Kenmar Associates

Dedicated to Investor Protection

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Comments on OSC Notice 11 -753 Priorities for fiscal year ending March 31, 2011

Kenmar welcomes the opportunity to comment on the DRAFT Statement of Priorities. In our view, the *primary* purpose of securities regulations and regulators is to protect investors. Hence, we believe the priorities should be heavily biased towards investor protection initiatives. It is also necessary that SRO's be required to align themselves with Commission priorities. A disconnect between the MFDA's priorities for example, with the OSC's goals, would significantly de-optimize the whole process.

By way of introduction, Kenmar is an Ontario- based organization focused on mutual fund investor education via on-line papers hosted at www.canadianfundwatch.com. Kenmar also publishes ***the Fund OBSERVER*** on a bi-monthly basis discussing investor protection issues primarily for mutual fund investors. A subsidiary, Portfolio Analytics, assists abused investors and/or their counsel in filing investor restitution claims.

Recent high profile corporate scandals such as ABCP, "advisor" abuse and Ponzi schemes, growing retail investor unrest and changing demographics (seniors, pensioners and retirees) suggest that investor protection demands HIGH priority attention. Billions of dollars are being needlessly lost each year. A November 2009 report by PricewaterhouseCoopers found that Canada was the fourth most fraudulent nation in the world -- behind Russia, South Africa and Kenya. http://www.pwc.com/gx/en/economic-crime-survey/download-economic-crime-people-culture-controls.jhtml In this environment, the OSC must be constantly vigilant on behalf of the investor.

According to a study by Osgoode law school associate law professor Poonan Puri, *How Effective is Capital Market Enforcement in Canada?*, the role of regulators needs to be re-evaluated because of a "disconnect" that exists between how they view their mandate and what investors expect. According to Ms. Puri, securities regulators have historically interpreted their mandate as forward-looking and deterrence based. On the other hand she points out, individual investors who have lost their savings due to the misconduct of regulated market participants are most concerned about being compensated or made whole. To bridge the gap, Prof. Puri recommends re-evaluating the role of securities regulators. "Moving forward, perhaps the securities regulator should act more as a facilitator or catalyst to assist investors in receiving compensation" –this advice should be taken seriously by the OSC and **action** plans should be evident in the list of 2010/2011 priorities that address the issue.

With the evolution of the investment markets, a multitude of complex new products and the volatility in today's markets, investor risks are much greater than ever before. Accordingly, there should be a bias towards enforcement action on existing rules and a de-emphasis in 2010/2011 on new rule making. Investor losses have reached epidemic proportions in the last 5 years with horrific consequences to individuals and the Canadian social system. Senior abuse in particular continues to emerge as a serious issue. We recommend the establishment of a Branch dedicated to seniors issues.

For the 2010/2011 priorities, we note that the Commission has identified four strategic goals to achieve over the next five fiscal years but no metrics or milestones are provided. They are: identify the important issues and deal with them in a timely way; deliver fair, vigorous and timely enforcement and compliance programs; champion investor protection, especially for retail investors; and, support and promote a more flexible, efficient and accountable organization. In principle, the items listed are "OK" but it is definitive actions that will speak louder than flowery words. For instance, what exactly does "Champion' mean and how will it be measured? We refer the OSC to the National Quality Institute www.nqi.ca for processes to enable these changes and a path to excellence

We would like to enumerate some specific recommendations regarding investor protection priorities:

1. An **Investor Advisory Panel** along the lines of the Australian Securities Commission and the U.K.'s FSA should be established. It should have a separate mandate, staff and funding. This structure would assist investors in having a real voice at the OSC as regards regulation, issues, priorities, goals and operations. We urge the OSC to proceed with this recommendation without undue delay ensuring that adequate funds are provided for in this year's operating budget.

2. **Mutual funds:** Fund governance has been a critical investor issue since at least 1995 with the issuance of the Stromberg reports. The 2004 mutual fund market timing scandal and the Norbourg fiasco highlighted once again the importance for independent fund governance boards and the maintenance of robust regulatory provisions and prohibitions. We are deeply concerned that National Instrument NI 81-107 Investment Review Committees effectively allows the elimination of long-standing conflict- of -interest prohibitions. Furthermore, Canadians pay some of the highest mutual fund fees in the world, no doubt in part due to lack of fund governance.

We believe the POS disclosure initiative has been hijacked by industry participants. It has been a sore spot with the investor advocacy community for over a decade. Kenmar recently submitted a comprehensive critique explain why the standard deviation is not an appropriate risk measure. The current fiscal year should be the year that the OSC makes it clear that investor protection supersedes other interests.

The OSC should make U.S. mutual funds available to Ontarions -a priority task that would see fees reduced and competition increased would be in the public interest.

Mutual funds have over $ 600 billion in assets and embrace the lives of well over 10 million Canadians .This is an industry that effectively is entrusted with the nest eggs of Main Street Canadians.

3. **Enforcement:** The unacceptably long time to bring firms and individuals to justice and the lack of results is well documented. Cases like Bre-X, Hollinger, Livent and now bankrupt Nortel hardly give investors confidence in the regulatory enforcement process. The $32 billion non-bank ABCP debacle certainly shook investor confidence further with the modest fines imposed. It is therefore essential that the OSC conduct a complete enforcement process re-engineering and staffing analysis to ensure that justice is effectively applied in a timely, effective way. We would like to see publicly disclosed specific action plans and metrics that will turn broad investor protection goals into measurable reality ["***What gets measured gets Done"***-Jack Welch, former GE CEO]. Additionally, there should be more oversight of the IIROC and MFDA as SRO's. In particular, the MFDA's governance regime should be thoroughly assessed as there appears to be an ever increasing number of issues raised by member firms and investors.

Investors want to see that justice is done and that white-collar crime is considered a serious form of financial assault. One research report suggested for instance that the Bre-X debacle was responsible for at least a half-dozen suicides by investors who were victims of the estimated $9 billion fraud. Beyond money, industry wrongdoing affects many aspects of people's lives including stress, marriage and health. We therefore recommend that the priorities include some initiatives in this regard.

4. **Penalties:** The penalties imposed on offenders are regarded as nothing more than wrist slaps. The penalties contained in settlement agreements often pale in significance to the gains made by those involved in wrongdoing. In fact, many of the fines imposed on individuals are not paid since registrants leave the industry or declare personal bankruptcy. We suggest that fines be increased and punitive damages be added to the tool kit. More wrongdoers simply have to end up in jail and not just the small fry. Further, investors are very interested in **investor restitution** not just wrist slaps or small fines imposed on registrants. The well attended 2005 Investor Town Hall event made this abundantly clear. Inexplicably, there was never a second meeting.

As an aside, we are increasingly concerned about the processes used, mitigation criteria employed and fairness of investor restitution decisions reached by industry complaint resolvers including industry-sponsored and funded OBSI. Para 26 of OBSI's new Terms of Reference (ToR) is particularly troubling. We recommend that the OSC or CSA review this weak link in the investor protection chain. Specifically, the governing OBSI Framework should be re-assessed and the ToR reviewed for congruency.

5. Engaging the Public: We believe that to better engage the investing public. We recommend that the OSC *pro-actively* seek out individual retail investors to participate in all OSC panels, studies and focus groups. Investors/ advocates should be given the same access as industry participants. The OSC's roles and responsibilities are not understood

by the public and there is a strong belief that policies and regulations are unduly influenced by industry participants. We respectfully refer the OSC to ***Canada Steps Up***, a comprehensive research report by the Task Force to Modernize Securities Legislation in Canada http://www.tfmsl.ca/ Volume 6 contains an especially relevant paper by Prof. Julia Black***, Involving Consumers in Securities legislation in Canada.***

As FAIR recommended in its submission on February 23, 2009 to the Ontario Standing Committee on Government Agencies **(**SCOGA) , we too strongly urge the OSC to appoint a Commissioner with a strong retail investor perspective.

The OSC Web-site should be overhauled to make it more investor- friendly and useful. More topics on education and awareness, investor research and Case studies should be added. The site design should be enhanced to provide better navigatability and search capability for the retail investor. Updates of various committee proceedings should be added. For instance, we never heard a peep from the Investor Advisory Committee, which has unfortunately been abandoned.

Companies and individuals who have been sanctioned/disciplined should be listed in an on-line alphabetized central registry on the OSC site (or a link) that contains their transgression and the penalties imposed to readily enable small retail investors to carry out due diligence or support disputes and claims. An email ALERT system such as that employed by the Australian Securities Commission [“FIDO”] can be used to economically reach subscribing investors, consumer organizations and advocates regarding timely topics of import and concern to small investors.

The OSC Stakeholder Survey should be reconfigured to provide more polling of retail investors on a broader range of topics. We believe the results will be illuminating and helpful.

In the money market mutual fund probe resulting from the credit crisis, details were not revealed. In fact, we had to request information under Freedom of Information. The OSC must be more transparent if it is to achieve any level of retail investor trust and credibility.

We also strongly recommend that the OSC schedule an Investor Town Hall meeting no less frequently than every 18 months. Since there has not been such a meeting in 5 years, one should be planned for 2010/2011 with supporting budgetary funds.

6. **New investment products** such as Structured products and SPAC’s need to be better regulated and their distribution channels better understood. Despite our strong recommendation to limit the sale of risky CFD’s to retail investors, the OSC authorized their sale. We never received a rebuttal to our arguments. On October 8, 2009, the Commission granted relief to CMC Markets UK Plc and CMC Markets Canada Inc. (together, CMC Markets) that now permits CMC Markets to distribute "contracts for difference" (CFDs) and foreign exchange contracts (forex) to Ontario investors without the necessity of a prospectus filing..See Australian Securities Commission take on

CFD's.
http://www.fido.gov.au/fido/fido.nsf/byheadline/Contracts+for+difference%3A+complex+and+high+risk%3F?openDocument **"CFDs are like borrowing to gamble``**
Accordingly, we recommend that the OSC take targeted pre-emptive action to prevent a meltdown due to this controversial product .More importantly, we recommend the OSC heed the advice of investor advocates when permitting the unleashing of risky products on the retail market.

It seems to investors that the regulatory process is so slow it is unable to anticipate even the obvious problems and abuses such new products will cause for retail investors. A case in point are the 2X leveraged ETF's which led to a lot of unnecessary grief for Main Street .These too had come with warnings from advocates .Why was regulatory action so slow and muted? In essence, little corrective action was implemented. Something isn't working right. It should be a priority to find out how to correct this protection deficiency.

7. The **OSC must become more anticipatory and less reactive.** New systems must be put in place to monitor and detect problems before they occur. While it is comforting to know that the OSC may impose fines on offenders for breaking securities laws it doesn't help the retail investor that has lost his/her life's savings. An ounce of prevention is indeed worth a pound of cure. One chronic problem –non-standard, misleading NAAF forms within the industry .If the KYC process were re-engineered a large number of complaints could be avoided. We recommend this be a specific 2010/2011 objective.

8. Influence a change in the Limitations Act We would add a goal that the OSC convince the Ontario AG that the 2 year period in the Limitations Act is oppressive, unworkable and re-baseline it at 6 years as before. This is a MAJOR investor protection priority with small investors, seniors and retirees. Some Industry participants are exploiting this shortened statute of limitations period to ensure the limitation clock runs out before complaints are resolved.

9. Regulatory exemptions cause us considerable concern. These are generally not reviewed by the retail investor community, the very population that is most affected by the exemption. In most cases we find that the exemptions effectively nullify sound protective measures that investors inappropriately believe are in place. We recommend an overhaul of the approach so that original protective rules are not clandestinely removed via opaque exemptions.

SUMMARY and CONCLUSION

By any measure, 2009 was not a good year for the OSC or investor protection. SIPA has painted a grim picture of Investor Protection in Canada .The financial devastation of 2008-09 is reviewed in detail in this Special Report on Investor Protection It lays out comprehensively the major disasters that befell Canadian small investors during the year. It is an update of SIPA's prior Five Year Review issued in 2004. This latest report shows that little has changed for small investors over the last five years, and regulators are still failing to provide adequate investor protection.

The investor has to know that someone is working to keep the playing field level - that 'someone' has to be the OSC. Investor protection really has to become **"Job One"** for securities regulators.

The enhanced use of TIP lines, financial incentives for truth tellers (whistleblowers), systematic information sharing and scheduled, formal meetings with the FSCO/IIROC/MFDA/AG /RCMP/OBSI et al could prove effective tools for investor protection. We would like to see the OSC's priorities demonstrate a proactive measured approach to prevent, detect, deter and meaningfully punish those inflicting harm to investors.

Kenmar believe that a comprehensive Human Resource review should be conducted to ensure that OSC resources are adequate and perhaps more importantly, that staffing competencies, experience, diligence and assertiveness are aligned with the many recommendations and improvements articulated here. Without the right people, culture and leadership the OSC is doomed to failure. We encourage the OSC to set investor protection goals for each staffer and provide attractive incentives for accomplishment and disincentives for failure.

We cannot comment on the OSC budget but we can say we are concerned that even with fee increases (but with a 23% increase in expenses), the OSC expect to operate at a deficit for each of the next three years- operating costs will exceed revenues by a whopping $25.4 million. Perhaps it may not be inappropriate to initiate an operational effectiveness review, benchmarking and a compensation study to assess where the problems lie. Applying accumulated surpluses to cover the shortfall will only mask a deeper issue and inevitably adversely impact investor protection.

We would like to take this opportunity to recognize the Getsmarteraboutmoney.ca website initiative and the OSC Inquiries Service. These are functioning well and merit nurturing and increased stable funding. The education site should be more effectively marketed. so there is greater awareness. We'd also like to see more timely Investor Bulletins, "push" ALERTS and investor protection Checklists e.g. one for SPAC's.

We agree to public posting of this Comment Letter.

We would be pleased to discuss our comments and recommendations with you in more detail at your convenience.

Respectfully,

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