# SIPA Sentinel

June 2012

Small Investor Protection Association - A voice for small investors


The SIPA Sentinel is issued bi-monthly. From time to time articles and re-prints are included that offer opinions on subjects related to investment and regulation. These are meant to help increase investor awareness, and SIPA may not share these opinions.

## Know Your Client Forms – Finally the OSC takes action

Many of our members reported issues with their Know Your Client forms. SIPA had made a submission specifically on forged signatures on KYCs but there has been no positive action. Recently, Mary Condon, Ontario Securities Commission, spoke out about the OSC intent to check with clients as well as firms when they check on KYCs. Inevitably the industry is opposed to such a move by the OSC citing various reasons including it could raise concerns amongst clients that the firm is being investigated. If their record is clean and they have provided accurate KYCs to their clients and kept them updated they should have nothing to fear. However, past practices indicate there is an issue with inaccurate KYCs. This is a welcome initiative on the part of the OSC, but the initiative is receiving strong pushback from the industry.

The OSC is proceeding to improve the Fund Facts document for mutual fund disclosure, but they need to take action on client statements to ensure that investors are receiving essential information and are not being mislead. Of course there are many intertwined issues which could be ameliorated by simply holding the investment industry to a fiduciary responsibility. If the industry acted responsibly there would be less need for detailed rules and regulations. As it is now investing is simply INVESTOR BEWARE.

Let us hope that the OSC will continue with some of its initiatives, listen to investors, and resist industry's pushback against change.

## *SC compliance calls likely to alarm clients - EMDA (Exempt Market Dealers Association of Canada) calls on regulator to actively publicize new policy* *By Megan Harman, June 27, 2012*

*The Ontario Securities Commission's (OSC) new policy of calling clients of registered firms during compliance reviews is likely to alarm clients, and could cause "significant" reputational damage to industry firms, exempt market dealers say.*

*At a conference hosted by the Exempt Market Dealers Association of Canada (EMDA) in Toronto on Tuesday, speakers raised concerns about the OSC's recent announcement that it would begin contacting clients of registered exempt-market dealers, scholarship plan dealers and portfolio managers as part of its routine compliance review process. The purpose of the practice is to verify the accuracy of information given to OSC staff about a firm's relationship with its clients.*

*"It's important to recognize that the regulators need some levers to pull to get the information, the facts," said Brian Koscak, chairman of the EMDA and partner at Cassels Brock & Blackwell LLP in Toronto. However, he said he's surprised that the OSC decided to implement this practice without consulting members of the industry. "There should be more dialogue with the street on how this should be done in a fair and equitable way that protects investors, allows the regulators to do their jobs as well as protects dealers, how they do business, and their reputations."*

*David Gilkes, vice chairman of the EMDA and president at Toronto-based regulatory consulting firm North Star Compliance & Regulatory Solutions Inc., said he can understand why the OSC has decided to contact clients directly during compliance reviews. "If you're going to call clients, you will get accurate information, perhaps, on whether their KYCs are filled out correctly; you will be able to question whether or not the investor understood the product that he or she was buying," he said.*

*"However," Gilkes added, "clients don't necessarily tell the truth."*

*Indeed, he's concerned that clients might blame their dealer or advisor for poor performance of their portfolio, or give the regulator different information about their risk tolerance than they gave their dealer. Another concern is that clients will be alarmed by getting a call from a regulator, and could interpret it as a sign that their dealer or advisor has engaged in misconduct. "We know what investors are like. They're not necessarily rational," Gilkes said. "The potential reputational damage to a dealer is significant."*
*Toronto-based Advocis, which represents financial advisors across Canada, has raised similar concerns about the new practice. To minimize potential reputational damage caused by the calls, Gilkes said the OSC should actively publicize the new policy so that investors are well aware that they could receive a call from the regulator as part of routine compliance examinations. "Right now, that message hasn't gotten out there, and I'm pretty sure investors are going to be frightened when they hear a call from the OSC," he said.*

## Perception or Deception - What you may not know about registered representatives called "Financial Advisors"

A couple of weeks ago after paying golf with my golfing buddies, one of them mentioned dissatisfaction with his mutual fund investments. We then had a discussion about the investment industry and how the public is often deceived. Lack of disclosure means most investors are in the dark. I mentioned the fact that persons that call themselves "Financial Advisors" (with an O) are generally registered representatives with a responsibility to sell products. They do not have a fiduciary duty to their clients and are not legally required to put clients' interests first. There are representatives who do put their clients first and provide a good service. However the lack of fiduciary duty can and does result in issues which cause investor loss.

I have always been intrigued by the fact that the industry regulators allow this sort of deceipt to be practiced, and is a contributing factor to why I believe all persons and firms who provide advice or sell financial products should have a fiduciary duty to their clients, with the exception of those who are simply taking orders for a product. These latter individuals should be called salespersons or order takers to show the real difference from one who provides advice whatever they are called.

A few days ago I received an e-mail from my golfing friend on the subject of "Advisors with an O" and "Advisers with an E" which I will pass on. He was interested enough to do some research and found the following article from the web:

# I ❤ Wall Street.

### *Advisor or adviser?*

*Posted on April 16, 2011 by **Scott Bell***

### *Merrill Lynch boosts assets, adds advisers*

*From Reuters*

*Bank of America Corp's (BAC.N) Merrill Lynch brokerage business provided a bright spot in an otherwise dismal first quarter for the* *bank, reporting sharply higher revenue and client assets as well as a net increase of nearly 200 financial advisers.*

*You probably didn't even notice it. – It might be a typo.*

*The increase in financial advisers.*

*Ya see, there's a pretty monstrous difference between an Advisor with an 'O' & an* ***Adviser****. Your friendly neighborhood broker is typically called a Financial Advisor. Not an Investment Adviser. Or Financial Adviser. At least not always. And there's a good reason. Their role is as chameleon-like as their title, changing minute to minute & without having to tell you. Slippery.*

*It all comes down to* ***fiduciary responsibility,*** *which makes self-dealing really hard. And Wall Street loves dealing to itself.*

*So instead, you are placed in relationship silos.*

*For this account? I'm your broker aka your Financial Advisor. For that account? I'm your Investment Adviser. For bonds, I'm a broker. For Investment Managers, I'm an Adviser. For mutual funds, if it's a small amount of money– probably Broker. If it's a big pile of cash, Adviser. Stocks? Could be an Advisor or an Adviser.*

*Annuity? Broker. Long Term Care? Broker. Financial Plan? Adviser, but to implement it – Advisor. Life Insurance? Advisor. And an Advisor is a Broker, right?*

*Confused yet? Now add an army of bankers institutional sales people, stuffing god knows what into the mutual funds & managers you're Advisor (and even Adviser) is probably using.*

*So, no matter how you slice it, the house always wins.*

## WHAT ARE THE REGULATORS DOING?

Why do the regulators including the CSA (Canadian Securities Administrators) allow this misrepresentation to continue. For many years the registrant sales persons were registered as "sales representative" (now dealer's representative) but are allowed to call themselves "Advisors (with an O)". It was "Advisor with an (O)" because there is a registration category of "Adviser" (this is Adviser with an E) and so in their legal minds they believed this subtle difference was legally defensible.

The reality is that many Canadians are not so good at spelling and Advizer with an E or an O is like a Dockter with an E or an O. Surely the regulators must recognize this as "smoke and mirrors". It's high time that the regulators clean up the investment industry and hold them accountable by holding them to a Fiduciary Duty.

## PONZI SCHEMES KEEP HAPPENING

Although regulators claim to protect investors they state that it is preventative rather than remedial. History shows that regulators are unable to prevent fraud and wrongdoing from happening on a regular basis. Therefore regulators must change and provide remedial investor protection by providing restitution to victims of fraud and wrongdoing by the regulated industry.

At the same time legislation must be changed to address the issue of non-regulated sales of investment products. The investment scene in Canada is complex. In addition to provincial and federal regulators there are exempt markets and exemptive relief provided by the regulators. Small investors should invest only with the regulated market and first check with the regulators to determine the registration of the individual and firm, as well as the products they are registered to sell.

## ANOTHER PONZI PLAY – IN CALGARY

### *Two charged in $35M scheme; Family team accused of bilking clients*

*By Clara Ho, Calgary Herald*

*A Calgary investment company owner and his daughter face fraud charges in connection with an alleged $35-million Ponzi scheme in which trusted clients, family and friends were bilked, say RCMP.*

*While these charges relate to 43 people who invested about $6 million, RCMP say there could be hundreds more victims reluctant to come for-ward.*

*Some of the people - mostly older investors - have been unable to retire and had t,o re-turn to work after they took out lines of credit and mortgaged their homes to invest in the scheme, police say.*

*"It's very unfortunate be-cause people's lives change dramatically when they get involved in these scams and getting the bottom end of the stick, so to speak," said Supt. Eric Mattson, of the RCMP Calgary Integrated Market Enforcement Team.*

*Robert Sellars, 75, and Penny Sellars, 48, both of Calgary, were each charged with two counts of fraud over $5,000 and two counts of theft over $5,000.*

*An investigation was launched in January 2010 after an investor filed a complaint alleging that he had been defrauded by Robert. Investigators examined files dating to March 2003.*

*Police say Robert was a successful insurance salesman for 50 years and started his own company, Sellars Financial Inc., in 1992.*

*He recruited some of his insurance clients, friends and family to invest with him, and promised returns of 15 per cent to 18 per cent annually, and on occasion as high as 24 per cent and 36 per cent annually, Mattson said.*

*Robert's daughter, Penny, worked with her father as an insurance saleswoman and was later employed at the investment company where she helped recruit investors, he said.*

*Investors were reportedly told their money would be invested in gold mining operations and European money markets. In some cases, they didn't ask where their money was going because they put their trust in Robert, Mattson said.*

*Sellars Financial raised about $35 mil-lion from about 350 people, with one person investing as much as $1 million. But when the company collapsed in 2009 and declared bankruptcy in 2011, many people lost millions, he said.*

*"The investments were not put in place where they could reasonably expect to ever create the income that they were promised," Mattson said. "The investments did not pay out. What was paid out was investors paying other investors.*

*"Our opinion was they were using it to supplement their lifestyle, but not necessarily living the high lifestyle. In this particular case, an awful lot of money was repatriated to some of the victims."*

*Police sent letters to about 300 possible victims asking them to help with the investigation, but only 100 people replied.*

*The charges laid relate to information from 43 of the 100 people who responded, whose investments total about $6 million, Mattson said.*

*It's not uncommon for people to be reluctant to come forward, he said.*

*Some are embarrassed about investing in something unfamiliar, others have involved their friends and family and don't want to "lose face," and some have made returns and don't want to get taxed, Mattson said.*

*This particular Ponzi investigation was "unique" because most of the financial transactions remained within the province, he said, adding most of the victims were from Alberta.*

*Only once in this investigation did police travel overseas to trace a money trail, though Mattson declined to elaborate.*

*In general, Mattson said red flags to look out for include the promise of high, sustained and consistent returns on investments, as well as the threat of losing money if the police are notified.*

*Robert Sellars has already served jail time following a regulatory investigation by the Alberta Securities Commission.*

*In October 2010 he was handed a two-year sentence in Alberta provincial court in relation to the alleged Ponzi scheme after being found guilty of making misleading or untrue statements to investors and breaching a 2006 commission order by trading in securities without being registered.*

*He was also banned from trading in securities and ordered to pay nearly $2 million in restitution to four Alberta investors. Mattson confirmed Robert has since been released and is on probation.*

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## ANOTHER PONZI FROM THE HALIFAX CHRONICLE-HERALD

### *Five Albertans stung by N.S. Ponzi scheme*

*Byline: Bill Power Staff Reporter*

*At least five Albertans were duped by a couple of Nova Scotia Ponzi schemers who bilked millions out of investors.*

*Documents obtained Friday from the Alberta Securities Commission indicate fraudsters Quintin Earl Sponagle and Trevor Wayne Hill persuaded at least five Alberta residents to invest in their illicit Jabez Financial Services Inc.*

*The Alberta commission said it has reciprocated a permanent ban on trading imposed on the two men by the Nova Scotia Securities Commission.*

*"Securities commissions in other provinces will implement reciprocal bans when there is evidence residents of a particular province have been victimized," Tanya Wiltshire, with the Nova Scotia commission said Friday.*

*The Nova Scotia commission levied $500,000 fines for securities fraud against Sponagle and Hill, the biggest fine available at that time. They were also banned from trading in investments in future in this province.*

*Alberta stepped in with its own ban after learning at least five residents of that province were bilked in the fraudulent investment scheme.*

*"It was determined they posed a threat to Alberta investors so we issued a reciprocal order," Mark Dickey, with the Alberta commission, said.*

*The Nova Scotia commission alleged that Sponagle and Hill promised investors, including some from Lower Sackville's Rock Church where Hill was a parish-ioner, returns of up to 214 per cent through Jabez.*

*A commission tribunal found that $4.2 million of investor money was deposited in a Curacao bank account Sponagle controlled. Authorities shut down the scheme in late summer 2006.*

*The Nova Scotia commission will not say if they ever collected the fines levied against Sponagle and Hill.*

*It is in general difficult to obtain fine payments in these cases, said Wiltshire.*

*"Many of the people we place sanctions against are Ponzi schemers and don't have any money," she said.*

*The securities commission in this province does not have criminal code authority to pursue individuals when fines go unpaid, Wiltshire said.*

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## INVESTMENT ADVICE FROM THE TORONTO STAR

## *Avoid common investing mistakes;*
## *Some things will go wrong in your investment life, but you can learn from the duds, and you should have a plan*

*Everyone makes investing mistakes from time to time. But what sets successful investors apart is their ability to learn from setbacks and go on to build their fortunes on a stronger foundation.*
*In a 2010 CNBC interview, billionaire Warren Buffett admitted that the worst stock he ever bought was Berkshire Hathaway, which has long been the foundation of his empire. He took the company over in 1965 because he was angry with its manager, Jack Stanton, and was stuck with Berkshire's declining textile mills for years afterward.*
*Of course, Berkshire still went on to become a multi-billion-dollar conglomerate. But in Buffett's estimation, ploughing money into the struggling textile firm instead of starting a new entity cost him and his shareholders a whopping $200 billion over the years.*
*The takeaway? Don't invest based on emotion (see mistake #5 below).*

*The good news is that most investment mistakes are easy to spot before they trip you up. And with a simple course correction, you'll be able to steer clear of the vast majority of them.*
*Here are five common ones:*
*1. Not having a plan: Just as a business will inevitably founder without a sound business plan, you need a clear strategy for meeting your goals. A solid investment plan takes into account your time horizon, the amount you have to invest now and plan to invest in future years, your age and your risk tolerance. By clearly identifying goals, you'll also have a better understanding of exactly what to invest in at different stages of your life.*
*If you don't yet have a plan, don't feel bad. According to the Financial Planning Standards Council, just two in 10 Canadians have one. But it's never too late to start.*
*2. Being too aggressive: Younger investors often feel they should be more aggressive, because they have longer to recover from mistakes. However, that's the opposite of the approach they should be taking, according to financial author and investment newsletter publisher Gordon Pape. That's because if you take steep losses when you're young, you'll waste years just getting back to your starting point.*
*"Instead, younger investors should be more conservative," says Pape. "This lets you get a better understanding of investing with less risk. That way, you'll be able to make more sophisticated choices later on."*
*3. Owning too many investments: The average North American mutual fund holds 220 securities. If you hold a number of funds, that quickly multiplies so that even your winners will barely budge your overall returns.*
*Raymond James financial advisor Bryan Snelson typically recommends that his clients hold between eight and 12 securities (that could include individual mutual funds, stocks, or fixed income investments like GICs).*
*Too many more than that, he says, and your portfolio becomes too difficult to manage. You also increase your risk of getting into investments you don't fully understand.*
*4. Not asking enough questions: When seeking an investment advisor, it's fair game to ask questions until you're completely comfortable with the advice you're getting.*
*If you don't understand something, say so. And if you feel you're still not getting the information you need, it's time for another advisor.*
*5. Not being focused: It's easy to pay too much attention to short-term market moves.*
*Instead of investing based on what you hear in the news, spend more time building and updating your investment plan. That will give you a clear framework to guide your future decisions - and act as a counterweight to any emotion-based moves you may make.*
*Know the difference between mistakes and bad luck. Sometimes you do everything right and you still end up on the losing end. But if you focus on quality and diversify appropriately, winners will more than offset losers over time.*
*Toronto writer Chad Fraser's work has appeared on The Successful Investor Network and Investing Daily investment websites.*

## CLIENT ACCOUNT STATEMENTS

Many client account statements do not provide sufficient information to properly inform the small investor so that appropriate decisions may be made. Many statements do provide a list of the investments and the current market value compared to last months market value. This is amongst the worst type of statement. Others provide a list of investments with book value and market value. This is better because the Book Value is your cost and the Market Value is what it is worth today, but it does not show investment performance and can be misleading when losing investments are sold to reduce total account Book Value to mislead investors into thinking the performance is better than it is. One lady called to say “My Advisor tells me I am making money, and my statement says I am making money but I have less money now than I had five years ago, how can that be? The answer is in the Book Value vs. Market Value type of report.

Account statements should report the annualized investment return for each holding and the total account as an absolute minimum to properly inform investors. Anything less can be misleading at best. The statement should also show how the return compares to a benchmark. The new Fund Facts is suggesting the benchmark the rate for GIC's … the implication being if your investments are not doing better that GICs, why are you risking your investments?

## SOME WISDOM FROM THE FUND OBSERVER

***This was written in 1998!*** *"...Another key dimension to disclosure is the account statement. Again, it has not been customary to view account statements as being part of the disclosure system. However, they are an essential part of it. Account statements provide an important opportunity to give investors the information that will answer their most basic question which in this context is "just tell me how I am doing". Consumer/investors should be able to use their account statements both to check the accuracy of the recorded transactions and to monitor whether their portfolio allocation is appropriate to what their goals are. In this respect, there is a need to develop some measures that will help consumer/investors understand how they are doing. The information provided by these measures will help them to evaluate how their investment objectives are being met and whether modifications are needed.....The present requirements for account statements are primarily transaction-oriented rather than advisory-oriented. They do not reflect the shift by intermediaries from a transaction-based relationship with their clients (with the advice being ancillary) to an advisory-based relationship with their clients (with the transactions being ancillary). They do not reflect the substantial bundling of services that is occurring through wrap accounts, pooling and asset allocation services, and fund-of-fund arrangements...".G. Stromberg, INVESTMENT FUNDS IN CANADA AND CONSUMER PROTECTION STRATEGIES FOR THE MILLENNIUM , Oct. 1998, Para 17.10 Account Statements*
*www.sipa.ca/library/Documents/Stromberg_Inv**Funds**-Oct1998.pdf*
***Obviously, regulators weren't listening these past 12 years - they've been consultationing.***

## SIPA Development

SIPA will be re-developing the SIPA website and has engaged a web designer to begin work. We estimate an autumn launch of the new website. We plan to have a focus group to formulate the new website and determine its content. There will be major revisions both in format and content.

SIPA members are invited to submit their comments on what they found useful on the current website and what they would like to see added or deleted. As substantial changes are anticipated this is your opportunity to contribute by making your comments to sipa.toronto@gmail.com.

At the same time communications will be a priority as we go forward. Systems for voice and video communications have been explored during the past year as well as social networking. The intent is to incorporate Twitter and Facebook in our communication strategy and employ chat systems and video conferencing to enable active participation of members from every province.

We expect to have a new newsletter editor, Dr. David Yudelman, in place by July, and future issues will include regular articles from Ken Kivenko, chair of SIPA's Advisory Committee, who also publishes the Fund Observer newsletter. A link will be provided to Ken's newsletter in the new website. 2012 should be an exciting year in the development of SIPA and we look forward to receiving your input to assist with this venture.