

From Desk of Lee Beyer



Oregon

Kate Brown, Governor

Department of Consumer and Business Services

Division of Financial Regulation

350 Winter St. NE, Room 410

P.O. Box 14480

Salem, OR 97309-0405

March 9, 2017

To: Senator Lee Beyer, Senate District 6

From: Richard Y. Blackwell, Policy Manager, Division of Financial Regulation

Cc: Senator Michael Dembrow, Senate District 23
Senator Floyd Prozanski, Senate District 4

Re: Senate Bill 96A

Senator Beyer,

You had asked some follow-up questions regarding Senate Bill 96A. Please find our responses below:

- Cases like one in which 18 investors were harmed by a violation of suitability requirements has prompted increasing concern in the Department about the lack of remedies for investors.
 - Most states require a bond between \$10,000 and 35,000. Bonds protect against fraud. They do not cover defense costs for the investment advisor or broker dealer.
 - Bonds are paid out on a first come first served basis. A \$10,000 bond is inadequate to cover the cost of bringing an arbitration action or lawsuit.
 - 3 other states are looking for ways to supplement current bond coverage because it generally provides minimum protection for investors.
 - The North American Securities Administrators Association and the Public Investor Arbitration Bar Association both looked at errors and omissions insurance as a way to address investor harm and unpaid arbitration awards.
- A typical small to medium sized investment advisor firm will manage between \$10 to \$20 million of investor funds.
- Most Registered Investment Advisor Firms already have Errors and Omissions insurance.
 - \$1 million is the most common amount. Estimates from insurers indicate premiums are about \$2,000 a year. Premiums for \$500,000 in coverage average \$1,500 a year.
- Insurance does not cover fraud or other willful acts. It does cover:
 - Negligent breach of duty, misrepresentation
 - Misstatements, errors, omissions
 - Defense costs

- Most cases involve negligence:
 - The purchase of a security that is not suitable for the investor.
 - Mistakes in entering an order or failure to enter an order.
 - Failure to make required IRA distributions.
 - Often individuals rather than firms are responsible. Policies cover “failure to supervise.”
 - Bonds contain a clause which requires the person purchasing the bond to repay the surety company for any amounts they have to pay out on the bonded person’s behalf.
 - Surety companies typically require both company and individual financials and a very good to excellent credit rating for a \$35,000 financial professional bond. Starting at 1.5% of the coverage, bonds prices are adjusted upwards based on overhead costs, the risk to the surety company, credit scores, and financial statements.
 - Losses sustained during the financial crises caused surety companies to hesitate to issue new bonds. New investment advisors and broker dealers could find it difficult obtain a bond.
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SB 96A reference points

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