Kenmar Associates
The Voice of the Retail Investor

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Ombudsman for Banking Services and Investments
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Kenmar Associates Response to Request for Comments

Consultation on Overhaul of Terms of Reference
http://www.obsi.ca/images/Documents/Consultations/TOR_13/tors_final_blackline_en.pdf

Kenmar Associates is pleased to submit comments in response to the request for Comments. By way of introduction, Kenmar Associates is an Ontario- based not-for-profit organization focused on retail investor education and protection via on-line research papers hosted at www.canadianfundwatch.com.Kenmar also publishes *the Fund OBSERVER* on a bi-monthly basis discussing investor protection issues primarily for retail investors. Kenmar routinely submit comments and ALERTS on proposed regulatory changes that could impact Main Street. Kenmar's Intervenor Service assists retail financial consumers with their complaints.

Although we are providing comments, we urge the OBSI board to delay the Consultation at least as far as making any changes that could impact retail investors. Our reasons are as follows:

- It is premature given a number of parallel related CSA initiatives that are ongoing
- Previous Comments have not been addressed . These include the frequency of complaint statistic reporting , clarification of limitation periods , the role of the Consumer and Investor Advisory Council among others
- OBSI's Consumer and Investor Advisory Council was created to provide the input of consumers and investors into OBSI's governance and operations ,yet there is no indication that the OBSI Consumer Advisory Council has reviewed or agreed with the proposals
- The CSA has not yet implemented an Accountability Framework and oversight protocols over OBSI
- There is simply inadequate time to provide comprehensively researched commentary given that half the time allowed falls smack in the middle of the traditional summer vacation period
- If EMD's ,PM's and Scholarship Plans fall under OBSI, a new set of T of R's will need to be developed for consultation

35
17 OBSI is too critical to investor protection for such material changes to be rushed. The dispute resolution service reports that it opened 446 investment-related cases in 2012, up from 405 cases in 2011 .

EXECUTIVE SUMMARY

Overall, the proposals are regressive and anti-investor. The proposal to no longer report on systemic issues removes one of the key differentiating strengths of OBSI. The OBSI proposals further fragment the regulation of financial products into the old product silos rather than recognize that these silos long ago broke down despite continuing to be regulated separately. The one Comment letter already posted from Doucette McBride suggests the proposals are material and merit more comprehensive debate than afforded by a Comment process. We agree and recommend face to face discussions with all stakeholders before these radical changes are made. As they stand they would degrade the value of OBSI and not be in the Public interest .

DETAILED COMMENTARY

Here are our comments:

1. The consultation indicates that OBSI is proposing to give up its ability to investigate serious "systemic issues", a critical feature it proudly promoted a few years ago.[A **systemic issue** is defined as an issue that will have an effect on people beyond the parties to a dispute. By dealing effectively with systemic issues and serious misconduct, OBSI can raise industry standards and help consumers to obtain fair compensation for financial losses.] This change in direction comes at a time when a recent Mutual Fund Dealers Association Bulletin http://www.mfda.ca/regulation/bulletins13/Bulletin0563-C.pdf sets out the SRO's regulatory priorities based on what it sees in the marketplace. These include excessive leveraging, blank signed forms, document adulteration, misleading marketing materials and seniors issues, particularly suitability. The 2011-2012 IIROC Annual Report comments that the issue of unsuitable trade recommendations "is a persistent and significant problem in the Canadian investment industry". The 2012 OBSI Annual report indicates that unsuitable investments and advice continue to be the biggest source of investment industry complaints. Systemic issues, like suitability and non-bank ABCP , have adversely impacted retail investors in the past and we see no reason to believe they will not do so in the future. By highlighting systemic issues OBSI can also function as a early warning system.

OBSI's complaint database can be used to identify systemic issues at the national , regional or dealer level. OBSI should report on all cases in a anonymous way so that lessons can be learned by the industry and the consumer will have another crucial education source. The database could , if used properly,provide an insight into long-term industry issues. For example , excessive borrowing, toxic securities, undisclosed fees , deficient complaint handling processes etc. It would be a travesty not to make maximum use of this treasure trove of information. An Ombudsman can serve as a

bulwark of financial consumer democracy in troubled times, protecting citizens and helping industry, regulators and government to improve in the face of a tough economy and fiscal constraint. See http://www.gouvernance.ca/publications/09-06.pdf for a review of the Ombudsman as a producer of better governance.

2. The comment that "OBSI's board believes that there should be one policy on systemic issues for the entire organization, and the decision by the Department of Finance has necessitated this policy change" goes against every recommendation by SIPA, FAIR Canada, Kenmar Associates , the OSC Investor Advisory Panel , and PIAC as well as recommendations from a Third party Reviewer. This is exactly the race to the bottom feared by investor advocateswhen Finance allowed Banks to choose their own Dispute Resolution Body. The original intent of establishing a dispute settlement system in 1996 was that complaints would be heard by one body. As such, besides improving access,efficiency and consistency, it would avoid criticism that allowing competing services encourages a "race to the bottom" on standards. In 2011 , the World Bank issued a paper condemning so-called "competition" among Ombud services, identifying the "severe risks to independence and impartiality" this represents. The Consultation is silent on how the proposed changes put OBSI on-side with Canada's international Agreements.

3. Another proposed change includes clarifying that OBSI not investigate any complaint involving insurance products (e.g. Segregated funds), referring these issues to a relatively unknown (to many retail investors) entity ,the Ombudservice for Life and Health Insurance (OLHI) , even if they form a part of a larger portfolio that is the subject of a complaint to OBSI. . In order to look at things fairly the whole portfolio has to be examined to get an understanding of the financial plan/objectives/risk tolerance and to determine if it is suitable or not. It is illogical to just look at select securities in isolation and not evaluate if the parts come together to make a well designed portfolio or a fiasco. When a dealer evaluates a complaint, it considers the whole portfolio including the Seg funds. How can they then be split off into two different streams when a complaint is made to OBSI?

The investment dealer complaint process is confusing and stressful enough without having investors deal with two Ombuds services This is just the kind of move that is 180 degrees away from the goals of a single point of contact for retail financial consumers and consistent practices and is inconsistent with the FAIRNESS STATEMENT. Split access is never in the investor's best interests. The consultation is silent on such products as PPN's and Index -linked GIC's promoted by banks. The insurance Ombuds service publishes reports, etc. but its profile is limited. However, it clearly does not have OBSI's depth of experience with investments so this redirection to the insurance Ombuds service may adversely impact fairness/investor protection and place investors in harm's way. Our limited research on OHLI in the past raised a few issues Re effectiveness, governance , regulatory oversight , depth of reporting and accountability as an Ombudsman service.

4. Another proposal involves the retention of OBSI's $350,000 limit with no commitment

for periodic reviews. The $350,000 limit has been in place since 2002, in effect cutting it by the ravages of inflation. This is particularly important as boomers enter retirement and seniors begin significant annual withdrawals from RIFF accounts. The Board should take this opportunity to address the maximum limit and any special provisions that may be needed to cope with retiree, seniors and pensioner issues .Some issues we have previously identified include assistance with complaints filing, setting investigation priorities , special training for investigators and use of personal visits to gather information.

5. In formalizing its process for "naming and shaming" firms that refuse its recommendations it appears OBSI may be adding even more time ,adding to investor stress and anxiety . It is a question mark whether the Board of Directors should get involved. In any event, the Board of Directors should have a set limited time constraint after which the process should immediately default to Name and Shame. As an aside ,we believe and have stated that Name and Shame is ineffective – that's because clients aren't aware of it, it's a punishment that really can hurt only a small firm because a big dealer isn't going to feel the impact . We have instead recommended, as have FAIR Canada , that OBSI recommendations be binding which is not addressed or discussed in the Consultation. Other alternatives may exist, but dialogue is required.[It is generally well known that some firms--including Royal Bank of Canada's RBC Capital Markets, Toronto-Dominion's TD Waterhouse, and Macquarie Group Ltd--have unsuccessfully sought to be exempt from OBSI participation altogether. On the investment side, the bank-owned investment dealers are the biggest source of new cases, although mutual fund giant Investors Group is number one, with 11% of investment complaints. It's followed by TD with 9%, BMO at 8%, National Bank with 6%, and RBC and Scotia at 5%. CIBC ranks further down in ninth place, with 4% of complaints.] The impasse Re the so-called “stuck cases” is strong evidence of the ineffectiveness of Name and Shame.

6. The proposals also establish that OBSI will continue to report to firms any threats against them that come to light during an investigation, but that it will now be keeping the identity of the OBSI staffer who reported the threat confidential. It says it's making this change because of several incidents over the years in which OBSI staff have reported these sorts of threats to firms, and have then themselves been exposed to threats from the complaining clients who made the initial threats against the firm. We're not sure why this is in the T of R.

7. OBSI is now proposing that it must submit itself to knowledgeable, independent third party evaluations of its operations at least once every five years. This was previously three years. Given the unprecedented turmoil and change facing the dispute resolution system and the possibility of an enlarged mandate, it is a mystery why the OBSI Board would extend the Review interval.

8. As for linking changes to Banking dispute resolution, we disagree with OBSI being harmonized with them. So do the Small Investor Protection Association, FAIR Canada, PIAC, CARP , the Consumers Council of Canada and the National Union of Public and

General Employees. Other groups that oppose this include the Investor Advisory panel of the Ontario Securities Commission , le Mouvement d'éducation et de défense des actionnaires (le MÉDAC) and the Canadian Community Reinvestment Coalition. So why is the OBSI Board now harmonizing with a standard so despised by Consumer groups and previously criticized by senior OBSI management? As an aside ,we note that the banking rules do not include a cap on compensation;if the Board is to be seen as consistent in harmonization, it should remove the $350,00 cap so as to be "harmonized" and consistent .

9. The section *Firm responsibility for actions of their representatives is most appropriate.* This section reinforces the principle that dealers, not their representatives, are responsible for paying complainants the compensation that OBSI recommends. Participating firms are responsible for the actions of their representatives, including dealer Representatives /agents, by virtue of their participating in OBSI's service and the nature of OBSI's jurisdiction. This is entirely consistent with the views of the advocacy community.

10. As regards **Section 14(a): Compensation limit ,** the language should be specific that OBSI does not limit the rights of complainants to pursue claims in other forums for amounts over and above OBSI's $350,000 limit should they so choose.

11. In the past ,OBSI has made reference to ISO 10003 *Quality management — Customer satisfaction — Guidelines for dispute resolution external to organizations*. Is there any reason why the Board is not taking the opportunity to hard wire this standard into the Terms of Reference?

12. We suggest the Board validate that the Code of Conduct is adequate to deal with conflicts-of -interest. OBSI retains law firms for advice and services. Those same law firms represent dealers before the OBSI. This should be deemed a conflict. It is terribly unfair to negotiate with the OBSI when you know that the other side's lawyer has an upper hand because that lawyer and his colleagues work for the OBSI on other matters. We note that Federal Regulations applicable to banking disputes require an approved Dispute Resolution Provider(DRS) to ensure that every person who acts on its behalf in connection with a complaint is impartial and independent of the parties to the complaint.

13. OBSI's Terms of Reference outlines the types of complaints that fall outside of its mandate, including complaints relating to the pricing of financial services by a participating firm and the commercial judgment of a participating firm. Thus the terms of reference clearly indicate what types of complaints OBSI would be unable to consider. We request clarification as to the complaint characteristics that would make OBSI fall outside its mandate (i.e. unwilling to consider a particular complaint). For example, would it be due to a lack of sufficient staff, funding,experience or any other combination of factors? We recommend that OBSI incorporate this information in its Terms of Reference in order

to enhance transparency and ensure consistency of OBSI decisions in this regard.

14. A number of important timelines are missing in the Terms of Reference. Federal/ Financial Consumer Agency of Canada (FCAC) Regulations require an approved DRS provider for banking complaints to resolve complaints by making a final recommendation to the parties within 120 days after the day on which it receives the complaint. This contrasts with OBSI's 80%/180 day target. It is our understanding that this timeline will NOT be harmonized . Regardless, we recommend all timelines be included in the Terms of Reference. Similarly , Federal Regulations applicable to banking disputes require an approved DRS provider to notify a person who has made a complaint within 30 days after the day on which it receives the complaint if all or part of the complaint is outside its terms of reference. We believe all applicable timelines should be revealed and integrated into the Terms of Reference.

15. We recommend that language be added that the Annual Report be publicly disclosed. Further ,Federal Regulations require an approved DRS provider to submit an annual report to the Commissioner of the FCAC on the discharge of its obligations, including a summary of the results of any consultation with members. As previously stated we believe that the Canadian Securities Administrators (CSA) should assume an oversight role in respect of OBSI's governance and accordingly recommend that OBSI be required to submit a similar report to the CSA on an annual basis.

16. We require clarification under section 15 (c) *"The Chair or his or her designate shall respond to the Complainant on behalf of the Board indicating the limits of the Board's authority.* " Does this mean that the Board will not address a complaint about the handling of a complaint even if it involves conflicts of interest, gross negligence , material errors , unlawful practices, breaches of privacy and similar major issues? If so , we question the governance practices of the Board.

17. There is no mention of the OBSI Consumer and Investor Advisory Council in the Terms of Reference . We recommend that this important Council be encapsulated in the Terms of Reference to prevent arbitrary limits placed on it or arbitrary termination of its mandate/operations.

OTHER REMARKS

Based on experience ,investment dealers have not embedded a culture that focused on delivering fair outcomes for complainants. The key drivers for a bad culture are a lack of senior management engagement with complaint handling, poorly conceived procedures and controls and inadequate staff training . According to the 2012 OBSI Annual Report, as regards compensation, Clients prevailed in 42% of cases, suggesting fundamental issues with how dealers are resolving complaints.

It appears to us that most of the quality assurance arrangements we observe are focused

on administrative checking of adherence to process (such as meeting cycle time targets) rather than assessing the quality of responses to customers and whether the outcome was fair. Thus, we urge the Government/regulators develop a common standard for dealer's **internal** complaint handling standards as a priority. We recommend ISO 10002 *Quality management - Customer satisfaction - Guidelines for complaints handling in organizations* It provides guidance on the process of complaints handling related to products within an organization, including planning, design, operation, maintenance and improvement. The complaints-handling process described is suitable for use as one of the processes of an overall ISO 9000 quality management system. We note parenthetically that in May 2011 the UK Financial Services Authority , Britain's financial regulator,issued new rules for complaint handling by financial institutions. They are very robust and Canada should assess them Re http://www.fsa.gov.uk/pubs/cp/cp11_10.pdf . It is unclear who will set this standard especially if OBSI takes on EMD's and Portfolio Managers as such member firms are not under an SRO cognizance.

Investor Advocates are concerned that the OBSI's Board has approved a budget for the year ahead that will decline slightly to just under $7.8 million for 2013 despite (a) unacceptably poor cycle time performance (For investment complaints, the average resolution time frame in 2012 was 290 days vs. a standard of 180 days) , (b) every indication that industry wrongdoing is on the increase and (c) industry complaint handling irresponsible and dismissive. For example, a recent Mutual Fund Dealers Association of Canada (MFDA) report says dealers should be reviewing the information they give clients about the complaint handling process, after a compliance sweep found a variety of shortcomings in the disclosure firms provide to clients.The MFDA issued a Bulletin http://www.mfda.ca/regulation/bulletins13/Bulletin0569-M.pdf spelling out the common issues it found when reviewing fund dealers' complaint handling documentation that must be provided to clients. The Bulletin says that, in certain cases the information in the summary contained unacceptably vague contact information; doesn't reference the MFDA or the Ombudsman for Banking Services and Investments (OBSI); doesn't spell out possible outcomes for complaints, or adequately explain various aspects of the process. It also found some issues with the process firms are using including: forms that use fonts that are too small and hard to read; and, information on legal limitation periods (a short two years in Ontario). We also are concerned about long cycle times most likely due to inadequate funding – perhaps the T of R should have language compelling the Board to providing adequate funding so that OBSI can fulfill its commitments and comply with acceptable standards.

It is very evident that the OBSI Directors are altering established standards to harmonize with controversial Department of Finance standards designed for bank disputes.One doesn't need to be a rocket scientist to see where this is headed. Accordingly, we are using this Consultation to publicly ask the OBSI Board to consider ending its banking complaint role. We believe this would be in investor's best interests. It's not as if there is a lot at stake here. According to the 2012 OBSI Annual Report ,investment firms carried the bulk of the compensation recommendations, representing $3.64 million of the total; just $123,938 (3% or the equivalent of the annual T&E budget for a senior bank

executive) in compensation was recommended in banking cases. The average recommendation on the banking side was under $3,200, with a median of just $900. On the investment side, the average recommendation was $22,613, with a median of $11,000. The biggest recommendation was just over $20,000 for banks, and just under $200,000 for investment firms.The drag of dealing with Federal rules/FCAC will only result in more complexity and less protection for investors.Removal of banks might have the collateral benefit of casting a bright light on the weak standards adopted by the Department of Finance for the BIG banks.

We note that Exempt Market Dealers and Portfolio Managers are being added as elligible Members (although the CSA has not yet decided on the matter of mandating these sectors to use OBSI and there is vocal opposition from PMAC, the trade Association for Portfolio Managers [see their June 3rd Comment letter on OSC 2013-2014 Priorities]) . Addition of these dealer sectors may be a good move in the long run but we urge the OBSI Board to plan and prepare for the disruptive effects on performance and cycle time and reputational risk such a move will have in the short and intemediate term.

We support a strong independent OBSI and therefore hope that our recommendations and comments will be considered n that light.

Should the Board wish to discuss this submission, we would be glad to attend such a meeting.

It is our firm conviction that these proposals are of such significance that the Board should engage with securities regulators before approving them. In our opinion they have a materially adverse impact on investor protection in Canada.

We also strongly recommend a Roundtable with all stakeholders to constructively discuss and debate critical complaint handling issues rather than be wholly dependent on written consultation letters.

Permission is granted to post this letter on the OBSI website .

Sincerely,

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