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Dedicated to Investor Protection

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Comments on OSC Notice 11 -765 Priorities for fiscal year ending March 31, 2012

Kenmar welcomes the opportunity to comment on the PROPOSED Statement of Priorities (SOP) . Kenmar is an Ontario- based privately-funded organization focused on investment fund investor education via on-line papers hosted at www.canadianfundwatch.com.

Kenmar also publishes *the Fund OBSERVER* on a bi-weekly basis discussing investor protection issues primarily for investment fund investors. An affiliate, Kenmar Portfolio Analytics, assists, on a no-charge basis, abused investors and/or their counsel in filing investor complaints and restitution claims.

In our view, the *primary* purpose of securities regulations and regulators is to protect retail 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 OSC priorities. There should be more oversight of the IIROC and MFDA as SRO's.

A disconnect between the SROs priorities for example, with the OSC's priorities, would significantly de-optimize the whole process. Specifically, we urge the OSC to examine current SRO CRM proposals, attempts to tighten up the definition(s) of suitability and a controversial and risky scheme to permit adviser incorporation. FYI , SIPA's CRM submission (to IIROC) is posted at: <http://www.sipa.ca/library/Documents/600-SIPA-CRMsubtoIIROC-20110228.pdf> – it illustrates some of the key issues that the OSC should examine. These include, but are not limited to, financial pornography, the lack of personal rate of return information , limited adviser disclosure at account opening and the abusive use of title inflation. We note that these same issues recur every year suggesting that the OSC continues to put them on the bottom of the priority list. Hopefully, with a new Chairman in place, the 2011-2012 fiscal year ,will be the year the needs of Main Street will finally be addressed.

Recent high profile scandals such as non-bank ABCP , Steven Michael Chesnowitz , “advisor” abuse and numerous Ponzi schemes,online scams/frauds, growing retail investor unrest and changing demographics (seniors, pensioners and retirees) suggest that investor protection demands HIGH priority attention .Continued deferral is not a responsible option. Billions of dollars are being needlessly lost each year. Surprisingly, there does not appear to be any statistics published by the OSC regarding the dollar losses incurred by Ontario retail investors . 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 dangerous environment, the OSC must modify its priorities to laser focus on specific retail investor issues.

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 more evident in the list of 2011/2012 priorities that address the issue.

With the evolution of the investment markets, a multitude of complex structured products and the volatility in today's markets, investor risks are much greater than ever before. The 2008 financial crisis is an indicator that should not be ignored. Investor losses have reached epidemic proportions in the last 5 years with horrific consequences to individuals and the Canadian social system. Abuse of the elderly in particular continues to emerge as a serious issue. We strongly recommend the establishment of a Branch dedicated to seniors issues such has been implemented at the SEC and elsewhere.

For the 2011/2012 priorities, we note that the Commission has identified five strategic goals to achieve but no specific metrics or milestones are provided. It is definitive actions that will speak louder than flowery words ["strive", "focus", "monitor" are a little lame] .We refer the OSC to the National Quality Institute www.nqi.ca for processes to enable improvements and a path to excellence. [Disclosure – I am a Board of Governors member]

We would like to enumerate some additional recommendations regarding investor protection priorities for the year ahead:

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 adequate funding for research. It should not be restricted to commenting on OSC proposals. This revised IAP 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 improve the current Panel's limited mandate without undue delay ensuring that adequate funds are provided for in this year's operating budget .Dr. P. Reeve has articulated the areas for improvement – these can be found at <http://files.me.com/pjreeve/w55ab5>

2. Investment funds governance: Fund governance has been a critical investor issue since at least 1995 with the issuance of the Stromberg reports. The Norshield, Portus and the Norbourg meltdowns highlighted once again the need for independent fund governance boards and the maintenance of robust regulatory provisions and prohibitions. We are also 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 and the commission-based model of “advisor” compensation . We recommend the OSC move away from the transaction model and pursue a fiduciary regime for advisors without undue delay. This is well underway in the UK, US , Australia and in other jurisdictions.

We believe the mutual fund 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 has submitted a comprehensive critique explaining why the risk measure and lack of benchmark info. adds to investor risk. We respectfully request that the OSC reassess, on a priority basis, the efficacy of Fund Facts Point of Sale disclosure.

3. Enforcement:A review of the OSC 2010 Enforcement Report suggests there are significant issues with illegal distributions and enforcement (just \$12 million in penalties and settlements and only 2 short jail terms for proceedings launched by the OSC). The small penalty handed out to BMO Nesbitt Burns for their leading role in the FMF fiasco is also disturbing .FMF was just one of several business income trusts that forensic accountant Al Rosen had warned regulators were loaded with defective accounting, misleading disclosure and false advertising .Regrettably, his wise words were not heeded. We are therefore surprised that there is so little focus on specific vigorous and active retail investor protection , improved investor engagement action plans and tougher penalties .

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 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. Were it not for the courageous leadership of investor Brian Hunter aided by heroes, the investors would not have been compensated. Regulators stood on the sidelines as small investors fought pitched battles with the banks and securities dealers. This deficiency was identified by the Standing Committee on Government Agencies as a deficiency of the OSC .The Committee's Report noted *"In this respect, we have some concern that the Commission may have adopted a narrow interpretation of its public-interest jurisdiction in responding to the ABCP crisis. "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 for each listed priority that will turn broad investor protection goals into measurable reality [***What gets measured gets Done***”-Jack Welch, former GE CEO].*

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 definitive and auditable initiatives regarding more robust enforcement.

4. Penalties and Restitution: 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. Moreover, dealers should be held accountable for any unpaid fines by individuals – this rule change would result in an immediate change in dealer behaviour. According to the SRO's somewhere between 80 and 90 % of fines are never collected. Further, investors are very interested in **investor restitution** not just wrist slaps or small fines imposed on registrants. The Commission has to utilize its existing powers to order fines, disgorgement and compensation and apply them for the benefit of Main Street or if inadequate, pro-actively promote legislative changes. The status quo is just not working – the published SOP does not, but should, address this long standing issue.

5. OBSI: The governing OBSI Framework should be re-assessed and the ToR reviewed for congruency and adequacy. It appears as if this Framework Agreement has no OSC or CSA ownership. We therefore recommend that a individual be assigned and named to provide this oversight and liaison. OBSI is a public service entity that merits regulatory oversight.

6. 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.***

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.

OSC registration search information should be added to the CSA website to provide one stop shopping for retail investors (Ontario is the only province not in that search database). 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 reconstituted to provide more polling of retail investors on a broader range of topics. We believe the results will be illuminating and helpful.

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 since 2005, one should be planned for Spring 2011/2012 with supporting budgetary funds allocated.

7. **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 generally, we recommend the OSC heed the advice of investor advocates when permitting the unleashing of risky products onto the retail market.

It seems to investors that the regulatory process is so unresponsive 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 OSC priority to find out how to correct this protection deficiency.

8. 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 2011/2012 priority.

9. Promote a change in the Ontario Limitations Act We urge the addition of a priority goal that the OSC convince the Ontario AG that the 2 year period in the Limitations Act is oppressive, unworkable, not in the public interest and re-baseline it at 6 years as before. This is a MAJOR investor protection priority with small investors, seniors and retirees. The OSC is no doubt aware that some Industry participants are exploiting this shortened statute of limitations period to ensure the limitation clock runs out before complaints are resolved.

10. 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 wrongly 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 most measures, 2011 was not a good year for the OSC or investor protection. Our 2010 Investor Protection Report highlighted numerous breakdowns and missed opportunities to protect retail investors. The recent FAIR report on Financial Scandals lays out comprehensively the major disasters that have befallen Canadian retail investors and makes specific recommendations. These recommendations do not appear to be addressed in the OSC priority listing for the coming fiscal year.

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 IMET/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 retail investors.

Adequate resources are required to operationalize the priorities. We note however that an amended fee rule had to be approved by the Minister of Finance on April 5, 2010. We are concerned that even with fee increases, the OSC expects to operate at a deficit in each of the next three years. These deficits are expected to largely eliminate the OSC's accumulated surplus. The OSC expects a revenue shortfall of \$22 million in 2011. The OSC's plan is not to return to full cost recovery until 2013. We are clearly concerned when we read in the 2010 Annual Report "The OSC's fiscal approach recognizes the circumstances faced by market participants". We are not aware of what these circumstances are or why they are relevant to protecting Ontarions under the Securities Act. If it is true that "*The interests of investors are at the core of everything that the OSC does* ", resources need to be increased, not restrained. Applying accumulated surpluses to cover the shortfall will only mask deeper issues, colour staff motivation, delay improvements and inevitably, adversely impact the retirement savings and lives of retail investors .

Given the extra resources needed to deal with IFRS implementation, a National regulator, the planned LSE acquisition of the TMX, IT/flash trade challenges and other unavoidable tasks, we believe that the OSC resources need to be vastly increased if retail investor protection is not to be compromised. 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 and diligence are aligned with the recommendations and improvements articulated here. Without the right people, culture, allocation of resources and leadership the OSC will not achieve its objectives. We encourage the OSC to set investor protection goals for each staff person and provide meaningful incentives for accomplishment and disincentives for failure.

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 the Commission. The priorities announced will not, in our opinion, be sufficient. A significant rework is required before they receive Ministerial approval.

We would like to take this opportunity to recognize www.Getsmarteraboutmoney.ca website initiative and the OSC Inquiries Service. These are functioning well and merit nurturing and increased stable funding. We note parenthetically that in a report by Carleton University professor Saul Schwartz published in December by the Institute for Research in Public Policy: *Can Financial Education Improve Financial Literacy and Retirement Planning?* the conclusion was that rather than raising financial literacy, "governments should seek to better protect consumers of financial products and services." Accordingly, we believe, OSC staff should focus on investor protection and leave financial literacy and investor education to the Investor Education Fund, FCAC and others.

The current fiscal year should be the year that the OSC makes it clear, through concrete actions, that investor protection is top of mind.

Kenmar 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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