

# Wealthsimple

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## DELIVERED BY EMAIL

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British Columbia Securities Commission  
Alberta Securities Commission  
Ontario Securities Commission  
Autorite des marches financiers  
Nova Scotia Securities Commission  
Manitoba Securities Commission  
Superintendent of Securities, Nunavut

Financial and Consumer Affairs Authority of Saskatchewan  
Securities Commission of Newfoundland and Labrador  
Financial and Consumer Services Commission of New Brunswick  
Registrar of Securities, Yukon Territory  
Registrar of Securities, Northwest Territories  
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

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**Re: Proposed Amendments to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("NI 31-103") and to Companion Policy 31-103CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("NI 31-103CP") – Comment Letter**

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Dear Sirs/Mesdames,

Wealthsimple Inc. ("**Wealthsimple**") is registered as a portfolio manager throughout Canada and specializes in the delivery of investment advice directly to investors through its online investment management portal. We appreciate the opportunity to comment on the Proposed Amendments to NI 31-103 and NI 31-103CP (the "**Proposed Amendments**").

### **What is Wealthsimple?**

Wealthsimple's mission is to make high-quality financial services, including investing, accessible to everyone. We believe that access to financial products and services is crucial for helping people attain financial autonomy and achieve the lives they want for themselves and their families. We make our services accessible by keeping barriers to entry low: no minimum account size, a quick and simple sign-up process, financial concepts and products explained in everyday language, and low fees.

Since we launched in September 2014, over 100,000 clients have come to trust Wealthsimple with over \$3 billion in assets. Our approach to developing products is client-driven: we develop a "minimum viable product", test it with a small group, and then improve it based on data and real-world feedback from users. This ensures we're building solutions that people want and that add value to their financial lives, and it improves the efficiency of our business.

Wealthsimple currently offers automated investing in standard, socially responsible, and Shariah-compliant index-based model portfolios, and Smart Savings, a portfolio managed account that selects the highest available deposit rates for clients. In the near future, Canadian ShareOwner Investments Inc., Wealthsimple's affiliate, will launch *Wealthsimple Trade*, a mobile version of its order execution only business. Wealthsimple Advisor Services Inc. will launch *Wealthsimple Advisor Services*, its mutual fund dealer business, which will allow traditional registered financial planning professionals the ability to use Wealthsimple's portfolio management and innovative

technology to deliver effective solutions for their clients.

### **Summary of Comments**

Wealthsimple fully supports the goals of the Proposed Amendments, including focusing on client outcomes rather than individual transactions, transparency, and resolving conflicts of interest in the best interest of the client. These goals are aligned with Wealthsimple's company mission, and we have created innovative solutions to achieve these same objectives.

While we are fully supportive of the desired outcomes, we are concerned that some of the proposals, particularly when applied to innovative, technology-based businesses like ours, may not advance these goals, but rather may in fact set them back.

We are concerned that the restrictions on referral arrangements in the Proposed Amendments will make it more difficult for Canadians to connect the financial planners they choose with the low-cost solutions they need, rather than improving Canadians' access to professional financial planners, qualified investment advice and low-cost investment solutions.

We are also concerned that the prescriptive Know Your Client (“**KYC**”) requirements in the Proposed Amendments will not demonstrably improve registrants' suitability review and may in fact prevent providers from developing KYC processes that will result in better outcomes. In our view, prescriptive requirements in the Proposed Amendments to NI 31-103CP will impair innovation and make it harder for Wealthsimple to use its experience to continuously improve how it gathers its clients' KYC information to determine suitability. This will stifle innovation and not advance the investor protection objective.

While the Proposed Amendments explicitly describe what exempt market dealers, mutual fund dealers, investment securities dealers and portfolio managers must do in order to comply with NI 31-103, the Proposed Amendments do not explicitly distinguish between all of the businesses models that currently exist, cannot contemplate business models that may be created in the future, and most importantly, do not explicitly provide registrants the latitude to seek alternative methods that are proportionate to the simplicity (or complexity) of the investment solutions offered.

Finally, we are concerned restrictions on referral fees in the Proposed Amendments may have the unintended effect of eliminating common, low-cost marketing channels for online providers. Increasingly, services are sold through peer-to-peer referrals, social media, and partnerships; the restrictions proposed would place the marketing of online securities services needlessly apart from all other industries. We agree that referral arrangements should be clearly disclosed but eliminating these marketing channels will limit access of all Canadians to low cost online solutions — simply because they will never learn about them.

Overall, we respectfully submit that the Proposed Amendments are too prescriptive, and where prescriptive, need to specify that registrants can use their judgement to create innovative alternative solutions to achieve better outcomes for clients. We have proposed an alternative approach to referral arrangements and request that the Canadian Securities Administrators (the “**CSA**”) review these alternatives and re-issue the amendments for future comment before inclusion as a final amendment to NI 31-103.

## Specific Comments

### *Prescriptive Requirements and the Best Interest Standard*

As a portfolio manager, Wealthsimple is a fiduciary<sup>1</sup>. We wear that title with pride because it means that our clients can put their trust in us. We must earn that trust by adhering to high ethical and professional standards. The fiduciary standard is a principle that focuses on the outcome, not the process.

Accordingly, we support the CSAs' effort to introduce a practical application of a best interest standard through the Proposed Amendments, so long as it only applies to registrants who are not already fiduciaries. We agree with the position of the Portfolio Managers Association of Canada that prescriptive requirements for KYC, Know Your Product, Suitability and Conflicts of Interest in the Proposed Amendments should only apply to registrants who are not already fiduciaries.

We are also concerned that prescriptive standards will make it difficult for an innovative portfolio manager like Wealthsimple to use technology to meet its best interest standard. The application of prescriptive requirements can be a barrier over time for firms like Wealthsimple that want to innovate, adding considerable cost and time. For any online business model that relies on agility and the ability to iterate (make quick incremental changes), delays and cost will hamper innovation, reduce efficiency, and hamper Canada's ability to be a global hub for FinTech leadership.

Many of the comments in NI 31-103CP suggest that registrants should not tailor the KYC questionnaire to match the investment strategies offered. We respectfully disagree: A professional portfolio manager should be able to choose the information it needs in order to determine suitability.

For example, the proposed amendments to section 13.2 of NI 31-103 have added a requirement to collect a client's personal circumstances and in the proposed amendments to the NI 31-103CP, the information required in order to determine personal circumstances includes: civil status or family situation, number of dependents, and occupation. Wealthsimple tracks how much a client can save each month by asking about the client's net assets, income, and debt and from that data we calculate how much the client can save. Collecting and interpreting a client's marital status and number of dependents will not impact an algorithmic risk score that has already determined how much the client can afford to save.

As a result, in order for a client to invest \$10 in Wealthsimple's Smart Savings account (high interest savings account), the client would have to answer over 30 separate questions including a breakdown of all their assets and the securities they hold with other institutions. It is unclear why these answers are needed in order to open a managed account that only holds bank deposits guaranteed by the Canadian Deposit Insurance Corporation. The Proposed Amendments do not allow Wealthsimple, a fiduciary, the authority to exercise its professional judgement to only ask its clients the questions it determines are necessary to confirm that the investment is suitable.

Wealthsimple's business decisions are driven by data and we encourage the CSA to continue to collaboratively generate data that helps us all go beyond proposing solutions, but that also demonstrates that the identified problems are actually solved by the proposed solution. Similar to the way pharmaceutical firms test new medication, "A/B" testing can compare a small set of investors using the proposed solution against the current approach to demonstrate that a purported improvement is actually successful. We recommend that the Proposed Amendments, especially the prescriptive requirements, be tested against a baseline to evaluate the efficacy of the

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<sup>1</sup> Four provinces (Alberta, Manitoba, Newfoundland and Labrador, and New Brunswick) have a statutory requirement that when advisers or dealers have discretionary authority over their clients' investments, the adviser or dealers must act in the clients' best interests. As discussed in CSA Consultation Paper 33-403: *The Standard Of Conduct For Advisers And Dealers: Exploring The Appropriateness Of Introducing A Statutory Best Interest Duty When Advice Is Provided To Retail Clients* (CSA - 2012), it is the CSA's position that this is consistent with the common law where an adviser or dealer that has discretionary authority over a client's assets virtually always owes the client a fiduciary duty.

## Proposed Amendments.

Ultimately, we believe that the proposed prescriptive KYC questionnaire will result in fewer people seeking online low-cost alternatives, because of the significant additional steps in the onboarding process, and will increase the cost of delivering these services for those who do. We do not see how many items in the proposed prescriptive KYC questionnaire will improve our understanding of our clients or gather information that is relevant to determine suitability.

Accordingly, in order to eliminate the additional cost and complexity of applying for an exemption from these prescriptive requirements, we propose the CSA exempt portfolio managers from the prescriptive questionnaire in NI 31-103CP and allow them to decide which information is needed in order to determine suitability.

### *Conflicts of Interest*

Wealthsimple fully supports using the best interest standard to resolve conflicts of interest because in our view, principled regulation that focuses on outcomes is superior to prescriptive requirements that focus on specific processes. The Proposed Amendments require registrants to assess non-material conflicts of interest. By their very nature, non-material conflicts refer to matters that have no impact on the client or the registrant and may be confusing to apply. We recommend that registrants like Wealthsimple that are already held to a best interest standard, should be exempt from the Conflicts of Interest section of the Proposed Amendments.

### *Referral Fees*

Wealthsimple supports reforms that ensure clients receive value for the fees they have paid, that no client is confused about who is providing them with investment advice, and that securities advice remains the exclusive responsibility of registrants.

We are concerned that the prohibition on paying referral fees to non-securities registered individuals and the lack of a distinction between referral fees and non-securities service fees ("**Service Fees**"), will reduce consumer choice, will encourage registrants to only consider products and services which their registration permits them to sell and will prevent professionals from collaborating with each other in order to deliver an ongoing holistic service, the very type of comprehensive financial planning services the CSA clearly wants clients to receive.

Wealthsimple for Advisors ("**W4A**") is a program that combines Wealthsimple's low cost portfolio management with accredited or professional financial service planners<sup>2</sup> (the "**Planners**") using a Service Fee.

W4A provides clients with transparency of:

- what services Wealthsimple provides;
- what services the Planner provides; and
- how much each will charge for these services,

because we want clients to understand the value, and continuously evaluate the cost, of all the services they receive. We do this because we want clients to have the clearest possible understanding of the services they pay for and we want them to continuously have the opportunity to evaluate the value of these services. Only with full transparency on all parts of the service chain can clients proactively make an educated decision on their supplier relationships. Wealthsimple will continue to build and enhance service components that promote this transparency and that enable consumer choice.

Our concern with the Proposed Amendments on referral fees lies mostly in the broad definition of referral fees, and also, in certain circumstances, in their prohibition. Wealthsimple leverages its digital platform to collect from a client the fees that are investment fees owed for the use of the Wealthsimple digital investment platform and its investment advice, the Service Fees owed to the Financial Planner for the delivery and maintenance of a financial

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<sup>2</sup> Financial planning is a profession. In Quebec, only accredited planners may provide financial plans to the public. Elsewhere in Canada certified financial planners build financial plans for clients. While some planners are registered, if no securities advice is given, no registration is required.

plan and the sub-advisory fees owed to any sub-advising management firm being used for active investment management. Wealthsimple directly remits these fees to external parties in line with the agreements in place with the client and as clearly reported on our client platform.

Where the broad definition of referral fees leaves room for interpretation is around one-time or recurring payments that may be paid to a referring advisor, a planner or a referring organization as compensation for maintaining a financial plan and doing the work in order to match clients with service providers who are integral to a holistic service offering.

We do agree that perpetual payments made to a person or organization in exchange for the referral of a client's business and where the referring party offers no service or ongoing value to the client is not appropriate.

In addition, without a distinction between referral fees and Service Fees, the restriction on the payment of referral fees to registrants that exceed 25% of the registrant's revenue and the ending payment of referral fees after 36 months would make it difficult for Planners to deliver complex financial plans in combination with Wealthsimple's simple low-cost managed solutions. We believe the Proposed Amendments need to explicitly distinguish between a Service Fee and a referral fee in order to ensure that Canadians remain free to choose their own Planner.

The proposed amendments to referral fees were a new addition to the consultation process, and in our view, need more refinement to be effective. For these reasons, we believe that the proposed amendments to referral arrangements should be excluded from the final amendments to NI 31-103 and NI 31-103CP and should undergo a separate consultation process.

### *Marketing*

The internet was founded on collaboration and peer to peer interactions, including allowing users of a service the ability to recommend services to their friends. By expanding the definition of "referral fee" to include non-monetary benefits and prohibiting the payment of referral compensation to non-registrants, friends can no longer receive a fee reduction (or give their friend a fee reduction) if they refer a registrant to their friends. Removal of this low-cost marketing channel will dramatically increase the cost of client acquisition, which will ultimately be passed on to all clients. Currently, referral arrangements need to be disclosed to prospective clients before they agree to the service and we question how prohibiting peer to peer referrals increases investor protection or makes capital markets more efficient.

We believe that the current regime, which relies on clear pre-disclosure of the compensation someone might receive in return for making a referral continues to be the proportionate solution to manage the conflict of interest referral arrangements may create.

It is also unclear whether other market intermediaries such as professional associations, member reward platforms, and non-financial services are also prohibited from receiving a fee for participating in joint marketing arrangements. While large financial institutions may be able to engage in enterprise wide marketing arbitrage (ie use a non-registered co-branded affiliate for referral marketing), smaller players and those without co-branded affiliates will be at a distinct disadvantage and will incur higher marketing costs. These concerns were also raised by Portag3 Ventures GP, Inc.'s October 16, 2018 comment letter. We trust that this is an unintended consequence of the Proposed Amendments and recommend the CSA conduct a more detailed review of the impact the proposed changes to referral arrangements will have on low cost marketing channels before re-issuing changes to referral arrangements for a new round of comments. Accordingly, we also do not believe the impact of this proposal is fully understood and as a result is not ready for inclusion in the final rule.

### **Concurrence**

We have been participated in the creation of, and unless contradicted herein are in substantial agreement with, the Portfolio Managers Association of Canada's comment letter.

### **Conclusion**

Wealthsimple supports the objectives of the Proposed Amendments and believes that with the refinements discussed and reconsideration recommended above, the Proposed Amendments will improve the outcomes of Canadian retail investors.

We believe that the goals of the Proposed Amendments will be most effectively achieved through the regulation of outcomes rather than process. We recommend that before implementation, the CSA test the Proposed Amendments against the current requirements to determine whether the CSA's goals will be achieved.

Thank you for the opportunity to comment on the Proposed Amendments.

Kind regards,

**WEALTHSIMPLE INC.**

(signed) *Michael Holder*

Michael Holder  
Chief Compliance Officer  
Associate General Counsel