Aug. 19/04
2:50pm

EXHIBIT No. 1/06/029
FILED ON Aug. 19/04

Presentation To Ontario Legislative Assembly Standing Committee On Finance And Economic Affairs

By John Hollander, B.A., L.L.B.

Table of Contents

Executive Summary 2
Background and Clientele 2
Nature of Suitability Claims 3
  Setting Risk Tolerance - the Benchmark 3
  Solicited Trades 3
  Unsolicited Trades 4
  Deviation from KYC Profile 4
  Summary of Claims 5
Dealing with IDA and OBSI 5
Recommendations 6
Summary of Presentation 6

DOUCET McBRIDE LLP
Lawyers/Avocat(e)s
81 Metcalfe Street, 6th Floor
Ottawa, Ontario
K1P 6K7

John A. Hollander (LSUC 18174E1A)
Tel: (613) 233-4474
Fax: (613) 233-8868
www.stockloss.ca

Executive Summary

The purpose of my presentation is to address a major failing in the regulatory scheme as it affects relations between the securities industry and the public and to propose solutions to that problem.

The interface between capital markets and the private investor is the financial adviser. Financial advisers are not required to obtain much in the way of formal training, and nothing with respect to portfolio management. If the industry decides that poorly trained sales staff are to be allowed the freedom of advising private investors, the industry should pay the losses where the advice provided is unsuitable for those investors. This should be a cost of doing business by reason of their failure to invest in proper training and supervision. It appears that loss prevention and compensation are alternative strategies.

Unlike the medical Royal Colleges and my own Law Society, the IDA and MFDA are not statutory authorities, but are industry groups that deal with their members. Where a private investor contacts the IDA or MFDA to complain of losses arising from unsuitable advice, both impartiality and expertise are assumed. Unfortunately, both those assumptions are unfounded and lead to the abandonment of valid claims.

Background and Clientele

To establish my credentials and my apparent bias, let me introduce myself. I am a trial lawyer with 26 years of practice as a civil litigator. I currently practice with a mid-size Ottawa law firm, Doucet McBride, and represent several clients with claims against investment and mutual funds dealers for allegedly unsuitable portfolio advice. I maintain a website devoted to this area of my practice, www.stockloss.ca, and have been the subject of several articles in the Globe & Mail, the National Post, the Ottawa Citizen and the Law Times (a law profession trade paper). I have flown here from Ottawa to make this presentation.

I either currently represent or have already settled claims for 33 distinct clients (counting the claims of a family as being a single client). I have ongoing investigations concerning several other potential clients. I accept as clients approximately one third of people who approach me for an opinion. Most of my clients have retainer agreements by which I am compensated only in the event of success of the claim, and I can confirm that few would hire me on a traditional hourly rate basis.

While it is difficult to provide a precise profile of my clients and their claims, I can provide the following statistics:

- The average amount of capital lost by each distinct client is approximately $175,000.
- The average age of the clients is at or near retirement.

- Approximately half of the claims are directed against the brokerage arms of chartered banks. The balance is directed approximately equally against other brokerage firms and mutual funds dealers.

Nature of Suitability Claims

The nature of the claims varies, of course, but there are certain trends that can be seen from the 33 distinct claims I have undertaken.

Setting Risk Tolerance - the Benchmark

In almost all my cases, the clients have said that the adviser did not provide any advice with respect to the investment goals and risk tolerance that ought to apply. In many cases, expert witnesses have said that the clients' actual risk tolerance was far less than indicated in the account application forms, or KYC's (for "Know Your Client"). Accurate KYC information is required by both the IDA and the MFDA, as the OSC's regulation 31-505 obliges registrants to conduct reasonable investigations to ascertain the general investment needs and objectives of the client, and the suitability of proposed transactions. The courts have ruled that financial advisers owe their clients the duty to give advice with respect to appropriate investment goals and risk tolerance.

Does it make sense for the patient to tell the doctor the diagnosis so that the doctor can prescribe appropriate treatment? The patient provides the facts, either in discussion or through test results, and the doctor diagnoses and prescribes treatment. While the patient gives instructions, it remains the professional duty of the doctor to apply scientific knowledge to the facts of the case. So, too, is it the obligation of the broker to learn the client's history and retirement or other goals so as to enable the broker to provide advice on the client's appropriate investment goals and risk tolerance. If a client wants to retire rich, but cannot save enough to reach that goal, then the adviser should tell the client this. If an existing investment strategy puts accomplishment of attainable goals at risk, then the adviser should state this as well.

Solicited Trades

After setting the goals and risk tolerance, the investment adviser moves to portfolio recommendations. The adviser is presented with a portfolio of securities (either transferred from another firm or newly invested money). The adviser should recommend steps to align the portfolio with the goals and risk tolerance so, for example, a working investor nearing retirement can draw the retirement income likely required. What I see routinely in my cases is that advisers recommend their clients buy individual stocks, or groups of stocks in mutual funds dedicated to a sector (for example technology or healthcare) which investments the clients cannot understand and the adviser does not explain. Are these recommendations suitable for the client? Both the Canadian Securities Institute's "Conduct and Practices Handbook" and the courts' case law mandate that the adviser provide suitable advice and provide the client with the cons as well as the pros of

the investment decision. Risk of loss in individual stocks or sectors, high volatility, concentration of securities, high management fees, are all factors that should be discussed, but my clients routinely deny their advisers have done so.

My clients also report that their advisers hold themselves out to be financial advisers of a general skill level, when their training is clearly restricted to selling securities either to or for clients without regard to the significance on the portfolio as a whole. When I question the advisers in the court process, they maintain that they are in fact knowledgeable about portfolio management, but cannot point to any training that gives them such expertise beyond the experience of being "in the market". Doctors, accountants, lawyers, engineers, and architects undergo many years of educational training followed by mandatory apprentice programs. Financial advisers, on the other hand, can take the Canadian Securities Course or the mutual funds equivalent in a few weeks of home study, and then take on clients with 6 and 7 figure portfolios with little else but their sales skill. Is it any wonder we hear of abuses in the realm of financial advice? This lack of training does not contravene any regulatory requirement, but leads to huge unstated risk to private investors.

Unsolicited Trades

Frequently a client already has a security, or wants to procure a security, that is outside the client's objectives and risk tolerance. The recent examples of Nortel and JDS, and the 1990's Bre-X, were preceded by their equivalents in every bear market to date. There is nothing new about "irrational exuberance", words taken from Alan Greenspan during the technology bubble of 1999. If the client requests that the adviser buy a specific stock or fund, then the Handbook requires the adviser to provide "appropriate cautionary advice". Again, my clients routinely deny that their advisers have done so.

Deviation from KYC Profile

In some cases, the investments recommended by the broker deviated from the risk profile set out in the KYC. If a profile specifies "medium risk", what does that mean? Financial advisers receive no training in portfolio management or in matching investments to the KYC profile, and the brokerage firms have no guiding rules to define the relevant terms. Therefore, there is no applicable benchmark against which to apply the test for a specific trade. Could it be that buying all Nortel stock can be medium risk in one case, high risk in another. If Nortel trades at $120, or at $5.00, should this determine how much risk is in the trade? If the portfolio consists only of the securities of many technology firms, or of a mutual fund that does so, is that medium risk?

My clients routinely report that the trades in their portfolios were offside the recorded KYC profile, and really offside from what their KYC profile ought to have been. Also, they report that their advisers failed to recommend adjustments to their portfolios to take the massive gains or losses in their portfolios by reason of market changes.

Summary of Claims

As can be seen, my clients claim they suffered losses because their portfolios acquired and held investments that the clients feel were unsuitable for them. The unsuitability arose from alleged misdiagnosis of their needs, and poor investment advice. My clients do not claim any criminal or unethical malfeasance, and do not seek to have the advisers lose their licence or their ability to earn a living in their chosen field of endeavour.

Dealing with IDA and OBSI

The manner in which my clients (and by extension, all claimants) have been dealt by the system is the real focus of my presentation today. Approximately half of my clients have submitted claims to either the IDA or to the Ombudsman for Banking Services and Investments (the OBSI), or both. The MFDA has not been involved to date in my cases, as it was created after the subject of my clients' claims arose. I have no reason to believe my position would be different with respect to their involvement.

In virtually all cases, the IDA or the OBSI has repeated the response from the brokerage firm, taking the financial adviser's word and position as being gospel truth. They freely express opinions that clear the financial advisers of any liability, without considering the alternative.

In doing so, the IDA appears to be expert and impartial when in fact it is neither. The IDA and OBSI routinely provide legal advice with substantial consequences to the investor and without accountability to the investor for the accuracy of the advice given. They tell the clients that there is no validity to the claim. The IDA fails to identify its bias or its lack of expertise in assessing the merit legal claims, and fails to recommend that the investor seek independent and expert advice to determine the validity of the claim. It would appear that the IDA sees as its mandate the rejection of claims to reduce the liabilities of its members at the expense of the public. In the John Grisham novel and the movie made of it, "The Rainmaker", the disability insurer had a claims manual with Tab W, instructing adjusters to reject all claims. It appears that this Tab has found its way into the manuals of the IDA.

This process concerns me for 3 reasons:

- First, many of the clients who have retained me have expressed their concern that my opinion differs from that of the IDA or OBSI. The clients retain a respect for these institutions on the basis that they appear to be independent and mandated to represent the interests of the clients. I expect that many people who raise their concerns to the IDA, MFDA and OBSI accept the denial of liability from these apparently impartial arbiters, without further enquiry. I therefore expect that many valid claims are therefore abandoned, which is the real reason for the positions taken by the IDA and the OBSI. In other words, these organizations are in fact serving the needs of their

constituencies, the securities dealers and banks, at the expense of the public. Trade organizations should not be cloaked with the apparent authority arising from OSC delegation of powers, in dealing with the public.

- Second, as a professional, I am jealous of others entering my field without training. The IDA and OBSI provide legal advice, with neither the safeguards nor the accountability that apply to my profession. They tell clients that their claims are illfounded. My settlements and experts prove these opinions were wrong. Simply out, the IDA and OBSI are practicing law without a licence.

- Third, the process of submitting the claim for review by the IDA or OBSI takes so long that, with new limitations legislation (2 years from the date that the client knows the extent of the loss and the reason for it), the clients may well face a statute-barred claim if this practice continues.

Recommendations

1. Clarify the roles of industry organizations. Are they lobbyists, or are they statutory bodies (like the Colleges in medical professions or the Law Society in my own)? In both cases, they should be restricted to dealing with their members and with the regulator, and prevented from issuing opinions to the public with the aura of independent authority.

2. Raise the standards to qualify as a registrant.

3. Where the IDA, MFDA or OBSI deals with claims from private investors, they should state in clear language that they represent the industry and not the public or the Ontario government and that their opinion is not one cloaked with legal authority. Further they should recommend that the claimant seek expert advice from someone not beholden to the industry.

Summary of Presentation

- The IDA and MFDA are not regulated.

- These organizations appear to be impartial and expert, when they are not.

- They provide legal opinions that are ill-founded without any accountability or safeguards for the clients.

- The low minimum standards to qualify for registration as a financial adviser suggest that the industry has chosen not to invest in loss prevention.

- The IDA and MFDA, supported by the OBSI, are the instruments of their industry in encouraging investors with valid claims to abandon these claims, to reduce the cost to the dealers.