Investor Protection

Investor protection at the highest level is “a guarantee that protects the investor from losing their investment because of fraudulent activity or unforeseen circumstances”. It is one of the most critical factors that help in reducing the risks associated with financial trading.

Unfortunately it has happened too often that brokers or other intermediary third parties commit financial fraud by adopting bogus practices, which is why a healthy general investment protection environment must be in place for investors to return to, in case their investment becomes subject to these mala fide practices.

From our Curacao perspective, this protection must apply to both domestic and foreign investments, to ensure that foreign investors are treated correctly and as equals. The mechanics must be such that they provide a safe passage for foreign investments and help them in reducing the risk of loss. Regulatory, governmental (political) discrimination and non-transparent tax regulations are often important factors that cause such losses.

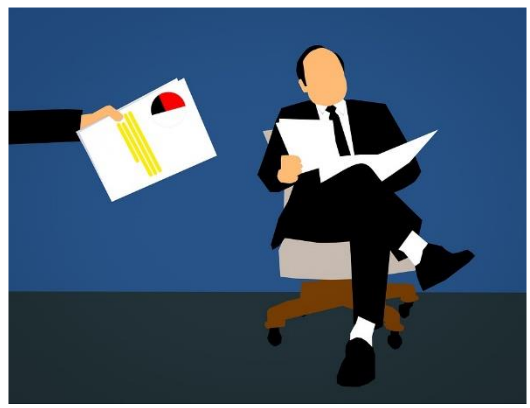
The Importance of Investor Protection

The main focus of this protection is really to ensure that investors are “as best as possible” aware of their purchases, and these investments are secure even in case of a “failure” or fraudulent action of any of the financial intermediaries that investors normally use, like for instance the brokers.

Investors must inform themselves and/or a good financial intermediary should inform the investor, on how the process of the investment works. Who are the parties involved and what happens if any of those parties acting as an intermediary "fails" and/or commits fraud?

In this publication we will of course focus on investments in securities and simply try to awaken the investor to some important factors they should always keep in mind when investing, in order to protect their investment. The factors we will mention are not the only ones, but we hope that the ones we mention assist investors in getting a clearer picture of what they should be on the outlook for.

In general, securities' investments have a few levels of possible operational risk. The levels may vary from the bank or broker the investors use, the parties that those banks or brokers use on their turn, and the ultimate so-called custodians, that in the end hold the investments.



Other issues to consider are, in general: who else is investing, and what am I getting into. With equity investments, that are private placements or where there are clear majority shareholder groups, the question becomes if your rights can be curtailed by those majority shareholders.

While the listing of securities on a securities exchange definitely brings with it a higher sort of "status" in the sense that there are some professional parties that have been involved, like the Listing Advisor, legal counsel and the exchange itself, the listing alone is of course never a guarantee that something can't go wrong operationally and you can lose your investment or a part of it.

Another issue investors should pay attention to, is how the ownership structure of the company they are investing looks like. In several countries, controlling shareholders often can defacto "expropriate" minority shareholders' interests. The delicate issue here is the relationship between cash flow control and voting control. A very difficult issue that is not suitable to treat in detail here, but one that investors should be aware of. In general, securities listed on exchanges will give proper information on the ownership structure so that investors can take that into consideration.

Insiders/majority owners could also use the firm's profits for self-benefit rather than returning the outsider investor's money thru an adequate dividend policy. With the help of investor protection rules, corporate governance, and a well-developed jurisprudence on tort or unjustified enrichment, outside investors can be protected against such expropriation dangers by the hands of controlling inside traders.

The Risk of Investment

One can never invest by depending on their intuition. It is a work of extensive research and requires close observation to turn out fruitful. Use the necessary bona fide advisors before investing and once advised make sure to read up on the intended investment. In our nowadays world there are more than sufficient sources that an investor can “consult” online before he/she/it makes the actual investment decision.

An investor must create a diverse portfolio to reduce the potential risks of investing and take the following generally applicable risks into consideration. It should be noted that companies that are listed will always have to describe these risks in their respective Offering Memoranda.

Some of these risks are:

Interest rate fluctuation: Multiple factors determine the interest rate in a specific market. These rates tend to fluctuate the overall value of the security that an investor has invested in. To take a very simple example, an increase in the prevailing interest rates for corporate bonds can reduce the prices of a bond that was issued before the date on which this prevailing interest rate changed.

Risk of reinvestment: Bonds and Commodities have fluctuating interest rates a/o prices. There is a possibility that the yield that the investor earns from the original investment will not be as profitable if it has to be reinvested, because of a prepayment corporate action by the issuer, i.e. if the issuer has the right to repay the investor before the initially intended period/tenure of the investment.

Risk of default in payments by the issuer: There are times when the issuer is not able to make the contractual payments on time and may have to defer payments to investors. This is a common risk when investing without checking the credit strength of the issuer, and it is most common in bond trading.

Market Risk: A country’s overall economy plays a critical role in determining market rates. If the economy is declining, the return may quickly become less, especially when investing in cyclical securities.

Risk of equity: The movement in the value of listed shares varies based on the demand and supply of these shares. And such demand and supply may often be influenced by forcers that as such have nothing to do with the performance of the company. The risk of loss caused by the reduction in the share prices is known as equity risk, and can indeed be influenced by for instance a sudden psychological investor mindset (the famous fear versus and greed phenomenon).

Currency Risk: The risk of loss on foreign investments due to the shift in foreign exchange rates.

Liquidity Risk: The risk regarding the inability to pull or sell your investment at an optimum price or when you want to do the transaction. You may need to settle for a lower price to be able to sell. There is also a possibility that some conditions might restrict you from selling altogether.

Risk of concentration: The potential of losing your investment because of investing everything in 1 particular investment type. A certain level of diversification over different asset classes and within each class is often the wise thing to do. A good investment advisor can assist the investors here.

Horizon Risk: The loss caused by the unpredictability of futuristic events. For example, the need to sell your investments because of sudden unemployment.

Longevity Risk: This risk is common in elderly and retired people. It refers to the loss caused by outliving your savings. Careful planning and fine-tuning of your investments to assure a certain cash flow and decrease of risks as you get older is important.

Existing Protections

Each country has a different policy to protects investments. However, some conditions are generally applicable throughout the world.

Some of the most common strategies are investor protection treaties and bankruptcy laws. Investment protection treaties [also known as Investments Protection and Promotion Agreements (IPPA) or Bilateral Investments Protection and Promotion Agreements (BIPA)] and Bilateral Investment Treaties are mostly used in bilateral agreements between countries.

Most exchanges often demand that issuers state the investor risks in a clear and high-quality prospectus and submit it to the exchange. People usually refer to a prospectus as a formal document that states comprehensive information about an investment available to the public.

It is essential to properly complete a clear and well informing prospectus when an issuer offers bonds, stocks, mutual funds, and/or any other financial instrument that is acceptable, to the investing public.

Whether it is a private placement, a listing to create a secondary trading facility for investors, or a capital seeking initial public offering, the prospectus must contain all the essential information allowing the investors to make a sound decision about their investment.

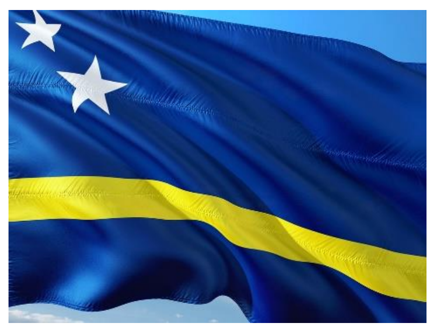
Some of the information that the issuer should minimally describe clearly in a prospectus:

- The history of the business and its reason for success
- The overall operational and management experience of the company
- The plan of action: objective to raise funds (how much, why/use of funds, and repayment/return expectation)
- Financial forecast including cashflow details
- Risk assessment: potential risks of the business, industry, politics, etc.

A related subject to investor protection concerns financial literacy. There are many countries where financial illiteracy makes it difficult for investors to protect themselves. Especially for those markets a clear (level "101") common language description of the above referred to risks is of great importance.

Investment Protection in Curaçao

The Dutch Caribbean Securities Exchange is established in Curaçao, an autonomous country within the Kingdom of The Netherlands. For Investors in or into Curaçao including investors investing in securities listed on the DCSX common investment protection is achieved through applicable bankruptcy laws, Central Bank of Curacao and Sint Maarten regulations on attracting capital and supervision of the financial market as a whole, including the DCSX. At the same time Bilateral Investment Treaties for the Kingdom of the Netherlands are applicable based on the country's position within the Kingdom. See also below.



A few specific protection guidelines incorporated in the local laws and regulations or fully endorsed by the Curacao Government that are worthwhile looking at are:

Last year, Ministry of Economic Development of the Government of Curaçao, the Curaçao Investment & Export Promotion Agency (CINEX), Caribbean Export Development Agency, CAIPA & UNCTAD Launched the iGuide Curaçao. The iGuide is an online investment guide under the auspices of a trusted international agency, UNCTAD in Collaboration with the International Chamber of Commerce. It is a very important tool to position Curaçao and capture the attention of potential investors. UNCTAD and the International

Chamber of Commerce built this platform from the investor's perspective, therefore, it contains hands-on relevant information investors need, including details on investor protection.

The investment Guide covers the protections covered in the constitution, dispute settlement, and international investment agreements (the afore referred to Bilateral Investment Treaties of the Dutch Kingdom). In the following paragraphs you will find some details on a few topics as presented in the iGuide.

Constitution

Article 16 of the Constitution of Curaçao provides for the protection of property and adequate compensation if that property its expropriated because of the public interest.

Dispute settlement

In the case of a legal dispute, parties can turn to the public court system or opt for arbitration. So yes, it is also possible to include an arbitration clause in any contract in order to avoid the public court system and go straight to arbitration, which has its advantages, like the confidential nature of the proceedings and price point.

If one of the parties doesn't adhere to the arbitral decision, the wronged party may turn to the public court system to enforce the arbitral decision, but such will only uphold if procedural rules have been observed and the enforcement of the arbitral decision is not against public order or good morals.

The legal basis for arbitration can be found in Section 1020 of the Code of Civil Procedure. Every arbitration that takes place in one of the jurisdictions of the Dutch Caribbean is subject to the English version of the UNCITRAL Model Law on International Commercial Arbitration, as adopted by the United Nations Commission on International Trade Law.

The enforcement of a foreign arbitral award is subjected to the provisions of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of New York, 1958.

International Investment Treaties (Bilateral Investment Treaties)

Curaçao forms part of (i.e. is a Country within) the Kingdom of the Netherlands. As such, the investment protection treaties concluded by the Kingdom of the Netherlands, in general, apply to Curaçao. This means that if Curaçao is used as the home base to invest in other countries, these treaties may help to mitigate certain risks that are involved with such investments. Based on these investment treaties the business is entitled to equal protection as an investor who is a resident of the treaty partner. As of April 27, 2020, there are 107 Bilateral Investment Treaties (BITs), 77 Treaties with Investment Provisions (TIPs), and 31 Investment Related Instruments (IRIs). A full list of investment treaties can be found here: Complete List

Final Thoughts

Investor protection is a set of regulations and guidelines that are enacted or fully endorsed by the relevant legal systems and authorities in the different countries and geared towards protecting the foreign or domestic investments from unforeseen risks. Most of the laws are different in each country, but some similar ones are also found. It is essential for every investor to always study the issuer's information (see our remarks above about the content of the prospectus of an issuer), make additional research like verifying the credit history of the company and in general before deciding to invest "read up" on the potential investment and its issuer. In addition, focusing on the issuer, investors should research different ways to protect their investment thoroughly and know their rights as investors. To do this successfully, investors are required to improve their financial literacy to understand the information.

In general, we know that most people are financially fairly illiterate in this world. The residents of Curaçao are no exception. So, it is logical that most of the time people tend to seek out assistance from investment and/or financial advisors, rather than invest time in financial literacy. If you seek help from an investment advisor, financial advisor, or broker that is locally based on the island, it is important to know that such advisor or intermediary must be approved by the Regulator, the Central Bank of Curacao and Sint Maarten.

Financial Literacy remains an important topic for the DCSX. We started with easy to understand educational publications in 2017 and 2018. In 2019 we teamed up with several organizations to provide financial education courses. In 2020 we will level up our publications to continue the development of our readers. For the DCSX financial literacy is really a "continuous education process".

The trick is to be clear and try to explain things in common language.
Any professionals interested in joining us in this continuous education process are welcomed.

Sources

UN UNCTAD iGuide Curacao https://www.theiguides.org/public-docs/guides/curacao

DCSX Requirements for Tradeable Listings https://www.dcsx.cw/wp-content/uploads/2020/03/Tradeable-Requirements-Feb-2020.pdf
Previous DCSX educational publications: https://www.dcsx.cw/education/page/3/

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