Via Email

October 18, 2018

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission of New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
Superintendent of Securities, Nunavut

The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor, Box 55
Toronto, Ontario M5H 3S8
Fax: 416-593-2318
comments@osc.gov.on.ca

Me Anne-Marie Beaudoin
Corporate Secretary
Autorité des marchés financiers
800, Square Victoria, 22e étage
C.P. 246, tour de la Bourse
Montréal (Québec) H4Z 1G3
Fax: 514-864-6381
consultation-en-cours@lautorite.qc.ca

Re: Proposed Amendments to NI 31-103 and Companion Policy 31-103
Reforms to Enhance the Client-Registrant Relationship (Client Focused Reforms)

TD Wealth is pleased to provide these comments on the proposed amendments to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("NI 31-103") and Companion Policy 31-103CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("31-103CP" or the Companion Policy, and together with NI 31-103, the "Instrument") in respect of proposed reforms to enhance the client-registrant relationship (the "Client Focused Reforms").

We support the efforts of the Canadian Securities Administrators (the "CSA") to improve the client experience and to enhance the relationship between clients and their investment advisers, including securities dealers who provide investment advice. We further appreciate the CSA's efforts to reflect the views expressed by stakeholders in previous consultations, including the tailoring of certain requirements to suit different business models. In providing these comments, we strive to help the CSA to achieve its stated objective of striking a fair balance between the public policy goals of investor protection and promoting efficient capital markets.

While we are supportive of the CSA's efforts to advance investors' interests, we believe that there are certain aspects of the Client Focused Reforms that will have unintended consequences and may, in fact, be contrary to the best interests of investors. Among other things, we are concerned that the proposed reforms may not allow sufficient flexibility to account for evolving technology and consumer preferences.

Our comments are intended to assist the CSA in revising the Client Focused Reforms to avoid unintended consequences and to continue to promote innovation while supporting the effective implementation of proposed new investor protection measures.

Before turning to our specific comments, we note as a general observation that the Client Focused Reforms address requirements applicable to registrants at the legal entity level (i.e. as entities in their entirety), rather than the discrete business units or operating divisions within the registrant. Some of the proposed Client Focused Reforms may be better framed as applicable only at the business unit or operating division level. For example, TD Waterhouse Canada Inc. ("TDW") houses separate divisions in accordance with IIROC rules. Different TDW divisions provide clients with order-execution only ("OEO"), advisory and portfolio management services under distinct branding and account opening processes for each division, as mandated by IIROC. Requiring TDW, as a registrant, to comply with cost option disclosure at the registrant level will, for example, result in clients receiving very different disclosure than that received by a client of a registrant operating exclusively as an OEO firm. In our view, certain registrant obligations, such as cost option disclosure, know your client ("KYC") and know your product ("KYP") requirements, would be better applied to specific business units and operating divisions within a registrant that operate separately, rather than across the firm as an entirety. We recommend that this option be expressly permitted in the Client Focused Reforms.

Summary of TD's recommendations

Our comments reflect our desire to meet our current and future obligations as a registrant while continuing to provide our clients with a broad range of product and service offerings, and to deliver those products and services in a manner that suits the needs, preferences and expectations of our clients. Our key recommendations relate to:

- Tailoring certain aspects of the Client Focused Reforms to address the specific needs and expectations of "do-it-yourself" and institutional investors.

- Tailoring the KYP requirements to encourage product innovation and preserve the range of product choices currently available to investors.

- Clarifying the Companion Policy's conflicts of interest guidance for registered firms that trade in or recommend proprietary products (i.e. securities that are issued, sponsored or managed by affiliates of the registrant).

- Permitting referral arrangements between affiliated entities to ensure investors are served by the most appropriate registered firm within the affiliate group based on each investor's changing needs and circumstances.

- Modifying the suitability requirements to minimize unintended consequences and unnecessary costs for registered firms in circumstances where the incremental benefit to investors is limited, at best.

- Extending the transition period for implementation of the Client Focused Reforms to allow for meaningful consultation with self-regulatory organizations ("SROs"). This will be critical, given the scope, significance and complexity of the Client Focused Reforms and the extent to which they will be impacted by SRO rulemaking.

1. **Tailoring requirements impacting "Do-it-Yourself Investors" (regulation of order-execution-only firms)**

(a) KYC requirements

We submit that the proposed enhancements to the KYC requirements should not apply to OEO firms ("OEO Firms") that are currently exempt from suitability requirements under IIROC rules (the "OEO Suitability Exemption")[1]. We are supportive of the CSA's goal of ensuring that registrants have sufficient information about the specific circumstances and needs of their clients to be able to perform a meaningful suitability analysis of investment options through expanded KYC requirements. However, unlike full-service advisers, OEO Firms obtain and maintain a very limited set of client information, including contact information, employment information, salary and the names of any issuers of which the client is an insider. In our view, "do-it-yourself investors" should not be asked to provide information that will not be used by a dealer in performing a suitability assessment. Requesting more personal information from clients than is reasonably required to provide an OEO service is both onerous for clients and potentially misleading, as clients may mistakenly assume an OEO Firm uses that information to inform its service or product offerings or to perform investor protection activities, when this is not the case.

Requiring OEO Firms to collect additional KYC information is inconsistent with their business model and imposes significant costs on the firm, including the compliance burdens, risks and costs associated with the safe-keeping and management of personal information about their clients. We further submit that no regulatory purpose would be served by the collection of this additional KYC information as the OEO Firm cannot use any of that information to assess investors' needs or to provide investment advice. For these reasons, we recommend that the CSA add an exemption from proposed section 13.2(2)(c) of NI 31-103 for OEO Firms, as well as exemptions from related KYC requirements such as proposed section 13.2(3.1) and section 13.2(4.1) of NI 31-103.

(b) SRO rule structure

We recommend that the existing regulatory structure of SRO rules governing suitability requirements should be preserved, to the extent possible, when finalizing the Instrument. Consistent with IIROC's OEO Suitability Exemption, we request that an express exemption from these suitability requirements be added to section 13.3 of NI 31-103 for OEO Firms.

(c) Suitability exemption

In light of the fact that an OEO Firm does not take, recommend or decide on investment action for its clients, we also note that it is inappropriate and potentially misleading to clients to require an OEO Firm to provide a statement to its clients that it must determine that any investment action it takes, recommends or decides on, for a client is suitable for the client. Accordingly, we recommend an exemption from proposed section 14.2(2)(k) for OEO Firms.

(d) Potential unintended consequences of the application of general conflict of interest provisions to OEO Firms

Finally, we note that proposed section 13.4.2 of NI 31-103 requires registered firms, including OEO Firms that do not provide advice, to address conflicts of interest as between registered individuals and clients. The

[1] IIROC Notice 18-0076, April 9, 2018.

generality of this requirement could have unintended consequences for OEO Firms by introducing obligations or creating expectations that are inconsistent with the basis of the offering, which is order-execution-only. We recommend that the CSA limit the conflict of interest provisions contained in section 13.4.2 of NI 31-103 for OEO Firms to matters such as shelf construction (i.e. product offering selection). This limitation aligns with the fact that no advice is given to investors by OEO Firms and their representatives.

2. Tailoring requirements impacting institutional investors (regulation of portfolio management firms)

We believe that certain aspects of the proposed KYC requirements, KYP requirements and requirements to provide training to registered salespersons would not meaningfully benefit sophisticated institutional investors. Rather, these requirements may unintentionally frustrate the investment objectives of institutional investors and would impose significant compliance costs on registrants. Generally, institutional clients include accredited investors and permitted clients which are not individuals.

(a) Enhanced KYC requirements impacting institutional investors

Proposed section 13.2(2)(c) of NI 31-103 requires a registrant to collect detailed KYC information in respect of each of its clients, such as personal and financial circumstances, investment knowledge, risk profile, and investment time horizon. We are supportive of the CSA's goal in the proposed amendments to section 13.2 of NI 31-103 of ensuring that registrants have a thorough understanding of the personal circumstances and investment objectives of their individual clients. However, in our experience, sophisticated institutional investors do not want to provide this information. Furthermore, having this information would not add value to the services we provide to them.

Institutional investors typically have their own internal processes for making investment decisions in accordance with the investment policies and procedures established by the institution itself, including decisions regarding which registrants to retain to manage particular investment portfolios. In many cases, institutional investors will select a registrant specifically based on that registrant's stated investment strategies and known capabilities and areas of expertise – for example, an institutional investor could select a particular registrant because of its reputation for expertise in the area of liability-driven investments. In many cases, these institutional investors do not wish to disclose information about other registrants they have retained to manage different investment portfolios, the overall size of their assets under management in other investment portfolios, or the investment strategies being applied for the investments held in those other portfolios.

Regardless of whether the institutional investor meets the current definition of a "permitted client" in NI 31-103, we do not believe it is appropriate to apply the proposed KYC requirements to an institutional investor. We note that proposed section 13.2(6) would exempt registrants from the application of proposed section 13.2(2)(c) and section 13.2(4.1) of NI 31-103 in respect of permitted clients in section 13.2(6), provided that the permitted client has waived the suitability determination requirements in writing and the account of the permitted client is not a managed account. We submit that this proposed exemption should be extended to include all institutional clients that provide a waiver of suitability requirements. For purposes of this extension, we propose that an "institutional client" should include any non-individual investor that qualifies as an accredited investor. In support of this request, we note that the securities regulators have previously granted advisers such as TD Asset Management Inc. ("TDAM") exemptive relief from certain requirements of NI 31-103 implementing phase 2 of the client relationship model, including cost disclosure and performance reporting in respect of all accredited investors that are not

individuals. Without the broader exemption from the KYC obligations we are proposing, advisers such as TDAM would be required to request, collect and maintain the additional detailed KYC information prescribed by the proposed amendments from all of their institutional investor clients without any corollary benefit to those clients.

(b) Potential unintended consequences of the application of KYP requirements to advising representatives selecting portfolios managed for institutional investors

Large institutional investors routinely retain advisers to manage investment portfolios or sub-portfolios on a discretionary basis and expect them to execute tailored, complex investment strategies. These investment strategies are determined by the investment policies and objectives of the institutional investor itself, as directed to be applied to each particular portfolio of assets under management. If individual portfolio managers are required to comply with the new proposed KYP requirements of section 13.2.1(4) of NI 31-103, they would not be able to purchase any securities for the portfolios of their institutional investor clients unless those securities have first been designated as approved investments by the sponsoring registered firm of the individual portfolio manager. This will have unintended consequences. The result would be either to deprive the institutional investor of access to those products or to require the sponsoring registered firm to designate certain specialized products as "approved investments" (which may not in fact be appropriate for retail investors or other non-institutional investors, generally). Either of these outcomes is contrary to the intended investor protection objectives of the proposed reforms. As a result, we submit that proposed section 13.2.1(4) of NI 31-103 should not apply to advising representatives when selecting investments for portfolios being managed for any institutional investor that has waived the application of the suitability requirements.

Discretionary portfolio management firms offer varied, segregated solutions to institutional clients. Such offerings may include everything from passive index tracking, active selection of individual stocks and bonds, and more complex derivative mandates. We submit that portfolio managers, as fiduciaries, should continue to preserve their discretion to select suitable investments to meet the specific mandates contracted with institutional clients without an additional, unnecessary and potentially restricting KYP obligation.

Advisers to institutional clients are often required to accept securities from their clients, such as in circumstances where the client provides a portfolio manager with a "sleeve" of securities in exchange for units of a fund (as opposed to purchasing those fund units with cash), or where a client provides an adviser with an existing portfolio of securities to manage on a segregated basis. The new proposed KYP requirements will be problematic in that context, as they will deter advisers from accepting securities in these arrangements if the securities are not already KYP-approved by the registered firm. Requiring an investor to liquidate existing securities to be able to transfer cash into a new account with a new adviser is not in the best interests of investors, as there would likely be tax consequences associated with the liquidation that would not arise if the securities were transferred in kind.

(c) Potential unintended consequences of the application of the proposed suitability requirements to institutional investors

Institutional investors typically determine their own investment guidelines, policies and procedures for specific portfolios or sub-portfolios and often direct their investment managers to comply with them through the terms of the investment management agreement. While the portfolio manager is granted discretion to manage that portfolio or sub-portfolio, the manager must do so within the confines of the institutional investor's stated investment objectives, strategies and constraints. The ability of institutional investors to impose these requirements on their portfolio managers is a necessary component of ensuring

their ability to manage all of their assets held across the institution, and to discharge their fiduciary and other duties to maximize return on investment for their own constituents.

Imposing prescriptive product suitability requirements on an institutional investor's portfolio manager for a particular portfolio or sub-portfolio may unintentionally disrupt the institutional investor's ability to achieve its own overall investment objectives. Contrary to the CSA's stated objective of enhancing investor protection, the result could be to render Canadian institutional investors unable to execute their desired investment strategies, placing them at a disadvantage to their counterparts in other countries.

For example, if a large Canadian pension fund cannot structure its investment portfolios and obtain directed portfolio management services in the same way that it does today, and in the way that pension funds in the United States and other countries will be able to continue to do, the Client Focused Reforms could have the unintended effect of prejudicing Canadian pensioners relative to pensioners in other countries. We note that large Canadian institutional investors often operate globally and can relocate pools of capital for investment purposes to branches or subsidiaries outside Canada. A Canadian pension fund may choose to place its assets under management with non-Canadian advisers who are not subject to the sort of suitability constraints that are being proposed under the Client Focused Reforms. We further note that, rather than relocate capital outside Canada, institutional investors in Canada may instead choose to hire non-Canadian advisers operating in Canada under the "international adviser" or "international sub-adviser" exemptions in NI 31-103, who will not be subject to the prescriptive suitability requirements of the Client Focused Reforms.

Canadian investment advisers are currently able to compete with other investment advisers globally to manage portfolios or sub-portfolios of non-Canadian institutional investors. However, their continued success in marketing their services globally could be impeded by the new proposed suitability constraints.

For the above reasons, a further unintended consequence of the Client Focused Reforms may be to render Canadian advisers uncompetitive globally. If Canadian advisers are unable to compete for the business of large institutional investors both in Canada and around the world, this would have the unfortunate effect of undermining the Canadian financial services industry without a demonstrable offsetting investor protection or market efficiency benefit.

Accordingly, we again urge the CSA to consider providing an exemption from the suitability requirements of proposed section 13.3 of NI 31-103 in the context of the provision of portfolio management services to institutional clients.

(d) Differentiating the obligation to provide training between advising representatives and dealing representatives

We note that proposed section 3.4.1 imposes an obligation on registered firms to provide training to its registered individuals, subject to an exemption for registered individuals of an investment fund manager acting in their capacity as such. The proposed obligation to provide training does not distinguish between individuals who are advising representatives and those who are dealing representatives. Advising representatives are subject to significantly more onerous proficiency requirements than are dealing representatives, particularly in their capacity as portfolio managers with a fiduciary duty. In our view, requiring advising representatives to meet the prescriptive training requirements in proposed section 3.4.1 would provide no incremental benefit to investors.

We recommend that the CSA limit the application of section 3.4.1 to dealing representatives as they are subject to less extensive proficiency requirements than advising representatives.

3. Tailoring the KYP proposals to minimize unintended consequences

We propose several modifications to the KYP proposals that we believe would minimize unintended adverse consequences to investors and avoid unnecessary compliance costs for registrants without compromising the underlying policy objectives of the proposals. We wholly support the obligation of registered individuals to know the products that they recommend to their clients. We caution, however, that requiring registered firms to know all products prior to making a product available would create significant unintended consequences, including the firm's ability to manage its product offerings to meet the needs and expectations of its clients.

(a) Removing KYP obligations for transfers in and client directed trades

Pursuant to section 13.2.1(6) of NI 31-103, the proposed enhanced KYP provisions will apply to a registered firm that accepts a transfer of assets into the adviser's account from another account. The application of the KYP provisions to a "transfer in" of securities already beneficially owned by a client will have the unintended effect of frustrating transfers of securities between firms to consolidate investor holdings. We submit this is contrary to the interests of investors. The adviser for the transferee account may not have gone through the KYP institution-level approval process for the securities being transferred. The application of the new KYP requirements in the circumstances of a "transfer in" is exacerbated by the detailed, documented analysis that is prescribed as part of the process of firm-level KYP approval of a new product. We submit that transfers-in should continue to be permitted with a related discussion between an adviser and client as part of the suitability review.

Section 13.2.1(6) introduces a new requirement for a registered firm to undertake a full analysis of each security a client proposes to transfer from holding at another firm to an account with the registrant before it can be accepted by the registrant. Among other things, this requirement is problematic from a client service perspective, as it effectively temporarily freezes the client's securities while the firm evaluates them. Alternatively, a client may be required to liquidate its holdings to transfer cash if those securities are not capable of being held by the receiving firm, which may create negative tax consequences for the client. The evaluation process will require some time to complete, and if there are any changes in the value of the securities or other events in the market during the period that the evaluation is being conducted, the client's interests could be significantly prejudiced.

We also note that the enhanced KYP provisions will apply to advisers executing a client-directed trade of a security if such security has not been KYP-approved by the firm, even if the client is a sophisticated institutional investor. The result is the imposition of unnecessary restrictions on the ability of investors to direct investments in a non-managed account. We submit this is contrary to the interests of investors.

We therefore recommend that the CSA provide exemptions to registered firms from the proposed KYP requirements for (a) securities already owned by the investor and being transferred into an account with a new adviser; and (b) purchases of specific securities at the direction of the client for which no investment advice, recommendation or endorsement of the adviser has been sought or given.

(b) Modifying the firm-level KYP approval process

We submit that the interests of investors are better served by requiring investment returns to be considered by advisers in the context of their recommendations to clients. The requirement for investment returns to be considered as part of a firm-level KYP process is misplaced. Including returns in the firm-level KYP approval process risks reinforcing short-termism and may lead to unintended negative consequences for investors as described below.

- The appropriate time horizon for considering investment returns is specific to individual investors and their investment strategy. A uniform approach at the firm level is contrary to interests of investors and may inadvertently reinforce short-termism. Furthermore, different adviser firms may take different approaches to the relevant time-period to apply for this purpose. This, or other differences in the application of the KYP analysis from firm to firm, may result in clients of one adviser firm having access to different or more limited product selection than clients of another adviser firm.

- A prescribed time period for performance assessment that is applied across all product types will not take into account market cycles and the inherent difficulty of making peer group comparisons for certain types of investment products under varying market conditions, or even selecting the appropriate peer group for comparison purposes. For example, in an extended period of positive market returns, growth funds typically outperform value funds. An assessment of the merits of a growth fund relative to a value fund could lead to the decision to remove the value fund from KYP approval, at a time in the market cycle when the value fund may be a superior investment to the growth fund despite having experienced lower returns than the growth fund over the measurement period.

- There is a significant risk that mandating performance criteria as part of KYP will stifle new product development. New investment products will not have a performance track record, which will potentially disqualify them from inclusion on a registered firm's shelf. Investment funds also typically must have a minimum unitholder base to qualify as eligible investments for a registered plan. The lack of performance data could result in that investment fund not being able to achieve the required unitholder base for inclusion in registered plans.

- A focus on investment returns may create disincentives for the industry to pursue new product development, due to the risk that adviser firms may not add the product to their KYP-approved list because its novelty makes it more difficult to assess returns.

- New products that may otherwise be suitable investments for KYP approval which are introduced during a period of market instability, political crisis or during a period that market activity is anomalous for any reason may not be able to obtain firm-level KYP approval during that abnormal period, when its investment return cannot be monitored without distortion by extraneous events.

- An adviser firm may become required to remove specific securities, or product types, from its previously KYP-approved product offering to clients if return levels change over time. It is not clear what implication would follow if a previously approved product that is held in an investor's portfolio with an adviser ceases to be KYP-approved by that adviser. Would the investor be required to liquidate that investment? Or transfer it to an account with a different adviser where it remained KYP-approved by that other institution?

- It is axiomatic in the investment industry that past performance is not necessarily indicative of future returns.

For all of these reasons, we submit that the firm-level KYP process proposed in section 13.2.1(1)(a)(i) of NI 31-103 should be revised to remove the reference to returns as a relevant criterion for making a product available to investors. We propose that the existing responsibility of an adviser to assess suitability of investments for their clients already requires the adviser to take considerations of returns into account to a sufficient degree, without precluding all advisers within a registered firm from making a particular investment product available to the firm's clients due to the difficulties and uncertainties inherent in an assessment of returns.

(c) Tailoring the KYP process to product types

We submit that different factors should be relevant to the KYP firm-level assessment depending on the product type, and that such factors should be applied consistently over time to ensure a stable product shelf for the benefit of investors. We propose that the Client Focused Reforms specifically recognize that different considerations should be applied to:

- **Manufactured products:** In this category, we include products such as mutual funds, ETFs, structured notes and GICs. For these types of products, we recommend the CSA consider requiring the application of a common set of criteria to meet KYP obligations. This could include setting minimum standards for product cost, embedded compensation, risk rating, liquidity, leverage and redemption costs. At the time of onboarding new products and on an annual basis, we recommend that the registrant consider non-performance metrics such as operational capability, custody, auditor engagement and assets under management to determine whether the products offered by the issuer should continue to remain KYP-approved. This comprehensive due diligence approach aligns with our existing commitment to clients to ensure a careful review of manufactured products prior to inclusion on our product shelf.

- **Capital Market Products:** In this category, we include fixed income securities, equities, derivatives, and preferred shares. We submit that requiring an adviser to review <u>all</u> listed securities (Canadian and U.S. listed) for KYP-approval purposes does not meaningfully serve the interests of investors. Requiring such a review and assessment, and allowing (or effectively requiring) advisers to determine that a particular issuer's security should not be KYP-approved, could also have the unintended and undesired consequence of crippling the issuer's ability to raise capital. To avoid this result, or precluding clients of a particular adviser to have access to all publicly traded capital market products without having to select a different adviser that has reached a different KYP-suitability determination regarding a particular security, we recommend that the KYP assessment for capital market products should be made on the basis of objective and transparent criteria that should lead to consistent suitability determinations by all advisers. Namely, capital market products should be dynamically risk rated and monitored at the household or account level to ensure that the aggregate portfolio holdings align with the client's risk profile.

4. Managing conflicts of interest arising from proprietary offerings

(a) Clarifying the guidance involving independent evaluation of controls for proprietary offerings

Although we are generally supportive of the proposed conflict of interest controls for proprietary offerings, whether through proprietary only offerings or through a mixed offering of proprietary and third-party products, as outlined in the Companion Policy, the scope of such controls is unnecessarily broad. More specifically, we submit that the interests of investors are not meaningfully advanced by requiring registered firms to obtain independent advice on, or an independent evaluation of, the effectiveness of the firm's policies, procedures, and controls to address this type of conflict. Requiring registered firms to be squarely responsible and accountable for managing conflicts of interest with appropriate policies, procedures and controls is sufficient.

Within an affiliated group, a registered investment fund manager and its affiliated registered dealer necessarily take a highly integrated and collaborative approach to client service and product development, taking into account the needs of the full organization's client base. We do not believe that a third-party consultant or adviser would be beneficial to an investor or be able to add value to developing or assessing the affiliated group's policies, procedures and controls to address potential conflicts of interest between the affiliated firms.

In our view, independent consultants should not become surrogates or replacements for the role and responsibility of the registered firm to assess its own policies, procedures and controls and to manage its conflicts. Adding an independent consultant review will simply result in a "form over substance" conflicts process.

We believe the other examples of controls set out in the Companion Policy for firms are sufficient to address potential conflicts.

(b) Preserving the materiality threshold when disclosing conflicts

In the absence of a materiality threshold, the proposed requirement to consider and disclose conflicts of interest is vague and may be disadvantageous to clients. Consistent with existing SRO guidance[2], we support maintaining a materiality threshold for conflicts of interest disclosure. In the absence of a materiality threshold:

- To reduce compliance risk, registrants may be driven to make extensive disclosure about conflicts of interest, or potential conflicts of interest, that are not material to investors. As a result, material conflicts of interest may no longer be clearly identified and sufficiently highlighted for clients.

- Registrants may unfairly and inappropriately become subject to increased regulatory and litigation risk for failing to identify immaterial conflicts of interest, or for failing to resolve such immaterial conflicts of interest in favour of the client.

We also urge the CSA to provide guidance on the form that conflicts of interest disclosure should take and the level of detail that should be presented. The Companion Policy currently proposes that firms should apply their discretion in determining the level of detail of conflict of interest disclosure, regarding both the

[2] IIROC Rule 42.

nature of the conflict and the manner in which it has been addressed. We are concerned that investors at some firms could be prejudiced relative to investors at other firms, if different firms take different approaches to the manner in which conflicts and resolutions are disclosed. Instead, we believe it would be preferable for the CSA to provide guidance that will set an industry-wide standard for this disclosure. We note that our concern regarding the potential prejudice to investors of divergent approaches to this disclosure requirement among registrants is exacerbated by the absence of a materiality threshold, as firms will be left to their own discretion regarding the appropriate extent of disclosure to make for a spectrum of conflicts ranging from material to immaterial.

(c) Disclosure of proprietary-only offerings

The Companion Policy guidance addressing firms that only offer proprietary products proposes that such firms should consider stating whether non-proprietary products would be better, worse or equal in meeting the client's investment needs. We submit that the disclosure currently made to clients cautioning them that the firm only offers proprietary products already provides sufficient cautionary disclosure to investors regarding the scope of the firm's product offering, and that investors would not have any reasonable expectation that the registrant should provide an assessment of its proprietary products relative to third-party products that it does not offer.

(d) Remediation period

It may take registrants some period of time to identify all existing and reasonably-foreseeable non-material conflicts of interest, and to consider, develop and implement appropriate resolutions of all conflicts of interest. We therefore request that, if for any reason the CSA determines not to adopt a materiality threshold as we have proposed, the CSA should alternatively revise sections 13.4.1, 13.4.2 and 13.4.3 to provide for a reasonable timeframe both for the identification and resolution of conflicts of interest.

5. Additional comments regarding KYC requirements

In addition to the comments already provided in this letter regarding the application of the proposed expanded KYC requirements to OEO Firms and institutional investors, we offer the following comments for your consideration:

- **Tailoring the KYC process**: We recommend that the CSA provide greater flexibility to registrants to tailor their KYC processes beyond the specific examples set out in the Companion Policy to account for evolving business models, technology and investor demand. For example, we recommend increased flexibility to modify and develop the KYC requirements to reflect advances in technology, and to address the specific circumstances of investment adviser with a technology-assisted business model (i.e. robo adviser).

- **Client confirmation**: We observe that an adviser must rely on the information provided by the client to satisfy its KYC requirements, particularly in respect of information regarding the client's personal circumstances (section 13.2(2)(c)(i)). We submit that an adviser should not be expected to verify personal circumstances beyond the responses provided by clients.

- **Application of KYC requirements to separately managed accounts:** We request that the CSA clarify whether the obligation to collect KYC information no less frequently than every twelve months for managed accounts is intended to apply to separately managed accounts ("SMAs") in which the client contracts with an adviser to invest in an SMA that is managed by a third-party. An

SMA account is akin to a non-managed account as the client directs the desired investment strategy and objectives for the account, and the adviser then manages the account as a stand-alone portfolio in accordance with the client's directions. We recommend that the client's KYC information should only be required to updated for such SMA accounts on a three-year cycle, consistent with the updating requirement for non-managed accounts.

- **Completing updates to client KYC information:** We recommend adding the phrase "within a reasonable time" to the end of section 13.2(3.1) to permit registrants flexibility to obtain the client's confirmation of the accuracy of information required at account opening and for subsequent significant changes.

- **Transition period for existing clients:** We request that the CSA clarify whether, or to what extent, the proposed enhanced KYC and KYP requirements are intended to apply to the existing investment accounts of existing clients. If it is intended that these proposals will apply to such existing accounts, we submit that the contemplated transition period does not provide sufficient time for advisers to contact their clients to obtain the required additional KYC information or to update existing KYC information. Specifically, for existing clients, we propose that the CSA should provide a 3-year transition period for all existing clients, to align with the 36-month transition period proposed for managed accounts.

- **Client education piece by regulators:** IIROC has developed a brochure entitled "Opening Your Retail Account" which provides useful and informative assistance to retail consumers. The CSA may wish to consider developing similar publications aimed at investor education explaining the new expanded KYC and suitability regimes to help them understand why additional information is now being required of them by registrants governed directly by the CSA members.

6. Suitability

(a) Removing guidance to collect information about accounts held at other registered firms

The Companion Policy calls for registrants to inquire about the client's investments with other registered firms as part of making its suitability determination. We anticipate that both retail and institutional clients will object to providing information to one registrant about investments held with other registrants, both for privacy reasons (in the case of retail clients) and to protect proprietary information and investment strategies (in the case of institutional clients). Further, even if clients agree to provide such information at the outset of opening an account with a registrant, we foresee tremendous difficulty in keeping information about holdings with other registrants current, and the potential for misleading clients about the extent to which one registrant's investment strategy will be integrated with those of other registrants managing separate investment portfolios.

These concerns are magnified in the context of registrants that only offer proprietary funds. Such registrants should not be expected to conduct an analysis of portfolios held with a different registrant, as they will most likely lack familiarity with those investment products, given the number and range of competitive products in the current marketplace. Further, it is unclear to what extent a registrant must take into account investments held with other registrants as part of its own suitability analysis and recommendations. Accordingly, we recommend removing the statements in the Companion Policy proposing that registrants should inquire about holdings with other registrants, and instead allow clients to make their own decision regarding whether to disclose information about holdings with other registrants, which information would then be weighed by advisers as they see fit in the circumstances.

(b) Account type suitability

The suitability requirements appear to impose an obligation on registrants to consider what type of account is appropriate for the client on an ongoing basis. For example, a registrant would be obligated to continually reassess whether a fee-based account or a transactional account is more appropriate for each client. In addition to the cost and complexity of revisiting this assessment on an ongoing basis, we note the following problems with implementing the proposed requirement:

- **Limited account offerings**: Certain firms only offer fee-based accounts and are not in a position to provide alternative accounts or make a meaningful assessment regarding the appropriate account type. Accordingly, we submit that requiring account type reassessment as part of ongoing suitability requirements is inappropriate. Alternatively, we submit that an exemption from any account-type reassessment requirement should be provided in respect of managed accounts for which only fee-based arrangements are permitted.

- **Multiple account transitions**: We submit that imposing an obligation on registrants to monitor the appropriateness of the type of account held by a client may result in the client being transitioned back and forth between different types of accounts based on factors that fluctuate in the short-term, which would be contrary to the client's best interests. For these reasons, we recommend that account type appropriateness should be determined only once, at the account opening stage, in consultation with and based on considerations discussed with the client.

(c) Seeking clarity regarding CSA expectations of what constitutes a "reasonable basis"

The suitability determination and related investment recommendation is premised on a registrant's reasonable basis for determining that the action is suitable for the client. We urge the CSA to provide greater clarity regarding what factors should constitute a "reasonable basis" for making suitability determinations, particularly given the overriding requirement that registrants must, in all cases, put the client's interests first. We suggest that guidance should be provided to clarify that a registrant would have a "reasonable basis" for making a determination if it has followed specified KYC procedures and taken into account the KYC information provided by the client, the registrant's knowledge of the recommended investment and available alternatives, and the assessment of the cost associated with the specific product.

(d) Tailoring portfolio concentration requirements

Proposed section 13.3(1)(a)(v) of NI 31-103 requires registrants to conduct a review of the overall concentration and liquidity of the client's accounts with the registrant when conducting a suitability analysis. Some clients, for privacy or other reasons, prefer not to provide account information about accounts held with one business unit of the registrant to any other business unit of the registrant. We propose that the requirement to assess concentration and liquidity across all accounts held by a client with a single registrant should not apply in circumstances where the client objects to allowing account information to be shared throughout the registrant's multiple business units.

(e) Seeking clarity regarding client suitability vs account suitability

It is unclear whether the CSA is proposing that suitability determinations should be made with respect to the client generally, or only with respect to a specific account of that client. Proposed section 13.3(1)(a) refers to a registrant determining whether a particular action is suitable for the *client*. However, proposed section 13.3(2) indicates that the registrant must review the client's *account* to determine suitability if

certain triggering events occur. We submit that the suitability requirement should be applied with respect to specific accounts, rather than to the client generally, as different accounts held by the same client will each have different investment objectives or strategies. Further, some accounts are entirely client-directed, such as accounts held with an OEO Firm. Finally, as noted above, a true client-level suitability determination is impractical, if not impossible, as it would require full information regarding all investment assets held by the client across multiple registrants, and in each business unit within the same registrant. For these reasons we propose that the Companion Policy should by revised to clarify that suitability assessments are to be made with respect to suitability of the investment for a specific account of the client.

(f) Timing of suitability analysis

Section 13.3(2) references conducting a suitability determination "promptly" after certain triggering events have been communicated to a registrant. We submit that a reasonable time-period is needed for a registrant to complete a suitability review and are concerned that the concept of "promptly" may be viewed differently by regulators and registrants. We request that the CSA add guidance to the Companion Policy indicating that a suitability review may occur within 90 days of a triggering event to enable the registrant to consider the specific event, discuss appropriate action with the client and, if approved by the client, to take such action.

7. Referral Arrangements

In response to the CSA's notice seeking commentary on structures for referral fee payments, including one-time payments, we caution the CSA from prescribing the structure of referral arrangements and would welcome the opportunity for further discussion. We highlight two specific instances below which may result in negative unintended consequences to investors.

(a) Permitting referral arrangements between affiliates

As proposed, section 13.8(1)(a) of NI 31-103 prohibits payment of a referral fee from a registered firm to an affiliated entity that is not a registrant. However, many large financial services institutions such as TD Bank Group currently encourage their various businesses to refer clients of a non-registrant business unit to an appropriate registrant able to meet their needs for investment advice. For instance, the retail and commercial bank staff routinely refer their clients to a portfolio manager or investment dealer for investment advisory services.

To prohibit these types of affiliate referral fee arrangements may reduce appropriate incentives to refer clients to seek investment advice from registrants and result in investors not accessing the appropriate range of investment products and advice to address their investment goals. We submit that proposed section 13.8(1)(a) should be revised to allow a registered firm to provide referral fees to its own affiliates within the same organization that are not registrants. This approach would promote the CSA's stated goal of encouraging individuals to be referred to investment professionals for advice regarding their investment needs, while avoiding the potential abuses that could occur if referral fees were permitted to be paid to third parties who make referral recommendations and are not themselves registrants.

In other instances, a client may be referred from one advice-based channel to another advice-based channel based on a client's changing needs and circumstances. For example, a client may open a basic RRSP account when first starting her or his career, but later benefit from personalized, full-service investment advice after five or ten years in the workforce. It is in the best interests of investors to be referred to the business unit within an affiliated group that is best able to serve their current needs, which may change over

time, and for the business unit holding the client relationship to be appropriately incentivized to make internal referrals to the appropriate business unit.

(b) Permitting referral arrangements with certain specified professionals

We submit that it should remain permissible for referral fees to continue to be paid to specified types of professionals, such as accountants and lawyers, to ensure that the clients of those professionals are referred to registrants who can advise them appropriately with respect to investment matters. This approach would help to further the CSA's objective of ensuring that clients are served by qualified registrants.

8. Unintended consequences of KYC and KYP requirements

We are concerned that the proposed expanded KYC and KYP requirements could have unintended and undesired consequences that are not proportionately offset by the benefits that will actually accrue to investors as a result. These include: increasing the cost of advisory services to individual investors due to the additional costs involved in compliance with the new requirements; related costs with potential impacts to the service offering to clients with smaller amounts to invest; decreasing the range of product choices available to investors as a result of the new KYP requirement for products to be approved by the registered firm before they can be recommended by individual advising representatives; the potential for industry consolidation in response to increased compliance costs; and the possibility that fewer Canadians will seek out and obtain the benefits of professional investment advice due to privacy concerns and reluctance, or discomfort, with providing their personal financial circumstances to advisers.

9. Application of the Client Focused Reforms to OTC Derivatives Dealing and Advising

It is our understanding that the Client Focused Reforms are not intended to cover advising and dealing in derivatives and that separate derivatives-registrant instruments are being developed.

If the CSA intends the proposals to apply to dealing and advising in derivatives (including OTC derivatives), we submit that further clarification is required and additional public consultation is necessary to ensure fulsome comment and consideration by impacted stakeholders.

10. Transition Period

Implementation of the Client Focused Reforms will impact numerous systems, internal policies and procedures ranging from client onboarding to product recommendations and client engagement practices. The systems necessary to enhance our capabilities to implement the proposed reforms, the redesign of our operations and the development of the new required compliance procedures will demand extensive resources. Projects and initiatives of this scope and scale involve resources that are scheduled on a multi-year basis. This project will require careful planning, including an enterprise-wide reprioritization of projects and initiatives that are already underway. Developing new functionality in legacy systems and processes is costly and time consuming and, in some cases, may not be technologically feasible, potentially resulting in the need to transition to entirely new systems. For example, a more extensive conflicts management system for our advisers across our wealth lines of business will be needed.

To provide context for our comments on the need for an appropriate transition period, we highlight several specific challenges posed by implementing the KYC aspects of the Client Focused Reforms:

- from a client experience perspective, the requirement to collect more detailed information regarding personal financial circumstances will involve a significant change as clients will be asked to share what they may regard as sensitive personal information with registered individuals;

- from a registered firm perspective, we will have to apply the new KYC requirements to existing client accounts, which will take a significant amount of time. To provide context, our registered dealer offering only proprietary products has approximately 2 million existing accounts. Implementation will require adapting our existing systems to satisfy the new requirements, followed by a significant outreach exercise to contact our existing clients; and

- to address the additional KYC requirements in our advisory businesses, we will have to implement changes not only to our physical account application and information change forms, but also to a number of our data processing systems, including the systems we maintain for client-facing accounts, our employee facing systems and ultimately the databases maintaining client information. Advisers will also face a significant outreach initiative to contact and obtain information from existing clients.

There are significant technical and logistical considerations which add to the complexity of implementing the new KYC requirements, including the design of quality assurance review and controls for implementing new suitability assessment procedures, account opening documentation, assessment of changes in client circumstances, ongoing suitability review procedures and integration with existing trade surveillance and monitoring programs.

The implementation time schedule currently proposed in the Client Focused Reforms will not provide firms and advisers with sufficient time to modify existing systems and processes, develop new systems and processes, and train advisers and applicable staff on the numerous, complex changes set out in the Instrument. Furthermore, time will be required for testing the new systems once designed and implemented, as well as time required for further modifications to address any deficiencies identified through such testing.

For example, as proposed, registrants will be required to comply with the new referral arrangement provisions immediately upon the Instrument coming into force. As rule amendments typically come into force three months after final publication, registrants will only have three months from the final publication date to incorporate the new requirements, as published in final form, into their referral arrangements. We do not believe that will be enough time to develop, implement, test and refine the required systems changes.

Also, we note that certain of the changes proposed by the Client Focused Reforms will require complimentary or conforming rule changes by self-regulatory organizations ("SROs"), and it will not be possible to finalize the design of the required systems changes by registrants until those rule changes have been published, further delaying the implementation process.

Given the scope, significance and complexity of the Client Focused Reforms, we argue that a longer transition period, with an opportunity for meaningful consultation with securities regulators and SROs, is necessary. To effectively operationalize the required changes, registrants require the final rules, including related SRO rules, before beginning implementation to ensure alignment of technical and logistical specifications with regulatory requirements. We recommend that the CSA take the following considerations into account with respect to a proposed implementation schedule and transition period:

- The period that registrants are given to complete implementation of the Client Focused Reforms should only begin to run **after** all related SRO rules are published in final form, including any related guidance;

- An additional period of at least 18 months should be provided for compliance with the new KYC, KYP and suitability rules; and

- Given the complexity of the **conflicts of interest** proposals, and the likely need for regulatory input on the design of the conflict management system, adding 2 years to the proposed implementation schedule.

We appreciate the opportunity to provide comments on the proposal. We believe the CSA has identified important investor protection goals in the Client Focused Reforms and we are supportive of this effort to improve the current regime. However, we also believe that deliberation and care must be taken in modifying the current proposals to minimize the unintended consequences for investors and to ensure the vibrancy of Canadian capital markets.

We welcome the opportunity to provide additional detailed commentary through in-person discussions with CSA staff.

Sincerely,

Leo Salom
Group Head, Wealth Management and TD Insurance