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General Counsel's Office

Canadian Investment Regulatory Organization
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Distributing Funds Disgorged and Collected through CIRO Disciplinary Proceedings to Harmed Investors (Phase II)

<https://www.ciro.ca/news-room/publications/distributing-funds-disgorged-and-collected-through-ciro-disciplinary-proceedings-harmed-investors>

Kenmar Associates appreciates the opportunity to comment on CIRO's proposal regarding the distribution of disgorged funds to harmed investors. With two decades of experience in investor advocacy and regulatory engagement, Kenmar is well-positioned to provide insights aimed at enhancing investor protection.

Kenmar Associates is an Ontario-based privately-funded organization focused on investor education via articles hosted at www.canadianfundwatch.com Kenmar also publishes the Fund OBSERVER on a monthly basis discussing consumer protection issues primarily for retail investors. Kenmar is actively engaged with regulatory affairs. An affiliate, Kenmar Portfolio Analytics, assists, on a no-charge basis, abused consumers and/or their counsel in filing investor complaints and restitution claims.

We appreciate that CIRO has provided detailed and clear response to comments made. CIRO will attempt to contact affected investors and not depend solely on a public notice. CIRO will assist claimants in filing their claim. CIRO will also work with Dealers as appropriate to contact harmed investors. We commend CIRO's efforts to maintain in-house administration to control costs and expedite payouts to harmed investors.

Our response to the current request for Comments

- **We are in agreement that the Proposal should apply to all CIRO Dealer registration categories.** It is essential that enforcement actions against mutual fund Dealers and Approved Persons isolate the disgorgement amount and do not merge with fines.
- We are not in disagreement with proposed restraints on claimants' eligibility, i.e. limiting the disgorgement distribution program by the parameters of the underlying enforcement action, where claims are readily provable as being connected to the misconduct giving rise to disgorgement. Disclosure will through transparency enhance investor's understanding of the calculation methodology which will result in higher acceptance rates.

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- There is a need to clearly distinguish the distribution of collected disgorged funds from restitution and investor compensation options in order to avoid and prevent retail investor confusion and overlap with the existing compensation options (such as OBSI). Prominent plain language on the application form should do the job supplemented by CIRO investor education materials. It is critical that the information about the Disgorgement Distribution Program clearly explain that acceptance of a payout from the disgorged funds distributed through the Program would not disqualify Eligible investors from seeking further compensation via other channels.
- The Proposal to keep the claim administration process as simple as possible to facilitate retail investors' access to disgorgement distributions is most appropriate as recommended in our original Comment Letter.
- **We agree that there should be an appeal mechanism to address disgorgement decisions.** We recommend at least 90 days for a reconsideration request. The request should be reviewed by persons that are different from those who made the original disgorgement distribution decision.

Other relevant points

While the current proposal represents significant progress, further enhancements and clarifications can amplify its effectiveness and impact.

Member accountability: **We urge CIRO to develop a process to ensure its Member Firms ("Member"), as opposed to the Member's representative(s) do not benefit from improper payments just because the Members were not named in an enforcement action involving their representative(s).** When the fees and /or commissions received were related to unsuitable activities, the Members share of the monies must be returned to harmed investors, not retained by a Member. By extracting payment of ill-gotten gains, such extraction can also serve as an effective deterrent. It could cause Members to be more diligent in recruitment, supervision and compliance. There could be potential reputational damage to CIRO as an SRO if it allows its Members to retain proceeds of unsuitable activities.

Program Transparency: We recommend that CIRO publicly disclose its methodology for calculating disgorgement, how to fairly allocate funds to impacted investors and the criteria for not making a distribution considered uneconomic.

One time payout: We agree that recipients of a Disgorgement Order should not benefit multiple times in different forums. Declarations are an acceptable approach to preventing double recovery.

Precedence of compensation: We recommend that the collection of disgorgement Orders should take precedence over the collection of fines. A recent Court decision

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involving the British Columbia Securities Commission concluded that offenders can escape payment of fines via bankruptcy but not payment of Disgorgement Orders. Indeed, unless the Bankruptcy and Insolvency Act is amended, CIRO may have an even greater challenge collecting fines.

Intensified Collection: We encourage CIRO to step up disgorgement collection activity to ensure sanctions are a credible deterrent. Without effective disgorgement collection, the value of this Program will decline.

Enhanced communications channels: Broader outreach through multiple platforms (e.g., social media, investor alerts) is essential to maximize awareness of disgorgement distributions.

Program Reporting : We recommend that an Annual report be prepared on the Disgorgement Program including statistics : Number of Orders, dollars announced , dollars collected and dollars distributed to harmed investors .A ten year chart should be included to highlight trends.
(The annual CIRO Enforcement report should cite the number of Hearings that resulted in investor restitution and the total dollars paid out to harmed investors. A ten year chart should be included to highlight trends.)

Uncollected disgorgements: **In our view, any uncollected disgorgement money owing from the Dealer's authorized representative should be to the account of the Dealer.** See Ref G20/OECD *High Level Principles on Financial Consumer Protection* 2022 which Canada endorses.
https://www.oecd.org/daf/fin/financialeducation/G20_OECD%20FCP%20Principles.pdf#:~:text=The%20G20%2FOECD%20HighLevel%20Principles%20on%20Financial%20Consumer%20Protection,an%20effective%20and%20comprehensive%20financial%20consumer%20protection%20framework
Under **Principle # 9 *Financial services providers should also be responsible and accountable for the actions of their intermediaries.*** This practice would prompt Dealers to be more vigilant on staff behaviour.

Priority of investor compensation: We reiterate our concern that investor compensation needs to be a higher priority in CIRO settlement agreements and Hearings. We expect CIRO to prioritize, where applicable, investor compensation. We are of the firm conviction that investor restitution is a potent deterrent especially when both the Member Firm and the Firm's representative are held to account and must face their client's dissatisfaction directly. Making a direct connection between rule breaking and a harmed client impacts reputation which Firm's want to protect and preserve at all costs. Full compensation payment to investors could be considered a positive mitigating factor in settlement hearings while inadequate or no compensation should be considered an aggravating factor.

This modern practice is in the Public interest and will also be most impactful in effecting credible deterrence and lead to enhanced Dealer supervisory/compliance systems and enhanced Approved Person training to prevent future infractions.

Conclusion

This initiative is a pivotal advancement in safeguarding Canadian investors. We urge CIRO to expedite its implementation, ensuring the proposed framework delivers tangible benefits to harmed investors. Kenmar remains available for further discussions to support CIRO in refining this Program.

We hope the information provided proves useful to CIRO decision making.

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