NOVEMBER 8, 2012 ISSUE

OBSI UPDATE – NOVEMBER 8, 2012

This note is one in a series of newsletters updating you on what's happening at the Ombudsman for Banking Services and Investments (OBSI).

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1. Firm Refusals to Compensate

Firm Refusals to Compensate

Since our organization's inception in 1996, only one firm has ever refused an OBSI recommendation to compensate a client regarding a complaint we investigated. Now, after a lengthy process aimed at trying to fairly resolve certain cases, we expect to be announcing several refusals by investment firms in the coming weeks and months.

A firm's refusal to compensate means that OBSI must publicize the refusal as well as our investigation's findings under the so-called 'name and shame' requirements of Section 27 of our Terms of Reference. It is the principal tool that OBSI has to incent firm cooperation, but it was never meant to be used. Some have likened it to a nuclear deterrent.

The cases in question have been stuck at an impasse for a long time, which is unfortunate. While we were in a position to have publicized the details some time ago, if OBSI announces a refusal to compensate it is the end of our process. It means that someone, a client of an investment firm or bank, will not receive the compensation they are fairly owed based on the facts of the case.

Recognizing this, we have taken some extraordinary steps in an effort to break through the logjam (we outline some of these steps below.) Our only interest is in finding fair resolutions to these "stuck complaints".

In many cases, OBSI's efforts succeeded. Although the complaints dragged on, in the end some firms agreed to settlements and their customers were satisfied that their complaints were resolved fairly.

In other cases, however, firms simply have not agreed to compensate their customers for the firm's own mistakes, liabilities and compliance deficiencies. Having exhausted all avenues to settle these complaints, OBSI is now preparing to publicize the refusals.

We remain hopeful that the cases will yet resolve before we announce them as refusals to compensate. The reality is that the overwhelming majority of complaints brought to OBSI are resolved in a manner we believe is fair: fully 99.8% since our organization's inception. Unfortunately, the coming period will likely focus significant attention on those cases that could not be resolved, as well as the firms involved.

BACKGROUND

As noted above, OBSI has taken some extraordinary steps to resolve the cases stuck at an impasse. These steps include:

- Consultation on OBSI's methodology
- Expert assessment
- Independent review of the case files
- Escalation within the firm

Consultation on OBSI's methodology: OBSI undertook a comprehensive consultation on our investment suitability and loss assessment methodology. We did this in part because the majority of investment complaints that we investigate each year revolve around questions of investment suitability and there had been criticism of our approach from certain securities firms. While firms may agree with all or part of OBSI's process, when there is not agreement it can lead to significant delays in resolving client complaints. This was an issue in the overwhelming majority of the stuck cases.

While these consultations were ongoing, we felt it would be unfair to the firms if we published their refusals. The process we had followed in their case, as well as the method used to calculate compensation owed to the investor, had the potential to be modified in a material way as a result of the consultations.

Now, that consultation process has concluded with a series of enhancements having been made to OBSI's investment suitability and loss assessment methodology.

Expert assessment: As part of its Framework for Collaboration with financial market regulators, OBSI must submit itself to knowledgeable, independent third party evaluations on a regular basis. The Navigator Company of Australia, which reviewed OBSI in 2007, was engaged by OBSI's Board of Directors, with the agreement of financial regulators, to review OBSI once again in 2011. Navigator has extensive experience in this field, having reviewed eight different financial dispute resolution schemes around the world – several of them multiple times – as well as having conducted similar reviews of several non-financial dispute resolution schemes.

Industry participants met with the reviewer to outline their concerns with OBSI. The reviewer specifically asked firms that voiced concerns about OBSI to submit actual complaint files, including OBSI correspondence and findings, for review in order to validate their concerns. Only a few firms took up this offer. The reviewer also looked at dozens of files chosen randomly from OBSI's case inventory.

The case file review found that OBSI's methods and conclusions were fair, rigorous, appropriate and consistent across files.

OBSI's Board of Directors also specifically tasked the independent reviewer with conducting a detailed examination of the investment suitability and loss assessment methodology as part of the larger report. The reviewer found that in many respects OBSI 's methodology is the gold-standard amongst its international peers in terms of the fairness and precision of the loss calculation.

Independent review process: At the end of October 2011 OBSI received a letter from the Canadian Securities Administrators (CSA), the Investment Industry Regulatory Organization of Canada (IIROC), and the Mutual Fund Dealers Association of Canada (MFDA) concerning the resolution of twenty-one complaints considered to be stuck at impasse as of the date of the letter (several have since been resolved).

At the direction of the regulators, OBSI identified a one-time method of independent review of these cases with a view to bringing them to a resolution. Firms were offered the opportunity to have credible and experienced former commissioners of the Ontario Securities Commission (OSC) provide an independent assessment of the files in question, at the firms' expense, based on standards consistent with OBSI's Terms of Reference. If OBSI had unfairly considered the facts of the case or our investigation findings were objectively flawed, the reviewer would say so in his or her report on the matter. As of today only one firm has taken up this offer and the review is ongoing.

Escalation within the firm: We recognize that sometimes senior management at a firm is unaware of the complaints about their firm that are in OBSI's office and at an impasse, even when involving large dollar amounts. On occasion, it is not until we have been about to go public with a refusal to compensate that the firm changed its mind.

It is OBSI's goal to allow firms plenty of time to resolve cases at the appropriate level before we announce a refusal. OBSI's escalation process is as follows:

1. Following OBSI's investigation, a draft recommendation is provided to the participating firm laying out OBSI's findings and providing the basis for that recommendation. The participating firm and the complainant are provided with 30 days to comment on the draft recommendation. Any comments received are considered and factored into the final recommendation.
2. Once a final recommendation is issued to a participating firm, OBSI will follow-up with the designated contact person at the firm to obtain the participating firm's decision to accept or reject the recommendation.
3. If the recommendation has been refused, the Ombudsman will contact a senior executive of the firm (often the CEO) to inform them of the refusal, the implications of it, and the next steps to be taken. The senior executive is encouraged to contact the Ombudsman to discuss the refusal. At this point, OBSI is free to discuss the matter publicly.
4. OBSI's Board of Directors is informed of the refusal and the facts of the case, including the name of the firm.
5. The appropriate regulators are informed of the refusal and the name of the firm.
6. The firm is provided with three hours notice before a news release announcing the refusal is published.