Even fewer serve the entire terms of the sentences.

Other infractions that lead to financial losses may be investigated only by provincial securities commissions or self-regulatory organizations, which may ban participants from working in the industry and set fines but rarely obtain compensation for investors.
For example, last week the Investment Dealers Association of Canada barred James Michael Brennan of Ottawa from the securities industry for life and ordered him to pay penalties and costs totaling $300,000.
The self-regulatory organization said Brennan, a 40-year-old father of four, had misappropriated $124,000 from three accounts in his mother's name when he worked at the Ottawa branch of Assante Capital Management Inc., which has since been taken over by CI Financial Inc., between November 2000 and June 2003.
No compensation was ordered.
A thirst to see more people sent to jail has been sharpened by the prosecution of a handful of top United States executives on a variety of offences that led to investor losses.
Professor Poonam Puri of the Osgoode Hall Law School at York University argues in a recent paper for the Capital Markets Institute that criminal prosecution can act as a significant deterrent to abuses in the financial markets.
She predicts that more criminal offences will be prosecuted as a result of amendments to the Criminal Code enacted last year, setting out new offences for tipping or trading on inside information, and for taking retaliation against whistle-blowers.
Maximum penalties for existing fraud offences were increased to 14 years from 10 and judges were given greater guidance for sentencing.
Puri argues that criminal prosecution should be saved for the most egregious offences, and that regulators should expand their focus from enforcement of regulations to providing assistance to investors to receive compensation for losses.
In addition to more jail sentences, the Concerned Canadian Seniors and Investors group is calling for a new federal Consumer Council of Financial Affairs, or CCFA, to advocate for consumers with both federal and provincial governments, regulators, law-enforcement bodies and financial institutions.
"It should have the power to investigate and independently publish its findings, possibly modeled partly on the very successful Financial Services Consumer Panel in the United Kingdom. ... A division with the proposed CCFA (should) provide a one-stop mediating and remedial service for all consumer redress concerns."

New Law Helps Investors: Permits Class Actions for Stock Fraud

Douglas Lennox of Klein Lyons

Aggrieved investors got a New Year's Eve present for 2006. That's when the Ontario government's long awaited legislation for strengthening the rights of investors went into effect. The new law, known as Bill 198, creates important new civil remedies for investors who have been the victim of stock fraud.

Until this year, the options for Canadian investors who were deceived into buying a stock by the false statements of an issuer were limited. Unless those false statements had been made in the issuer's prospectus, and the investor bought shares on what is known as the "primary market", then the investor did not have a remedy under the old legislation. The term "primary market" refers to stock purchases made during an initial public offering from an underwriter. About 95% of stock transactions are not made on the primary market, but rather, are made on stock exchanges in what is known as the "secondary market". Such secondary market transactions were not covered by the old legislation. Likewise, there are many documents that an issuer may use to attract investors, beyond just a prospectus, such as press releases, quarterly and annual reports, and other financial information. Under the old legislation, misleading statements made by issuers outside of a prospectus did not attract civil liability.

Bill 198 changes all that, and helps to level the playing field for ordinary investors. Now, investors have the right to sue for all misleading statements, and not just those contained in a prospectus, and for all transactions, not just those made in an IPO. In creating these rights for Canadian investors, our law may be said to be catching up with the United States, where American investors have, for many decades, enjoyed such rights to sue. Bill 198 has also helped to resolve an unfairness in our law, which treated investors differently, depending on whether they had bought in primary or secondary markets.

The most important impact of Bill 198 is in the area of class actions. For reasons of cost, and efficiency, if ordinary investors are to sue big corporations over stock fraud, then they need to be able to join together to pursue these cases as class actions. It does not make economic sense, for an example, for an individual investor who has lost a few thousand dollars on a stock to pursue a lawsuit alone. The cost of hiring a lawyer for a single investor in those circumstances would exceed the money lost on the investment. But if there are other investors in the same situation, then these claims may be combined so that it becomes economic for them to proceed together. A law firm may agree to act on behalf of such a group of investors on a contingency fee basis, and may help to bring the investors together as a group. The law firm may agree to cover all of the costs and expenses of investigating and pursuing the case, and may only charge the investors for this work if, and when, money is recovered by way of settlement or trial. The fee charged is then fixed as a percentage of the money recovered for the group, with the rest going to the investors as compensation. At the end of the case, a court reviews the fees, to make sure they are fair and reasonable, and are based upon the work done, and results achieved.

Bill 198 facilitates class actions by allowing for what is called "deemed reliance". That is, where an issuer releases misleading information, all investors who subsequently purchase stock in the company are legally presumed to have received that information, and to have been influenced in their stock purchases. Such investors are not required to come to court and prove that they actually received the information, or that it actually affected their purchases. As a practical matter, deemed reliance is critical to the manageability of a class action. If there are thousands of investors, and every single one of them has to come to court to prove their claim, then the class action cannot proceed. Put simply, it would take decades for everyone to testify. Rather than risk being overwhelmed by so many witnesses, the court will dismiss the case.

This is what happened in class actions involving *Bre-X*. In 1997, following public revelations that *Bre-X* stock was worthless, and its mineral claims falsified, class actions were filed across Canada by investors. In the absence of any statutory remedy, these lawsuits asserted old common law remedies for fraud and negligent misrepresentation. Such common law remedies, based on centuries of precedent, proved ill-adapted to modern securities litigation. At common law, a plaintiff must come to court and testify. Since thousands of

Canadians had purchased *Bre-X* stock, the case became unworkable, and the *Bre-X* class actions were dismissed against most of the defendants involved.

The legal concept of deemed reliance in Bill 198 is based on an economic theory known as "fraud-on-the-market". This theory states that where a corporation releases misleading information, the stock market as a whole reacts. Not every investor may receive the misleading information, but some will, and their actions will impact the market for everyone. The price of the stock will become inflated, and all investors will suffer. Prior to Bill 198, Ontario securities legislation did allow investors to claim deemed reliance if they had purchased stock on primary markets, but not for secondary market purchases. This enabled a handful of securities class actions involving primary markets to be brought and successfully resolved in Canada. The number of such cases was limited however, as most trading takes place on secondary markets.

Bill 198 has been a long time in coming to Canada, and its arrival was delayed for years by strong opposition from certain business-lobby groups. This opposition was misplaced. Laws which are good for the rights of investors are also good for business. Such laws encourage better corporate governance, and ethical business behaviour, and they punish the contrary. They also help to maintain investor confidence in our capital markets, encouraging more investment. Opponents of Bill 198 claimed that certain lawsuit abuses, alleged to exist in the United States, might be replicated in Canada if Bill 198 were passed. In response to this accusation, it may be said that stories about frivolous lawsuits in the United States are based much more on media myth and anecdote, than on reality or actual evidence. Repeated studies of American securities class actions by Stanford University Law School have not found evidence of abuse, but rather, have concluded that such lawsuits have been an important source of compensation for innocent investors in many legitimate cases. The *Enron* and *Worldcom* class actions in the United States, for example, have recovered billions of dollars in compensation for defrauded investors.

To address business-lobby concerns about the potential for frivolous lawsuits under Bill 198, a number of compromise provisions were included in the legislation. These provisions have the effect of diluting the rights of investors. These provisions include a cap on the amount of damages that may be recovered by investors, and a requirement that investors obtain leave of the court, showing a meritorious case, before being allowed to a commence a lawsuit under the statute. These provisions are unfortunate as they make it more difficult and time-consuming for investors to pursue legitimate claims, and they may result in investors receiving less than full compensation for their losses. The damages cap under the legislation, for example, provides that an issuer may be liable to investors for only $1 million, or 5% of its market capitalization, whichever is the greater. There may be cases where investors' collective loses will greatly exceed these amounts, and where the issuer may effectively profit from its misleading statements by having its liability capped. Bill 198 does provide an exception to this rule, permitting investors to recover their full damages, and bust this damages cap, but only if the investors can prove deliberate misconduct by the issuer. This is a hurdle that may be very difficult for investors to satisfy. Such evidence may not be forthcoming.

Our Canadian legal system already provides substantial safeguards to prevent frivolous litigation. The additional compromise provisions in Bill 198 are unnecessary and may deny investors full compensation. Despite these limitations, Bill 198 is still a significant improvement in shareholder rights. Investors now have a remedy where formerly they did not. The legislation may not be perfect, but it does give investors an important new legal avenue to make their voices heard.

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Investors Have Their Say in the Sentinel

SENIORS - AWAKE and ARISE! If you don't want to lose control of RRIFs – PAY ATTENTION!

Twenty years ago, as a result of a Charter Rights lawsuit, Ottawa conceded seniors the unfettered right to control how their RRIF money was invested. This was born the "self-directed RRIF". Now an association of private business is subverting senior rights and, in effect, exercising Big Brother control over investments. The IDA (Investment Dealers Association, authorized by the Ontario Securities Commission) is an "SRO – self regulated organization". SROs are mandated by provincial governments to regulate their members, NOT THE CITIZENRY! Nonetheless, aided and abetted by the OSC, the IDA has decreed investment dealers must demand all sorts of personal financial data from a client (net worth? Property? Have accounts with other dealers? Etc.) If a client refuses to respond or a dealer doesn't like the answers, he is required to freeze the account. Also, in a viable account, the dealer is now an IDA appointed Big Brother/nanny. When you place an order to buy a security with YOUR money, the dealer is required to decide if the investment is "Suitable" for you! If it is not so in his "opinion", he is required to freeze your order. When you protest, OSC, IDA and dealers state, with smug arrogance, this is all for your "protection" – whether you want it or not, and no, you can't sign a release, waiving their "protection". They claim their right to interfere with citizens' accounts is absolute and complete.

Clearly a "self-directed" RRIF cannot have two masters. I am now engaged in a fight to free my blocked account and restore total control of my money to me. Please contact me if you are having the same problem. For all others: wake up. Don't wait for 800 lb gorillas to come and squat atop your funds, override your rights and decide the "suitability" of how you invest your lifetime savings. If you want such protection, fine. But it should be an option, not an imposition.

SROs vs The Public

It is correct to state that the IDA is a "self-regulatory organization ... required to REGULATE ITS MEMBERS ..." The IDA, OSC, CIBC-WG, etc. all seem to have a congenital mental lapse in grasping that regulating members DOES NOT mean regulating clients or customers! Engineers, architects, MDs, lawyers, dentists, etc. are all licensed by their respective SROs. **None of these are empowered to impose punishments if a client refuses to reveal certain personal info or accept a professional recommendation**. When a citizen chooses to act thusly, any concern about some resultant liability falling on the professional can be easily relieved by a client signed waiver. There is no "right" for Big Brother/SRO to control a citizen without the citizen's express consent.

Lester Templeton, Jr, 2104-25 Bay Mills Blvd, Toronto, ON, M1T 3P4

SIPA Letter to the Chair of the Ontario Securities Commission Investor Advisory Committee

January 26, 2006

Mr. Eric Kirzner
Chair OSC Investor Advisory Committee

Dear Mr. Kirzner,

Congratulations to you and the members of the Investor Advisory Committee who have been selected by the Ontario Securities Commission to participate in this initiative following the OSC Town Hall Event last May when a crowd of over 500 overwhelmed the panel with an unending host of questions and complaints.

This is the first time in Canada that an Investor Advisory Committee has been created that includes members representing retail investors.

We look forward to reading the committee's reports and believe Ontario retail investors, and all Canadian investors will also be interested.

Therefore, if the OSC approves, SIPA is prepared to publish the committee reports on the SIPA website at www.sipa.ca.

We hope that this committee will be successful in putting forward the concerns of retail investors, and that this initiative will lead to change in the regulatory system that will result in improved investor protection to provide remedial measures for victims who have lost their savings due to investment industry wrongdoing.

Sincerely,

Stan I. Buell, P.Eng.

President

Comments from Kansas City

A new survey of American investors conducted by the **Opinion Research Corp.** for the **Securities Investor Protection Corporation (SIPC)** and the **Investor Protection Trust**. Sadly, surveys that show Americans lack the most basic financial knowledge are all too common.
Stephen Harbeck, SIPC president said it is like this:

¦ Just 21 percent of investors say they practice all four desirable behavioral traits mentioned in the survey: regularly reviewing account statements, reading prospectuses, checking out the disciplinary backgrounds of brokers/financial planners, and having a financial plan in place.

¦ Only 36 percent of investors who use a broker or financial planner checked out that person's disciplinary background. Perhaps even more disturbing, Harbeck said, 61 percent in this group said they failed to do so because they trusted the adviser and 9 percent because the adviser assured them that there was nothing to be concerned about.