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Options dwindle for burned investors

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Investor advocates say a restructuring plan approval vote is looking to be the only chance left for 1,600 retail investors to try to recover the money they invested in non-bank-sponsored asset-backed commercial paper.

Brian Hunter, a Calgary-based engineer, has \$658,000 of his retirement savings frozen in ABCP in an account with Canaccord Capital. Hunter says he's one of about 1,400 retail clients with Canaccord Capital who was advised to purchase ABCP as an alternative to GICs and other guaranteed fixed income investments.

Hunter is one of the leaders of a growing group of ABCP investors seeking to get their money back from Canaccord.

Monday's announcement by the Pan-Canadian Investors Committee for Third-Party Structured ABCP that protection had been granted under the Companies' Creditors Arrangement Act (CCAA) makes legal action against the firm virtually impossible.

If approved, the proposed restructuring deal would make all of the ABCP providers and sponsors immune from being sued by note holders. Hunter says the approval of the CCAA protection makes it impossible to go after them in the meantime. So unless retail note holders, each of whom gets a vote, turn down the approval agreement, they will lose all legal rights to go after their money.

"I had lined up a class-action lawsuit — you have to keep your options open, and that was absolutely the last resort. I had a lawyer who agreed to do that, but when I spoke to him this morning, he said he was backing off because he can't see his way through CCAA and what they have done there," Hunter says. "It's not just the trusts [we can't sue but] anybody, including all the banks that sponsored this — which is every one of them — including DBRS, including Canaccord, including Desjardins. They have taken the legal rights of everybody away."

If there are lawyers who can navigate CCAA, Hunter says, chances are they are already employed by the other side.

"I'm trying to find anybody who can represent me in court in Ontario, and that's not easy because anybody who knows anything about CCAA is already working with the vendors," he says.

Diane Urquhart, an independent financial analyst and vocal investor advocate, says by eliminating the legal recourse of investors, the proposed ABCP

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restructuring deal essentially protects corruption in Canada's financial system.

"It was sold without a prospectus, and I would say after having gone through the scene of the accident that non-ABCP was sold unlawfully into the whole market," Urquhart says.

To be sure, ABCP was an extremely complex financial product, which is why Urquhart says advisors who recommended the ABCP at Canaccord can't fully be blamed for recommending the investment vehicle, since it had high credit ratings from Dominion Bond Rating Service.

She says there is evidence to suggest ABCP should never have received investment-grade ratings in the first place because it had a flawed liquidity agreement backing it.

She points to a Standard & Poor's report from 2002 that outlines that the liquidity agreement underpinning commercial paper in Canada was insufficient. In the report, S&P says that liquidity agreements exist in Canada but that investing requires a "leap of faith" that liquidity will still be there if a crisis arises. As a result, S&P says it would not be possible to consider Canadian commercial paper investment grade.

"S&P indicated they had assessed the guidelines from the Office of the Superintendent of Financial Institutions and they had seen the content of the liquidity agreement behind the ABCP, and on that basis, they had determined that it was grossly deficient," Urquhart says. "There was not sufficient protection to give this an investment grade.

"Because this was short-term paper funding long-term assets, a liquidity crisis was inevitable, and OSFI would someday be sorry that they instructed the banks to offer such a liquidity agreement."

Urquhart says the banks that sponsored and distributed ABCP conduits are sophisticated enough to have realized this risk.

"I go back to the vendor, the financial institution that had a credit derivative research team, which likely had PhDs. To me it doesn't take a PhD to know that you have a flawed liquidity agreement," she says.

The 1,600 ABCP note holders do have the balance of power in the ABCP approval process, since they represent more than the majority of votes needed to pass, but the committee overseeing the restructuring has warned investors that if the deal falls through, investors risk losing everything. Instead, the committee has urged investors to hold on to the notes until maturity, at which time they might be able to recover most of their face value.

Urquhart estimates the majority of investors might get 60 cents on the dollar of their initial investment if they hold the notes for seven years. She doubts few, if any, will get all their money back.

"Using the estimated seven-year term of the proposed long-term notes and knowing how much credit spreads have gone up for AAA investment-grade credits, I would guess that the new notes will stabilize at 50 cents to 60 cents on the dollar, but all this depends on whether the material contracts within the trusts are released for independent examination to experts interested in buying or if indeed there are any buyers amongst the world's heavily damaged banks, hedge funds and other institutional investors," she says.

This solution doesn't help the contingent of retirees who invested in ABCP as a short-term income-generating vehicle — many of these investors need the money now.

Urquhart believes this could be solved if retail investors were remunerated by the banks that sponsored the ABCP, which she says is very costly, but they can afford to do it.

"These were being sold to these customers on the basis of being GIC and treasury bill substitutes with high credit ratings," she says. "The investment banks and their bank parents have had the means from the beginning and even now in light of the

current damages to take this all — including pension funds and government funds — onto their own balance sheets. [They should do this] because they sold a flawed product."