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Charge trusts with fraud, groups urge

REPRESENT 1.3 MILLION

Letters ask police to investigate 'deceptive' yields

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Three groups representing more than 1.3 million senior citizens and small investors are asking police to seek criminal investigations into the "deceptive cash yields" used in the marketing of income trusts.

The National Pensioners & Senior Citizens Federation, United Senior Citizens of Ontario and the Small Investor Protection Association (SIPA) yesterday jointly released letters they have sent to the RCMP and Ontario Provincial Police.

In a press release, the groups said their requests for criminal investigations were supported by a professional opinion letter sent by forensic accountant Al Rosen.

Mr. Rosen's opinion letter says "Canadians were repeatedly lied to by marketers about the so-called income yields that many trusts were supposedly generating." The "misleading" yields were often not sustainable because they represented cash yields Mr. Rosen says "were well in excess of the income generated by the underlying companies."

In many cases, cash returned to investors represented funds that should have been set aside to maintain the income-generating capacity of the businesses or to weather downturns in the business cycle. "I am not alone in having publicly characterized some trusts as mere pyramid schemes, perpetrated by professional marketers upon unwitting investors."

In an interview, Mr. Rosen estimated "half" the more than 250 income trusts could be categorized either as pyramid schemes or outright ponzi schemes.

He believes some unstable income trusts were marketed to individual investors by understating the capital risks.

"In my professional opinion, there is no doubt about the intent of using material deceit in such efforts. However, sufficient evidence must be gathered in order to proceed with prosecutions."

Tax benefits accounted for 25% to 30% of their over valuation but "these guys were selling them at two and three times what they were worth as private companies," Mr. Rosen said. "The rest of it was hype."

That's why — despite a roaring bull market in Canada — 25 trusts are still down by 50%, with some having collapsed entirely.

"The devastation has been huge but they don't talk about those who had been fleeced long before Halloween."

Mr. Rosen says the pro-trusts lobby has tried to shift the blame on the government's tax policy rather than where it should belong: on the country's underwriters and brokers.

The trust industry's most vocal face is the Canadian Association of Income Trust Investors (CAITI), formed soon after the Tories decided to tax trusts.

CAITI is a trade lobby group whose founding members include a dozen income trust firms or mutual fund companies and just four individual investors.

Asked to respond to the joint release, CAITI founder Brent Fullard said "They may very well have a valid point." The trust market was forced to evolve in response to unlimited liability "so I am sure these groups will find a satisfactory resolution to the concerns that they are expressing."

SIPA president Stan Buell says the trust industry is "trying to create the perception that CAITI represents retail investors. It shows the power of the industry at manipulating the public and how they mislead investors."

Mr. Buell says the investment industry "bastardized" the concept of income trusts and "created the illusion that all income trusts provide a safe haven for investors with a handsome rate of return."

CAITI also comes under attack at a popular financial discussion forum. There, investment counsellor Norbert Schlenker says CAITI "puts up hurt investors as its public face" but is funded entirely by investment bankers and income trusts and funds of income trusts — "i.e. the people whose livelihoods depended even more on the fiction than any individual investor."

Diane Urquhart, a consulting analyst who was at the press briefing in Ottawa yesterday, says her research shows the use of deceptive yields in trust marketing materials constitutes "potentially criminal conduct under section 380 of the Criminal Code."

Ms. Urquhart estimates 46 business trusts are still down $8-billion from their initial public offerings. While CAITI talks about $35-billion losses after Oct. 31, these were soon trimmed to $20-billion in a matter of days. Only a fifth of the losses were caused by the Finance department's decision to tax trusts, Ms. Urquhart said.

Consultant Andrew Teasdale, who is preparing several reports on trust valuations, says there is little doubt "the returns and the risks of these investments were misrepresented. I don't see how these could have been justified being sold to taxable investors at all."

Mr. Teasdale agrees with Mr. Rosen and Ms. Urquhart.

"There needs to be an inquiry about misrepresentation. It's not a spurious accusation. It's something that can be actually proved mathematically."

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