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## Veritas CEO Anthony Scilipoti's lonely quest for financial truth

By **TIM SHUFELT**



*Many don't want to hear what the investigative stock researchers at **Veritas** have to say, especially with the bull market in its seventh year*

As a forensic accountant, Anthony Scilipoti instinctively looks to the paper trail. He hunches over a receipt, which lacks a crucial piece of information. "It's killing me," he confides.

Twisting a silver cufflink stamped with a cursive "V" for "**Veritas**," the Latin word for "truth," he seizes on the bill's single cryptic lead: "AM."

Against the guiding principles on which he's built his career, he offers up a hasty conclusion on scant evidence.

"I'm going to go out on a limb," he says. "It's Amanda, right?"

"No," the server replies.

"Jessica?" he tries, scanning his memory from previous visits to the restaurant.

"It's Joelle."

It's an uncharacteristic scene for a man who prides himself on due diligence. **Veritas Investment Research**, the firm **Mr. Scilipoti** co-founded, is known for its investigative stock research, for poring over financial statements in search of [accounting](#) trickery.

**Mr. Scilipoti** interchangeably likens the firm's research to an umbrella, an insurance policy, and a bathing suit, the latter good to have when the tide goes out, lest one be discovered to have been swimming naked, as per the famous Warren Buffett quote.

No matter the metaphor, the message is clear: When bad things happen, investors are going to want one or the other.

It's pouring rain in Toronto when we meet at Taverna Mercatto, the latest addition to the Mercatto group of Italian restaurants, between the Air Canada Centre and the Rogers Centre. I'm told it's a "classic trattoria," with emphasis on the first and third syllables. "Italy would be like this. Loud."

That's a word that can also fairly be used to describe **Mr. Scilipoti's** reputation on Bay Street as a man making bold, contrarian calls against Canadian darling stocks.

His professional life is rooted in a fascination with accounting, his first lessons in which were provided by his father, Sebastian. Delivering newspapers in North York, Ont., the 14-year-old Anthony had saved up enough money for a bicycle. His father insisted that he make a business case to support his choice – a red and yellow steel-framed Coppi, named for the legendary Italian cyclist. At more than \$500 in 1984, it was far from the cheapest [option](#), but Anthony convinced his father that it represented the best value for money. He still has the bike.

The elder **Mr. Scilipoti** owned a furniture manufacturing business in Markham, instilling in his son an entrepreneurial streak. Having moved on from paper routes, Anthony started a business in his late teens, selling custom promotional gear such as hats, shirts and pens to other businesses. His father showed him how to track his revenue and expenses on Accpac, the accounting software.

After earning a commerce degree from the University of Toronto, **Mr. Scilipoti** landed a job at Arthur Andersen, at the time one of the Big Six accounting firms, working in a small due-diligence group. His first deep dive focused on retailer Adventure Electronics, which he believed was [drowning in debt](#). "I looked at the financial statements and said, 'This company is going to go bankrupt.'" The chain did just that in 1998, the year after he left the firm.

Taking a forensic approach to financial analysis, he found that numbers can tell stories. "I can look at financial statements and tell you what happened over the past year."

**Mr. Scilipoti** co-founded **Veritas** in 2000 as a research outfit free from the potential corrupting influence of an investment banking division. At the time, the [stock market crash](#) was taking hold as overhyped early Internet stocks crumbled. Investors awoke to the conflict of interest inherent in large brokerages, which were using their research divisions to drive business to their underwriting arms.

The so-called "Chinese wall" that was supposed to separate the two functions didn't really exist. Research analysts were essentially paid to be bullish rather than objective. In 1999, Merrill Lynch analysts had 940 "buy" ratings on stocks and "sell" recommendations on just seven.

Investors paid dearly, as the Nasdaq [Stock Market](#) composite index fell by more than 65 per cent between March, 2000, and April, 2001. A rash of accounting scandals followed, engulfing Enron, WorldCom, and Tyco International, reinforcing the need for independent equity research – a cause championed by New York's then attorney-general Eliot Spitzer.

"Accounting didn't matter," **Mr. Scilipoti** says, spooning spicy tomato sauce onto a stuffed risotto ball. "Auditing didn't matter. Analysts wrote whatever. The market was primed for our type of business."

Offering up independent equity research for a fee ran counter to the prevailing model of the financial sector, which treated research as a loss leader to support other divisions. **Mr. Scilipoti** says investors had come to expect to receive such information for free, an argument that sounds familiar to a newspaper reporter.

The firm built up a roster of about 60 institutional clients, such as banks and investment funds, in part through issuing scathing reports on large Canadian companies. **Veritas** denounced the lack of disclosure by building-products company Royal Group Technologies, which would soon be at the centre of one of the country's messier accounting scandals, beginning in 2004.

The firm was also an early detractor of the earnings reporting practices of Nortel Networks, which filed for bankruptcy protection in 2009. **Veritas** was also vocal in its objections to Biovail's aggressive accounting practices, before its stock tanked.

**Veritas** has since extended its criticism to Biovail's latest incarnation, Valeant Pharmaceuticals International, a company with such growth ambitions that should it reach its goal, it would become the single largest listing on the [Toronto Stock Exchange](#) by the end of next year.

"It's a poster child of today's market," **Mr. Scilipoti** says. "It has complicated accounting, it has a complicated tax structure, high leverage, and a very aggressive growth-by-acquisition structure. These are all the makeup of a high blow-up risk."

Few share those concerns. **Veritas** has the lone "sell" rating on Valeant's stock among the 23 analysts following the company and issuing recommendations.

Since **Veritas** put out its original accounting alert on the company in late 2011, Valeant's stock has risen sixfold. To be fair, **Veritas** didn't slap an explicit "sell" rating on the stock until last July, but even since then the stock has more than doubled.

In the case of Valeant, and other large Canadian companies such as Catamaran Corp. and CGI Group, investors could have made a great deal of money by ignoring the risks flagged by **Veritas** or in doing the opposite of what the firm recommended.

With North American stocks still riding a historic updraft, risks might not be met with due punishment by investors. The bull market is now in its seventh year, having tracked a fairly steady upward trajectory since bottoming out in 2009. Stocks are seen by many investors as the only alternative in an era of near-zero interest rates and miserly bond yields.

"The last few years have been difficult for this type of work," **Mr. Scilipoti** says. "The market is awash with cash, and risk-free rates are negative, so investors' appetite for risk is, in some cases, extreme. That's led to investors overlooking things that in other market conditions they would not overlook."

Spooning hot peppers on a bowl of orecchiette – "they don't add a lot of flavour, they just add heat" – he says he is not pulling for a market downturn. But it's when sentiment begins to shift that less sustainable companies become exposed. "We're pushing for the truth to come out," he says. "Sometimes it takes years."

The interim can be tough. The firm is often the sole outlier in a chorus of analyst support, as is the case with AutoCanada, Fortis, Enbridge, Exchange Income Corp. and CAE.

Management can react strongly to finding itself the target of a **Veritas** offensive. They make angry phone calls, issue legal letters. Occasionally, they blacklist **Veritas** analysts from participating in conference calls to discuss earnings.

Such is the lonely path of a contrarian. But the company remains one of the few sources of independent research in Canada and adding another bullish voice to the consensus would be of limited value.

A little more than half of the company's ratings qualify as "sells." The broader Canadian analyst community, meanwhile, has 1,845 "buys" compared with just 301 "sells" on the stocks included in the S&P/TSX composite index, according to Bloomberg data.

"You end up being known for making these very noisy calls. That gets people's attention," **Mr. Scilipoti** says.

Even in a relentless bull market, **Veritas's** warnings find an audience. In September, 2013, the company raised the alarm on DirectCash Payments, advising its subscribers to "cash out" of the stock over a lack of disclosure and the company's exposure to the payday loans market. DirectCash shares then promptly fell by 24 per cent without any other negative developments and just days after the company implemented a dividend, which prompted a trading halt.

With a staff of 22, the firm's research can move the market, what he calls the "**Veritas** effect," showing the work is relevant and that investors are still paying attention, he says.

Eventually, the broader market will become less forgiving of accounting irregularities and deficiencies in disclosure and more receptive to the dissenting few like **Veritas**, **Mr. Scilipoti** says. "The time will come. We're not going away."

In the meantime, he'll remain committed to the in-depth forensic research method on which the firm was founded. "Thanks Joelle," he says, after we settle up. "I won't forget again."

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#### **Anthony Scilipoti, President & CEO of Veritas Investment Research**

**Age:** 44

**Place of birth:** Toronto

**Education:** A commerce degree from the University of Toronto

**Family:** Married to Ana for 17 years; three daughters

**Siblings:** One younger sister

**What he's reading:** *The Most Important Thing: Uncommon Sense for the Thoughtful Investor* by Howard Marks

**Favourite band:** AC/DC

**Favourite movie:** *Rocky*

**Favourite vacation spot:** Used to visit Italy when he was younger but now prefers southern Spain

**Who he'd like to have lunch with:** Steve Jobs

**His latest thing:** A fitness enthusiast, he has recently taken an interest in adventure races. A couple of years ago, he was part of a team that completed Tough Mudder, a gruelling obstacle course that features fire, barbed wire and electricity. "Anything I can do to push myself," he says. "But I didn't really like the electric shocks. They hurt."