④ SIPA Sentinel
November 2004

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 pursue improvement of industry regulation and enforcement.**

Small Investor Protection Association - A voice for the small investor

SIPA Sentinel

The SIPA Sentinel is issued bi-monthly. From time to time we include articles that offer opinions on subjects related to investing and the regulatory system. These are meant to help increase investor awareness, and SIPA may not share these opinions.

SIPA Trivia

In 2003 SIPA's website received on average 11,970 hits per month. This year to date it has received on average 16,454 hits per month and in October 25,802 hits.

CARP / SIPA Report on Mutual Funds

Giving Small Investors a Fair Chance – Reforming the Mutual Fund Industry is the title of CARP's Report and Recommendations in partnership with the Small Investor Protection Association - September 2004.

The report examines the mutual fund industry and makes a number of recommendations for reform. The Number 1 recommendation is that a federal Investor Protection Act should be passed which includes the establishment of a single, national, independent Investor Protection Agency (IPA) accountable to Industry Canada or the Attorney General of Canada.

This is an important recommendation that will be followed up with the federal government by CARP and SIPA. SIPA's members have already communicated with every M.P. across Canada to ensure they have a copy of the report.

The report was presented to the Honourable Tony Ianno at a media conference on September 28th. In a preliminary meeting the Minister discussed the report with CARP and SIPA representatives. The minister stated he would discuss the report with the Minister of Industry, Hon. Lucienne Robillard, and the Minister of Finance, Hon. Ralph Goodale.

CARP and SIPA agreed to work with the Minister to develop strategies to move this initiative forward.

There was a good turnout for the media conference with several journalists, a couple of TV cameras, investor advocates and SIPA members, and industry representatives including OBSI's Mike Lauber. Glorianne Stromberg was also present.

The IDA was quick to respond to the CARP Report. Their comments in an advertisement in the Investment Executive are;

The Investment Dealers Association of Canada today responded to "Giving Small Investors A Fair Chance, Reforming the Mutual Fund Industry", a report issued by the Canadian Association for Retired Persons (CARP).

In a statement, the IDA said the CARP report includes a number of redundant recommendations where rules or policies are already in place as well as a number of inaccuracies.

The media also wrote about the report:

Rob Carrick, Globe and Mail, said:

The only way to improve protections for small investors in Canada is to get politicians interested, and the only way to do that is to have investor advocacy with clout.

Ellen Roseman, Toronto Star, said;

Buell gets lots of publicity, but he hasn't been able to move his agenda forward. That could change now he's allied himself with an *advocacy organization 100 times his size. … Reform is a tough nut to crack. But with CARP beavering away, I feel better already.*

Linda Leatherdale, Toronto Sun, said:

In a joint press release, CARP and SIPA warn, "The mutual fund industry suffers from deficient regulations, abusive industry sales practices, excessive fees, inadequate governance and lax regulatory enforcement."

John DeGoey, Globe and Mail, said:

The most important recommendation is that the federal government should pass an investor-protection act, creating an independent investor-protection agency, which is accountable to the federal government.

NOTE: Every SIPA member should write their Member of Parliament for Canada and also their Member of Provincial Parliament, and ask them to support this important initiative for a national Investor Protection Agency.

Response to SIPA's Five Year Report

In February this year SIPA issued a report entitled The Small Investors Perspective of Investor Protection in Canada. It was based largely upon anecdotal evidence gathered since SIPA was founded in 1998.

We have had the opportunity of speaking with hundreds of small investors and also with individuals working in the investment industry. This has enabled SIPA to outline how the industry operates and the challenges faced by investors in dealing with this industry.

The report was delivered to 25 leaders across Canada including the Prime Minister, the provincial premiers and several other key ministers and leaders.

Some of the responses are shown in part to illustrate the range of response received.

SIPA continues to contact both our provincial and federal politicians.

Lorne Calvert, Premier of Saskatchewan, Feb 20;

"Thank you for outlining your Association's concerns regarding the impact of unethical investment advisors. I have taken the liberty of forwarding your letter to Honourable Frank Quennell, Q.C., Minister of Justice and Attorney General, for his information."

Ralph Klein, Premier of Alberta, Feb 25;

"I have taken the liberty of forwarding your comments to the Honourable Greg Melchin, Alberta's Minister of Revenue, for his review and further response on behalf of the Government of Alberta."

Prime Minister's Office, Feb 25;

"You may be assured that the points you raised, on behalf of the Small Investor Protection Association, along with your support for the Government's measures to address the Auditor General's concerns, have been carefully reviewed. … I have taken the liberty of forwarding a copy of your letter to the Honourable Lucienne Robillard, Minister of Industry…"

Office of Minister of Finance, Mar 04

"I wish to acknowledge receipt of your correspondence which was referred by the Office of the Prime Minister, the Right Honourable Paul Martin."

Jean Charest, Premier of Quebec, Mar 2;

"Thank you for your letter in which you ask the government to provide investor protection.

Your query falls under the mandate of Mr. Yves Seguin, ministere des Finances and will be passed on to him to provide you with an appropriate response."

Bernard Lord, New Brunswick Premier, Mar 3;

"Small investors are the backbone of Canada's capital markets and your organization is an important voice for them. The introduction of a new Securities Act and the establishment of the New Brunswick Securities Commission will be significant milestones in New Brunswick's

economic history and of great benefit to your members."

Greg Melchin, Alberta Minister of Revenue, Mar 15;

"I have been working with other provincial ministers responsible for securities regulation on an initiative to reform the way securities are regulated in Canada. Providing provincial securities commissions with the authority to order restitution to investors is an option that will be carefully considered as we move forward."

Office of P.E.I. Premier, Mar 26;

"Please be assured that Premier Binns is aware that you have written and is appreciative of your efforts on behalf of our citizens."

Greg Selinger, Manitoba Minister of Finance, May 03;

The Government of Manitoba shares the views of the Small Investor Protection Association (SIPA). That is why we amended the Manitoba Securities Act in 2003 to allow the Manitoba Securities Commission to order financial compensation (restitution) to an aggrieved investor after an administrative hearing."

Cabinet du premier ministre, Quebec, May 4;

"Rest assured we have taken your document and its content into consideration."

Yves Seguin, Quebec Minister of Finance, May 5:

"An indemnity fund exists in Quebec for the victims of fraud in insurance and in mutual funds. We are studying with interest the possibility of expanding this indemnity to the victims of fraud in securities sector as well."

Ralph Goodale, Minister of Finance, May 31;

"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."

Jim Middlemiss is a freelance writer and lawyer based in Toronto. He's a frequent contributor to National Post, Investment Executive and Wall Street & Technology. The following article is on the Internet.

How safe are your mutual fund investments?

By Jim Middlemiss • Bankrate.com

A coalition of consumer groups is calling on the federal government to create an investor protection agency that would help oversee the mutual fund industry and protect Canadians' investments.

That is one of 17 recommendations put forward by the Small Investor Protection Association (SIPA), a volunteer organization that tackles investor issues, and CARP, a nonprofit organization that represents the concerns of Canadians over the age of 50.

The report, Giving Small Investors a Fair Chance: Reforming the Mutual Fund Industry, comes at time when the mutual fund industry faces an Ontario Securities Commission (OSC) probe into trading abuses. The commission has already sent notices of potential enforcement proceedings to four major fund-management firms asking them to respond to issues raised in the notice. The OSC also warned that more firms could receive enforcement notices in the coming days.

The commission says it has found examples of what it believes is market timing, a trading strategy that allows an investor, usually a large firm, to leverage discrepancies in stock prices across time zones by rapidly trading in and out of mutual funds.

While not illegal, market timing has a negative impact on long-term investors. The OSC says the conduct seems to have ceased. As well, it indicated that there was no evidence of late trading, which is trading that takes place after hours, usually following news that could move stocks. Such conduct is illegal.

The OSC probe comes after a U.S. crackdown on mutual fund trading practices in that country, which to date has resulted in almost $3 billion in fines. Stan Buell, founder and president of SIPA, says when it comes to investing and consumer protection, more needs to be done by both the industry and investors themselves.

"Investors need to become educated, as that is really the only way that they can avoid the pitfalls of losing their savings due to wrongdoing by the industry," he says.

Average investors need an industry watchdog

The report, which was presented to Tony Ianno, the federal minister for families, caregivers and seniors, sets out 17 recommendations and highlights the problems small investors face when investing.

The biggest is a lack of national investor protection. SIPA wants the federal government to pass an Investor Protection Act, which would establish a national securities regulator, which Canada currently lacks. Normally, oversight of the public markets is done at a provincial level, through securities commissions and self-regulating organizations.

A national securities commission is currently being examined and debated by a number of industry participants, but there is little consensus among provincial and federal governments on the need for a national regulator.

SIPA is also calling for the establishment of an Investor Protection Fund, similar to the Canada Deposit and Insurance Corporation, to protect investors if a fund company or dealer goes broke.

The 20-page report also calls for an overhaul of complaint systems that are "foggy and ineffective." It also calls for better disclosure of fees and the risks involved in owning a mutual fund and better reporting of fund performance.

The report also attacks what it calls "undisclosed marketing arrangements that could encourage financial advisors to recommend one fund over another for personal/corporate gain," noting that such arrangements should be disclosed or prohibited.

The coalition has other ideas on how better to protect the investments of Canadians, such as a 15-day cooling-off period, which would allow investors to cancel investments bought at an investor education seminar, in the same way that consumers can back out of deals made by door-to-door salespeople.

The report also wants the arbitration system governing disputes between investors and their advisors to increase its limits to $350,000 from the current $100,000.

Industry players say existing rules are enough

Another area of concern is how complaint records are maintained and retained in the mutual fund industry. The report calls for more transparency, but the Investment Dealers Association of Canada (IDA), which regulates brokerage firms and their sales forces, says those are already in place.

The IDA largely panned the SIPA/CARP report, noting in a statement that it contained "redundant recommendations" and "a number of inaccuracies."

For example, the IDA notes that Canadian regulators have "rules in place to prohibit compensation arrangements that create unacceptable conflicts of interest in the sales of mutual funds." It also points out there are already regulations in place requiring investment firms to maintain and retain records of complaints.

John Hall, a lawyer in the financial services practice at Toronto's Borden Ladner Gervais LLP, says the "level of analysis was shockingly poor" in the SIPA/CARP report. He says a lot of issues the report raises are already being addressed by regulators "or are in the throes of coming into place."

As for the notion of an Investor Protection Agency, Hall says it's wishful thinking, noting that provincial regulators can't agree on setting up a single, national securities regulator, something that has "floundered for the last two decades. I don't think it's going to happen," he says.

However, Hall agrees with the report's call for whistler-blower legislation that would protect employees who report non-compliant activities by their employers.

But when it comes to SIPA/CARP criticism of industry practices towards investors, Hall says there are already a lot of investor safeguards in place. "The real issue is whose job is it to educate the public on that and what's the best way?"

Buell, whose organization documents abuses investors have suffered at the hands of their financial advisors, says the problem is "there are codes of ethics and written rules, but it seems even corporate guidelines are not followed."

But he's optimistic the system will be changed for the better. "It will take time, but the industry is aware of the problem and (participants) realize that they must change if they are to survive. If they do not change investors will seek other alternatives."

Reprinted from AOL Personal Finance

Hans Merkelbach writes the following article. Hans was born and educated in the Netherlands, but came to Canada in 1956. In Canada, he worked as stock broker/options broker, a bond trader for Gairdner & Company at the Bank of Montreal, as well as several other investment firms over his career as a financial planning specialist. Hans writes, "I have been very busy in my so-called retirement. You can view my involvement on behalf of investors in "My Annual Report Card for 2003" at: http://www.strategicsector.com. I take on new clients sparingly as the present ones demand my full attention."

How Much To Put In Stocks? Zero! You heard right. ZERO.

By Hans Merkelbach

Hans Merkelbach

I offer Eric Troseth's article for The Christian Science Monitor, pointing out Yale economist Robert Shiller's admission that only 10% of his own money was in stocks and the warning of Ben Inker, director of asset allocation for Grantam, Mayo, and Van Otterloo & Co. (GMO), a money-management form with some US$ 85 billion in assets, who believes zero should be in domestic equities. You heard right. ZERO.

But contrast these views with strategists averaging 64% allocation to stocks, and obviously, mutual fund pros. Fidelity Magellan is the world's largest actively managed fund with $ 62 billion in assets and is so large that it has been closed to new investors for years. Cash position? Try 0.8% of total assets as of the end of July!

Should we pay attention to so-called gurus most of which has been discredited during the collapse of the Nasdaq in 2000? Should we pay attention to so-called analysts who are paraded onto the TV screens of CNBC and in Canada ROB TV? With certain exceptions like Alan Newman, Ross Healy, Bill Fleckenstein, John Embry and David Chapman these "analysts" are in most cases beholden to a pay-cheque issued by their prejudiced employers.

We do not need gurus and analysts who are beholden to their employer's pay cheques. What is needed at this manic stage of the equity markets are independent analysts, preferably the contrarian kind.

My synopsis: unless one is invested in sectors which are friendly to the underlying fundamentals one should be cognizant of the fact that investors in general have not learned from the March 2000 debacle in the equity markets and that potentially the equity markets are headed for another disaster. When? I don't know! Listening to the wrong pundits, gurus or whatever name you attach to that "circus" could be dangerous to one's financial health. Bill Fleckenstein in one of his most recent Reports says: " I don't know how long the bulls intend to drink the fundamentals pretty and party on. But when whatever they're drinking starts to turn sour, things are liable to get ugly, rather violently."

The information contained in this email is not to be construed as investment advice. I recommend that the reader seeks out his/her own counsel.

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What are the issues for Small Investors?

By Stan I. Buell, SIPA

“Giving Small Investors a Fair Chance: Reforming the Mutual Fund Industry” is a report prepared by a team of CARP and SIPA representatives. The report started as a mutual fund report drawing upon the expertise of Ken Kivenko, Chair of SIPA’s Advisory Committee. At an early meeting of the project team of Judy Cutler, Bill Gleberzon, Ken Kivenko, Robert Kyle and Stan Buell it was decided to incorporate a concept proposal for an Investor Protection Agency.

Glorianne Stromberg had examined the mutual fund industry and wrote a report for Industry Canada entitled “Investment Funds in Canada and Consumer Protection” and released in 1998. This report outlined the weaknesses in the regulatory system and made detailed recommendations for improvement. The report did not sit well with industry, as they preferred the status quo.

There were subsequent reviews and studies culminating in a Wise Persons Committee that produced another report “It’s Time” in December 2003. These wise people reviewed most all of the previous studies and reports and reached the conclusion that it was time for Canada to have a single national regulator. This was the recommendation of Ms. Stromberg in 1998.

Elliot Spitzer, the New York State Attorney General set the U.S. investment industry on its ear with his Bureau of Investment Protection headed by David Brown (not the OSC Chair), former assistant attorney general. The Bureau was enabled to act on the basis of the New York State Securities Law, commonly known as the Martin Act, and the Sarbanes/Oxley law, formally titled The Public Company Accounting Reform and Investor Protection Act.

Spitzer pursued a strategy based on investment protection rather than regulation. The Bureau was alerted to wrongdoing by whistleblowers because they are protected in the U.S. by legislation. Spitzer’s office accomplished what the mighty Securities and Exchange Commission could not. Wall Street brokerage firms and mutual fund

companies lined up to pay fines and avoid extended litigation that would have destroyed their firms. Some of the firms suffered considerable damage just from the publicity. Here in Canada the OSC is still investigating market timing, which is really a non-issue as far as extreme investor loss is concerned.

The CARP Report outlines many of the problems with the mutual fund industry and concludes that if investors are to be adequately protected there must be an independent agency with the authority to provide investor protection.

At present the provincial regulators have delegated investor protection to the SROs that represent the industry. This conflict of interest situation does not provide fair treatment for investors. The IDA was quick to criticize the CARP/SIPA report. Although they say they are responsible for investor protection, their attack on investor advocates indicates their interests lie solely with the industry.

The industry will employ tactics to discredit investor advocates and attempt to justify the way the industry operates … they have a lack of transparency, a laissez faire policy and a flagrant disregard of rules and regulations.

Eliot Spitzer has now exposed how the investment industry operates in the United States. First the brokerage houses on Wall Street, then the mutual fund companies coughed up hundreds of millions of dollars in fines to try to keep a lid on a deteriorating situation for the investment industry.

Canadians would be naïve to think our investment industry is any different. SIPA has documentation of file that corroborates the statements that have been made and illustrate industry's attempts to defend situations that are morally and ethically indefensible.

How many times have I heard or read that a mutual fund company or an investment dealer attempts to justify that all of their actions were appropriate when seniors have lost 50% and more of their life savings?

The issues for small investors are not so much the refinement of rules, a new set of recommended best practices, or mutual fund market timing or late trading.

The most important issue for small investors is the extreme loss being suffered by those who have been victimized by widespread industry practices of wrongdoing. Many of the victims have no opportunity to replace the loss and their futures are compromised.

An Investor Protection Agency, coupled with TruthTeller protection, and a means of dispute resolution that is affordable and timely is what is needed to save our seniors from financial hardship caused by industry wrongdoing.