SIPA Sentinel

February 2008

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 and re-prints that offer opinions on subjects related to investing and regulation. These are meant to help increase investor awareness, and SIPA may not share these opinions.

BEWARE REVERSE MORTGAGES

SIPA continues to believe that "Reverse Mortgages" are not a good product for most Canadians. While it is a means of getting equity out of your home, it is really a costly short term solution. We believe there are less costly ways of obtaining cash using your home as collateral. You should seek assistance from a good tax accountant prior to making any commitment for a reverse mortgage. An article from the New York Times indicates that some of those selling reverse mortgages tie them into investments that may be unsuitable. This combined with fees often results in unsatisfactory situations. The feedback we receive is that most plans are collapsed in less than five years usually at great cost to the homeowner. The following are excerpts from the NYT article:

Tapping Into Homes Can Be Pitfall for the Elderly

Sandy Huffaker for The New York Times

Erika Baker says she was steered into a loan with high fees.

By CHARLES DUHIGG

Erika Baker was 67 years old, divorced and worried about her job when a saleswoman showed up at her door in late 2006. A reverse mortgage, the saleswoman explained, would give Ms. Baker instant access to hundreds of thousands of dollars tied up in the value of her home. Such a loan, typically available only to homeowners in their 60s and older, would not have to be repaid until Ms. Baker moved out, the saleswoman said. And if she never moved, the loan would be settled by selling her house after she died. "Your Home Pays You Cash!" read a brochure the saleswoman left behind. Ms. Baker, who lives just outside San Diego, jumped at the offer, borrowing a little more than $200,000 through a company called Senior American Funding.

Then the problems began. The saleswoman pressured her to put the proceeds of the loan into complex investments that put her money out of reach, Ms. Baker said. She *received only about $33,000 in cash, far less than she needed for her final years. "I thought this was a safe way to make sure I'd never run out of money," Ms. Baker said. "Then everything became so confusing. No matter where I turned for help, it seemed like things got worse."*

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" a former sales agent, Hani Shenoda, and an agent who still works at the company who spoke on the condition of anonymity because of fear of retribution, said in interviews that managers at Senior American Funding encouraged them to pressure older homeowners into unwise loans and investments. The company disputes that assertion.

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"In the kitchen of the home, where Ms. Baker displays watercolors of dolphins and flowers she has painted, the saleswoman recommended a loan of $218,900, with a variable interest rate initially set at 6.57 percent. Because reverse mortgages do not require borrowers to make immediate repayments, the interest charges are added to the debt every day, and the total amount owed grows over time. The saleswoman did not explain that within 10 years, Ms. Baker's $218,900 loan could grow to as much as $400,000, Ms. Baker said. That debt would be paid by selling the house when she moved out or died. The saleswoman also did not emphasize the high fees, Ms. Baker said. The loan's fees cost her $17,100 — almost 8 percent of the total loan — which was paid out of the proceeds as soon as the loan closed."

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A survey released last year by AARP, formerly known as the American Association of Retired Persons, of more than 1,500 reverse mortgage borrowers found that almost one in 10 were urged to buy other financial products, like annuities.
Lawsuits against reverse mortgage companies, including the nation's largest, Financial Freedom Senior Funding, contend that those firms helped pressure older Americans into bad investments.

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New laws governing reverse mortgages are under consideration in Congress, though lobbyists for some lenders are mounting strong opposition, Congressional staff members say. For Ms. Baker, now 68, such safeguards would come too late. She says she wakes up in the night, terrified there will not be enough money for food, gas or anything else. To cut her grocery bill, she stopped buying meat and fresh vegetables. "Before, at least I knew my house was safe, and that no one would take that away from me," she said. "Now, I don't know if there is anything I can count on."

TAX FREE SAVINGS PLANS

The 2008 Federal Budget introduces a new Tax Free Savings Plan. This is good news for Canadians and provides an excellent vehicle for savings to grow tax free. Unlike Registered Plans, any amounts withdrawn from the TFSP will NOT be taxable. This will give Canadians the flexibility of withdrawing their savings without incurring tax liability. The following is from the Finance website:

"The Tax-Free Savings Account is the first of its kind in Canadian history," said Minister Flaherty. "It will provide all Canadians with a powerful incentive to save. An RRSP is primarily intended for retirement, but the Tax-Free Savings Account is like an RRSP for everything else in your life."

How the Tax-Free Savings Account Will Work

- *Starting in 2009, Canadian residents age 18 or older will be eligible to contribute up to $5,000 annually to a TFSA, with unused room being carried forward.*
- *Contributions will not be deductible.*
- *Capital gains and other investment income earned in a TFSA will not be taxed.*
- *Withdrawals will be tax-free.*
- *Neither income earned within a TFSA nor withdrawals from it will affect eligibility for federal income-tested benefits and credits.*
- *Withdrawals will create contribution room for future savings.*
- *Contributions to a spouse's or common-law partner's TFSA will be allowed, and TFSA assets will be transferable to the TFSA of a spouse or common-law partner upon death.*
- *Qualified investments include all arm's-length Registered Retirement Savings Plan (RRSP) qualified investments.*
- *The $5,000 annual contribution limit will be indexed to inflation in $500 increments.*

This new type of account should be a boon for Canadians to accumulate savings tax free that will provide more flexibility that the current registered savings plans for which tax is applicable on withdrawals.

INVESTMENT DECISIONS AND RATES OF RETURN

Most Canadians invest primarily in mutual funds or segregated funds. RRSPs and RIFs generally hold these funds. In recent years investors have invested in other structured products such as income trusts and principal protected notes. In many cases investors sought other forms of investment as the rate of return on G.I.C.s, Treasury Bills and Canada Bonds have deteriorated. Sadly many Canadians have seen their savings eroded due to decreasing value of these investments and reduced or suspended distributions.

Many investment experts suggest that funds are not an efficient way to invest. Keith Ambachtsheer issued a report that suggests ordinary Canadian investors are losing $25 billion per year when their fund returns are compared to returns obtained by those who manage pension funds.

Some experts suggest that investors would be well advised to invest in Electronically Traded Funds (ETFs) that track the indices. The concept is similar to mutual funds in that they provide diversification over the market or a particular sector of the market, but ETFs do not have the high fees associated with mutual funds or segregated funds.

Statistics show that very few funds can achieve the returns of the stock market indices. and if they do it is not on a consistent basis. As a result it would seem that a good investment strategy would be to invest in a combination of cash, bonds and ETFs.

The CASH component (G.I.C.s/Treasury Bills) provides readily available cash for immediate expenditures.
The BOND component (Government Bonds) provides security of capital and a modest rate of return.
The ETF component provides exposure to the stock market with the possibility of growth and the risk of loss. This component is for longer term investments … 5 years or more.

As an example:

Rate of Return	2003	2004	2005	2006	2007
CASH	3.9%	2.9%	3.0%	3.0%	2.9%
BONDS	4.1%	4.0%	3.7%	3.9%	4.0%
ETF (XIU-T)	22.5%	12.5%	23.5%	17.1%	8.9%

A Portfolio with 10% cash, 40% Canada Bonds and 50% ETF XIU would've provided:

Annual Return	13%	9.5%	13.5%	10.5%	7.0%

Many investors have obtained higher rates (up to 5%) in the recent past for G.I.C.s. You should keep in mind these rates are negotiable so you need to ask for a better rate. Compare your rate of return with the above table. Let us know how you did.

Benchmarks beat managers in 2007: SPIVA

An Advisor.ca article February 29, 2008 by Mark Noble indicates *"the vast majority of Canadian mutual funds continue to underperform their benchmark, according to the latest results of Standard & Poor's Indices Versus Active (SPIVA) Funds Scorecard.*
In 2007,

- *only 24.3% of Canadian equity funds beat the S&P/TSX Composite Index,*
- *while 37.0% of Canadian dividend and income funds beat the S&P/TSX Canadian Dividend Aristocrats Index. "*

"Over the past three years, only 13.3% of actively managed Canadian equity funds outperformed the S&P/TSX Composite Index,

while only 3.2% of active managers beat the S&P/TSX Canadian Dividend Aristocrats Index."

"Data included in the SPIVA report card and other similar studies are commonly used to support an "if you can't beat them, join them" attitude to investing, which champions the cheaper exchange-traded and index fund alternatives to actively managed mutual funds. "

ACCOUNT STATEMENTS

Do account statements show you what you need to know? Many account statements do not provide investors with essential information. Many show either book value compared to market value of this month compared to last month. Neither of these shows how your investments are doing over the longer term. Many statements show book value compared to market value for mutual funds. However, when losing funds are sold the book value is reduced so eventually the statement will indicate market value exceeds book value even though the value of your account may be less than the money you invested.

Many investors have reported confusion about their account statements. If your statement is not clear and does not provide the annualized rate of return for your account, ask your advisor to provide a better statement. Often these are available for the asking but are not offered unless requested.

Make sure your statement shows the information you need to know. You should also receive monthly statements or quarterly statements at a minimum.

EXPERT PANEL TO REVIEW SECURITIES REGULATION

On February 21, 2008, the Government announced the appointment of an Expert Panel to review Securities Regulation. Deja Vue? In December 2003 the Government Wise Persons Committee issued a report entitled "It's Time". The report concluded that Canada should have a national regulator and it is time to implement it. That was over four years ago. Nevertheless, SIPA has responded and advised the Executive Director that SIPA will make a written submission and is interested in meeting with the panel. Terms of Reference are available on the Finance website and their work is to be completed by the end of 2008 … Five years after the Wise Persons Committee Report. If you would like to make comment for the SIPA submission please send them to stanbuell@rogers.com. The following is from the GOC website:

Ottawa, February 21, 2008
Government of Canada Appoints Expert Panel to Review Securities Regulation

The Honourable Jim Flaherty, Minister of Finance, today announced the chair and members of an expert panel charged with providing advice and recommendations on securities regulation in Canada.

"I am asking the panel to develop a model common securities act to create a Canadian advantage in global capital markets," said Minister Flaherty. "This effort will build on positive steps taken in recent years by the full range of partners, including provinces, territories and regulators, contributions by private sector groups, and international best practice."

The expert panel will provide independent advice and recommendations to ministers—federal, provincial and territorial—on the best way forward to improve securities regulation in Canada.

The expert panel will be chaired by the Honourable Tom Hockin, P.C., former Minister of State (Finance) and former president of the Investment Funds Institute of Canada. Also appointed are:

- *Ian D. Bruce, Chief Executive Officer, Peters & Co Limited.*
- *Denis Desautels, Executive-in-Residence, University of Ottawa, and former Auditor General of Canada.*
- *Hal Kvisle, President and CEO, TransCanada Corporation.*
- *Dawn Russell, QC, Associate Professor, former Dean of Law, Dalhousie University.*
- *Terry Salman, Chairman, President and CEO, Salman Partners Inc.*
- *Heather Zordel, Partner, Cassels Brock & Blackwell LLP.*
- *Also appointed today are special advisors to the panel:*
- *Howard Davies, Director of the London School of Economics and former chairman of the United Kingdom's Financial Services Authority (FSA).*
- *David Green, Advisor on International Affairs, Financial Reporting Council and former senior executive with the FSA.*
- *Peter W. Hogg, QC, Scholar in Residence at Blake, Cassels & Graydon LLP and professor emeritus, Osgoode Hall Law School, York University.*

The expert panel will be supported by a small secretariat and other professional resources.

LIMITATION PERIODS

Much has been said about reduced limitation periods being reduced from six years to two years. While we believe this is unfair and unjust one must bear in mind that it applies only to duty of care situations. We continue to believe that most investment industry wrongdoing involves “fiduciary duty” to which the two year limitation does NOT apply.

Unfortunately the definition of fiduciary duty is not as clear cut as it could be and the judges will say it is dependant upon “a finding of fact”. Therefore the first step in any case could be determining whether fiduciary duty applies.

CAN'T AFFORD A LAWYER? CONSIDER SELF REPRESENTED LITIGANTS

With the high cost of civil litigation more Canadians are turning to representing themselves in court. To do this you must learn about the court system and the law. While this approach may be more successful in family law matters, some have used this approach for securities approach with varying degrees of success.

A good place to start is the Canadian Judicial Council Project on Self-Represented Litigants and Accused Persons website at http://cfcj-fcjc.org/research/srl-en.php. In Ontario a non-profit agency, Pro Bono Law Ontario provides a help centre for litigants at 393 University Avenue. Their website is http://www.pblo.org/

The Canadian Bar Association also provides information on Pro Bono Services at http://www.cba.org/CBA/groups/probono/default.aspx.

SIPA's PRO BONO LEGAL CONSULTATION

Recognizing the reluctance of many victims of investment industry wrongdoing to approach high cost lawyers, arrangement have been made with a number of securities litigation lawyers to provide a pro bono (FREE) initial consultation to SIPA members with a dispute. You simply need to provide a minimum of documentation and an initial consultation will be arranged. Take advantage of this FREE service for SIPA members.

Dispute Resolution in Retail Investor Loss Cases Roundtable

SIPA was represented by Ken Kivenko at the Roundtable organized by Osgoode Professional Development on January 30 in Toronto. It was attended mostly by lawyers, regulators, OBSI and corporate Ombudsmen. No media. Here's a summary of their report:

Best suggestions - Increase small claims court limit to $50,00 and consider a Neutral Evaluation process [Neil Gross]
Most shocking comment [to us] - IDA boards failure to approve an increase in the arbitration limit to $350,000. [The recommendation to increase the threshold for the IDA arbitration program was considered and has been reviewed over the years with no change. At the relevant time a decision was made not to change the $100,000 threshold and it has not been changed. The fact that there is a threshold does not prevent anyone, at least in theory, from any of the parties waiving the threshold stated. The threshold only applies to obligating IDA firms to participate in an arbitration and to restrict their ability to decline participation. Beyond the $100,000 threshold both parties are in the normal arbitration process which anticipates both

parties to voluntarily participate or not.]
Biggest surprise - animosity towards OBSI and their plans to deal with systemic cases
Disappointment - lack of audience interaction and engagement in retail investor issues
Second biggest surprise - Corporate Ombudsmen feel threatened by proposed 90 day rule giving right to investors to refer case to OBSI without further delay
Weirdest statements - the complaint system is working by MFDA and by IDA - IDA arbitration system is not unwell
Best question - How will we assess improvements once CSA approves proposed IDA/MFDA complaint handling system changes?
Best confirmation - Except for unusual circumstances, the OSC has not and does not intend to apply Section 128 of the Ontario Securities Act that empowers it to apply to the Court for investor restitution
Worrisome number- The range of numbers for a civil litigation case to be viable varied from $100,000 to $500,000

IFIC lets its position be known on investor complaints. Fund industry lobbyist IFIC has responded to OBSI's Request for Comments on proposed changes to its Terms of Reference. Last year, to the delight of investor advocates, an independent assessor recommended that OBSI look at systemic issues, not merely individual cases in isolation. This element of the proposal would allow OBSI to identify, investigate and recommend compensation in situations where the original complaint led to discovery of loss or overcharging for multiple unsuspecting others. Now IFIC wants to derail this pro-investor initiative. Here's an extract of their submission:
" .. The proposal to enable OBSI to investigate "potential Systemic Issues" and, further, to require a Firm to provide privileged and non-privileged information for use in an investigation, even when it is not the subject of a complaint, are substantial powers which duplicate, and even exceed, regulatory mandates. Our industry does not view it appropriate that OBSI, which is not held to the high standards of due process that are required of a statutory body, have such a mandate. We encourage you to work closely with the multiple regulatory agencies in considering revisions to your TOR such that they do not include regulatory powers..."

So, if OBSI notices say a miscalculation on a number of complaints from a particular firm IFIC says ignore the obvious pattern and deal with each individual complaint with blinkers on. Or worse, a pattern of unsuitable investment recommendations should, according to IFIC, just be ignored leaving each retail investor to fend for himself. It's hard to see how this is in the public interest. Ombudsmen organizations in other countries – the UK and Australia - successfully investigate systemic issues. Such a common sense investigation process would of course tend to reduce the value to the industry of onerous "gag orders" imposed on individual complainants who settle.