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September 30, 2016

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Dear Sirs/Mesdames:

Re: Canadian Securities Administrators
Consultation Paper 33-404 *Proposals to Enhance the Obligations of Advisers, Dealers and Representatives Toward Their Clients*

On behalf of Advocis, The Financial Advisors Association of Canada, we are pleased to provide our comments in regards to the Canadian Securities Administrators' ("CSA") Consultation Paper 33-404 *Proposals to Enhance the Obligations of Advisers, Dealers and Representatives Toward Their Clients* (the "Consultation Paper").

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1. Introduction and Executive Summary

In its introductory remarks to the Consultation Paper, the CSA states "the status quo must change" – and we agree. There are legitimate concerns about the quality of financial advice and the proficiency and conduct of those who purport to provide this advice that need to be addressed.

In our view, however, these concerns cannot effectively be addressed by introducing a myriad of new prescriptive rules; doing so would only create burdensome compliance obligations premised on distinctions (such as proprietary business models, or restricted registration categories) that needlessly segment the market of retail investors. And these obligations would be layered upon an existing structure that is fundamentally outdated: the regulation of advisors remains steadfastly tied to product, being a relic of a time when the advisor was seen merely as a salesperson.

That is simply not the way most consumers view their advisors today. Instead, the primary role of the modern advisor has evolved to offer holistic financial guidance to clients through relationships that last years or decades. Through these relationships, advisors help their clients ensure their financial preparedness for life's milestones. The sale of products, whether mutual funds, other securities or life and health insurance, is a means of helping clients achieve their goals and protecting them from unexpected events.

Further, there are persistent gaps in the outdated securities regulatory framework that put investors at risk. These include the fact that: (i) anyone can call him- or herself a financial advisor and offer "financial advice"; (ii) the product-based structure creates regulatory silos that create arbitrage opportunities; (iii) there is no universal requirement for advisors to keep their knowledge up-to-date; and (iv) there is no effective, industry-wide disciplinary process.

Given these major deficiencies, any attempt to improve investor protection by layering new rules on top of this outdated foundation is doomed to fail. To successfully fulfill our shared investor protection goals, we believe it is time to fundamentally re-think the regulation of financial advice and establish it as a true profession. In fact, the reforms set forth by the Consultation Paper make clear that the CSA already recognizes the importance of the advisor-client relationship – after all, it is the advisor that represents the "face" of the entire financial services sector to most consumers.

Throughout the Consultation Paper, the CSA comments that the reforms will be animated through the advisor's professionalism or judgment – we agree that this is the best, and most practical way, to approach the challenge, as there is no way to capture in any law or instrument all of the nuances involved in the day-to-day decision-making of the client-facing experience. Critical safeguards of the investor experience, including the know your client, know your product and suitability processes, depend on the proficiency, professionalism and judgment of the client-facing advisor.

Unfortunately, the Consultation Paper does not take the logical step of according financial advisors professional standing: the envisioned structure would maintain advisor regulation in the hands of existing regulators and self-regulatory organizations that do not consider advisors to be full

members but rather mere “approved persons” that have no dedicated voice on the boards that steer their fate. Frankly, it is absurd to expect that advisors act as true professionals without giving them professional respect and involvement in their own regulation.

We believe the best way forward is a through a professionalization model, like that enjoyed by professionals in the legal, accounting, medical and other sectors. All retail-facing advisors would be required to be members in good standing of a professional body, whose mandate would be the regulation of financial advisors and the practice of financial advice in the public interest. The body would feature a code of conduct that is enforced through a dedicated complaints and investigations system. Practicing advisors and members of the public would serve on its board and its key committees, including the disciplinary committee.

The professionalization model would better address all of the targeted reforms set forth in the Consultation Paper. The ethical standards set forth by the professional body would inform an advisor’s approach to conflicts of interest, KYC, KYP, suitability and relationship disclosure; the body would establish proficiency and continuing education requirements and recognize key titles and designations to address consumer confusion and the “alphabet soup” problem. It would leverage the real-world knowledge of its members in conduct investigations that determine whether an impugned advisor’s behaviour warrants reprimand.

And professional recognition would be absolutely necessary to make a best interest duty workable. A best interest duty is a professional standard of care meant to ensure that a client receives the utmost in their advisor’s care and judgment, driven by an underlying ethical responsibility to do what is “right” for that client. It necessarily involves subjective assessments that take into account the client’s goals and position, as well as the market conditions known at the time and expected in the future. A determination that a best interest duty was breached carries significant ramifications for the client, advisor, and the reputation of the industry as a whole. Therefore, it should be the professional body that interprets and enforces a best interest duty.

Certain members of the CSA are proposing that the duty be implemented, and compliance therewith judged, by regulators who are distant from the client-facing experience. We cannot support this: given their detachment, provincial securities regulators and existing SROs are not in a proper position to interpret the duty in the context of an advisor’s practice. It would be manifestly unfair to apply a best interest duty to a profession while failing to involve its members in their own regulation. Critically, we draw attention to the fact that there is no other profession, whether it be law, medicine, or so on, whose members are subject to a legal or regulatory best interest duty but who are not involved in its interpretation.

Ultimately, the proposals in the Consultation Paper aim to improve investor protection by entrenching higher ethical norms of behaviour in the representatives that serve them. But rather than focusing on reforms that address narrow areas of perceived concern, the CSA should embrace a higher, overarching standard of professionalism that would permeate through all facets of the advisor-client relationship and would be far more effective than prescriptive rules ever could be in addressing the issues that arise in a rapidly-changing environment.

2. About Advocis

Advocis is the largest and oldest professional membership association of financial advisors and planners in Canada. Through its predecessor associations, Advocis proudly continues over a century of uninterrupted history serving Canadian financial advisors and their clients. Our 12,000 members, organized in 40 chapters across the country, are licensed to sell life and health insurance, mutual funds and other securities, and are primarily owners and operators of their own small businesses who create thousands of jobs across Canada. Advocis members provide comprehensive financial planning and investment advice, retirement and estate planning, risk management, employee benefit plans, disability coverage, long-term care and critical illness insurance to millions of Canadian households and businesses.

As a voluntary organization, Advocis is committed to professionalism among financial advisors. Advocis members adhere to our published Code of Professional Conduct, uphold standards of best practice, participate in ongoing continuing education programs, maintain professional liability insurance, and put their clients' interests first. Across Canada, no organization's members spend more time working one-on-one with individual Canadians on financial matters than do ours. Advocis advisors are committed to educating clients about financial issues that are directly relevant to them, their families and their future.

3. The Need to Professionalize the Advice Sector

We agree that there are legitimate concerns about the quality of financial advice and the proficiency and conduct of those who purport to provide this advice to consumers. These concerns absolutely need to be addressed. But rather than attempting to layer patchwork solutions on an outdated regulatory structure, we believe it is time for a fresh start and for all securities market participants to fundamentally re-think the regulation of financial advice and recognize its evolution into a true profession.

The securities regulatory framework is based on an obsolete understanding of financial advice

The biggest problem with any attempt to modernize advisor regulation by making incremental changes within the existing regulatory framework is that the framework itself is fundamentally outdated – it is a relic of a time when the advisor was seen as merely a transactional salesperson, as a cog in the distribution chain of the large product providers who dealt with retail investors on a discrete basis or maintained only very limited relationships with them.

This is reflected in a regulatory structure that is based on product – insurance, mutual funds and other securities all have their own rules, with surprisingly different requirements and expectations amongst them. The structure maintains a stubborn adherence to the traditional "pillars" of the financial system, each with its own regulators and self-regulatory organizations ("SROs") that stand guard over their respective domains. This structure creates silos that make a financial product's sector of origin a defining characteristic.

But to consumers, these are all financial products, and with continuous product innovation and convergence, it is ever harder for consumers to see the differences between them and unreasonable for industry and regulators to expect them to do so. Consumers have moved beyond the pillar/silo mindset to simply consider whether a particular product, regardless of sector, can help them achieve their financial objectives. According to the OSC's own Fair Dealing Model, "an industry that is no longer product-based becomes problematic, in a way, for product-based SROs."[1]

The role of the advisor has evolved as well. Perhaps once, advisors were primarily the gateway to product. But today, if access to product is all that consumers are looking for, it is far easier to simply transact directly with a manufacturer on the internet. Instead, the primary role of the modern advisor is to offer holistic financial guidance to clients through relationships that last years or even decades. These relationships of trust ensure clients' financial preparedness for life's major events – such as marriage, home ownership, the raising of children, and even death, through trust and estate matters. In fact, in a 2015 survey of investors working with a financial advisor, 88 per cent responded that they see advisors more as advice providers than as salespeople.[2]

The holistic role of the modern advisor is more relevant than ever, as we find ourselves in an economic climate wherein governments, facing their own fiscal constraints, expect Canadians to become increasingly self-reliant so as to not rely on social safety programs that may not be as accessible as they were for previous generations. But the sustained low-interest rate environment has made private saving through traditional "safe" channels, such as bonds and GICs, incapable of providing the returns necessary to finance lifecycle objectives, particularly retirement. Arguably, the greatest risk that consumers face is not losing their money in the marketplace, but running out of money before the end of their lives.

Consequently, retail investors must look to higher yield options, including investments in securities products; once the domain of the wealthy or sophisticated, securities products are now firmly entrenched in the mass market. But securities have not gotten any simpler in response – in fact, product development and diversification has only increased the complexity of the offerings. So professional advisors must have the acumen and ability to understand and explain these products to their clients. After all, it is the financial advisor that serves as the "face" of the entire securities industry – from the regulators, to the manufacturers, fund managers and dealers – to the majority of the public. So now, more than ever, the professionalism of that advisor must be beyond reproach.

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[1] Ontario Securities Commission, *The Fair Dealing Model* (January 2004), http://www.osc.gov.on.ca/documents/en/Securities-Category3/cp_33-901_20040129_fdm.pdf.
[2] Advocis, *Investor Insights on the Financial Advice Industry* (November 2015), http://www.advocis.ca/pdf/Consumer-Voice-2015.pdf.

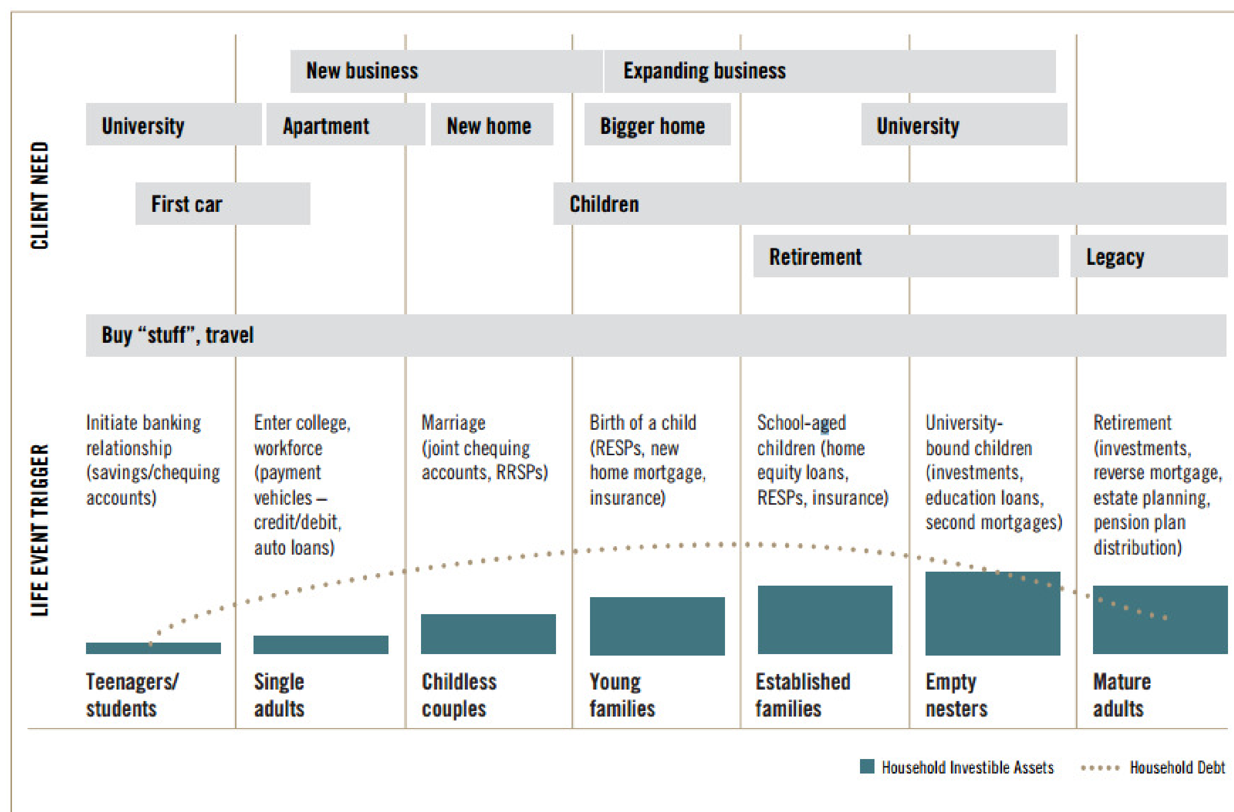

FIGURE 1: THE FINANCIAL ADVICE LIFECYCLE[3]

The existing framework puts consumers at risk

Given this critical role, retail investors should be able to trust that their financial advisors are proficient in core advice competencies, up-to-date in their knowledge, and compliant with the highest standards of conduct and ethics. While many advisors meet these expectations, there are inevitably some who do not – and due to persistent gaps in the current regulatory framework, retail investors are unnecessarily exposed to risk. There are four major sources of this risk:

(i) Anyone can call him- or herself a financial advisor and offer financial advice, including planning.

Across Canada, other than Quebec, anyone, regardless of their training, experience or education, can hold themselves out to the public as a "financial advisor," financial planner, investment advisor, or countless other titles. Neither the title of "financial advisor" nor the scope of the work under that

[3] PricewaterhouseCoopers LLP, *Sound Advice: Insights into Canada's Financial Advice Industry* (July 2014), http://www.advocis.ca/sareport.pdf at p. 116.

title is protected in law, so there is nothing to prevent an unscrupulous, incompetent or merely inexperienced individual from calling themselves a financial advisor and offering what is purported to be financial advice to the public, even if they have no training, experience or financial acumen.

This is a significant risk which must be addressed; time and again, consumer surveys have shown that most consumers mistakenly believe that titles such as financial advisor are regulated and someone holding themselves out as such has earned the right to do so through education and experience. In professional-style principal-agent relationships, consumers routinely put their faith in the title as a proxy for expertise, but unlike doctors, lawyers or architects, anyone can claim to be an advisor or offer financial advice and planning — which leaves the public needlessly vulnerable to incompetence or outright fraud.

(ii) Existing regulation focuses on products, at the expense of proper regulatory oversight on the most critical retail financial relationship — the ongoing relationship between financial advisors and their clients.

As discussed in detail above, much of our existing regulatory framework does not reflect the daily reality of how most consumers access financial advice and planning. Existing regulation is often based on the type of product being sold to the retail consumer. And while existing regulators are adept at regulating their member dealers or brokers, including regulating the constant product innovation in the industry, they do not have a collective focus on the retail consumer's overall advice-receiving experience.

Considering the issue from the consumer's perspective throws the problem into stark relief: many advisors hold multiple licenses which allows them to provide consumers with risk management and wealth solutions from across the insurance, mutual fund and securities sectors. As a practical matter, most consumers do not conceive of the retail financial services industry as structured in such rigid "silos." Nor should they be expected to understand the legal rules and regulatory processes which have produced this model. Instead, consumers work with their advisors to develop holistic financial plans which reflect their circumstances, and not a piecemeal delivery of advice which reflects the regulatory happenstance of how our system developed. Above all, consumers want assurances that their advisors are professional, knowledgeable and accountable, so that their advisor can provide the complete coverage they need.

Most consumers are not particularly interested in knowing that product *x* comes from the insurance universe and product *y* comes from the mutual fund universe. But, in the current regulatory framework which is focused so closely on product sales, it is often the case that the advisor-client relationship is not governed by a single regulatory entity, but by a combination of them. The result is that the protections which consumers do receive vary widely, as they are based on the sector from which the product originates. We have seen the importance of this distinction coming to light if problems arise, leaving consumers confused and disappointed.

We believe that consumers should enjoy the material and psychological comfort and security that comes with knowing that stringent and uniform protective safeguards have been embedded in the

rules and principles which help create and govern their relationships with their advisors. Consumers deserve access to formally professionalized advisor-client relationships which are not dependent on the nature of the underlying products that they purchase to fulfill their financial plans.

Underpinning the advisor-client relationship with a level of professional protection is to accord that relationship a level of legal recognition and protection which is much more fundamental than that offered by product regulation. For example, minimum and uniform standards of ethical and professional conduct and other professional safeguards should be in place across all retail-facing subsectors of the financial services industry. There should be an overarching code of conduct and an industry-wide requirement to maintain responsible levels of errors and omissions insurance.[4]

This sectoral approach also reveals why the existing regulatory framework cannot effectively regulate today's holistic advisory relationships. Certain stakeholders may suggest that regulation of financial advisors should fall under the auspices of existing regulatory bodies, and it is true that in recent years, some have given greater attention to the advisory relationship — for example, through the Client Relationship Model reforms of the CSA. Despite this laudable effort, existing regulators are structurally limited by their jurisdictions of authority; for example, even if an insurance regulator were to completely overhaul its expectations of licensees, those changes would only impact the consumer's relationship in regard to his or her purchases of insurance products — leaving the consumer's experience with mutual funds unaffected.

In an ideal world, all regulators would set comparable standards so that the client would be equally protected, regardless of the product's origination. But a century of experience and general common sense tells us that when you have multiple regulators that were created on the basis of regulating products, not advice, which already have standards that (in some cases) vary widely from each other, coordinating policies on financial advice is nearly impossible. And even if regulators did manage to agree to a uniform set of policies, those policies would do nothing to capture those individuals who are not registered at all, such as a fee-only planner who does not sell product.

(iii) There is no firm, clear, and universal requirement for advisors to keep up-to-date their core areas of knowledge.

One of Advocis' core membership requirements is that advisors keep their knowledge up to date by completing continuing education courses each year, including courses on professionalism and ethics. But for the same reasons discussed above, the regulatory requirements for continuing education are completely variable based on the product's sector of origination. For example, Ontario requires that life insurance licensees commit to 30 hours of continuing education every two years, without requiring a minimum learning component on professionalism or ethics. Several provinces do not have any CE requirements with respect to insurance licensees. And while IIROC has continuing education requirements for registered representatives, the MFDA only states that

[4] Current requirements to maintain errors and omissions insurance vary by province, industry sector and product type.

continuing education "should be provided" to its approved persons.[5] And those advisors who are not registrants with any regulator have no continuing education requirements whatsoever.

An advisor who does not keep his or her level of industry knowledge current is an advisor who fails to properly serve their clients and very likely puts their clients at risk. Moreover, the fields of knowledge with which an advisor should be adequately familiar are continually expanding. Competition in the industry is fierce, so product change and innovation is a constant. Therefore, static knowledge quickly becomes obsolete and impedes the ability of advisors to act in the best interests of their clients. Advocis believes that all individuals who offer financial advice and planning to retail consumers should be required to complete continuing education on a regular basis, with an emphasis on education related to professionalism and ethical conduct.

(iv) There is no effective, industry-wide disciplinary process.

The majority of advisory relationships are beneficial to the public, but some inevitably do not work out as anticipated by one or both of the parties. Sometimes, this is a result of negligence, incompetence or fraud on the advisor's behalf. Accordingly, the industry requires a strong and effective disciplinary process, one which will ensure that those advisors who have committed misconduct are appropriately disciplined, and which will also protect the public and deter other advisors from similar misbehavior.

Insurance regulators, the MFDA or IIROC are each empowered to impose a variety of sanctions, including the stripping from an advisor of his or her license or registration. However, the limitations of the existing product-based regulatory framework become most apparent when considering the gaps which open when one considers the practical impact of having three regulatory authorities investigate and act on matters of discipline: each regulator's enforcement powers are limited to its respective sector.

Suppose, for example, an advisor engages in misconduct so egregious in the course of selling a mutual fund that the MFDA determines he or she is unfit to work in the fund industry and, as a consequence of this finding, it revokes his or her registration. In such a case, there is nothing to prevent this same advisor from continuing to provide advice, and sell segregated funds through his or her insurance license.

We believe this sector-hopping represents unacceptable consumer risk. The type of serious misconduct which warrants an advisor's outright expulsion from one sector, such as fraud or gross negligence, is clearly indicative of that advisor's inadequate commitment to ethical and professional conduct. This is not a sector-specific concern. It is, rather, an industry-wide concern, which is the same as saying that it is a consumer concern.

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[5] On June 22, 2015, the MFDA launched a consultation to consider whether it should require mutual fund dealer representatives to fulfill continuing education requirements. Online at mfda.ca/regulation/bulletins15/Bulletin0644-P.pdf.

Permitting such an advisor to continue to offer “advice” to any consumer is a disservice to the public. And even if that advisor is eventually identified and removed by other regulators in their respective sectors, that person can simply continue offering advice on an unlicensed basis since the scope of work is not protected: for example, he or she could “advise” clients to invest in an affiliate’s Ponzi scheme.

Also, currently lacking is an effective, accessible and industry-wide mechanism through which the public may easily verify their advisor’s credentials and disciplinary history. While several regulators, SROs and industry bodies do maintain websites where the public can search for information on their advisor, the information returned is confined to the particular entity’s sector. As discussed above, the general public does not understand the difference between the various regulatory bodies and is not likely to canvass the registries or databases of each regulator to investigate a potential advisor.

In the example above, if a prospective client were to review their advisor’s credentials and work and disciplinary history solely through the insurance regulator’s website, the client would not be informed of the advisor’s expulsion from the mutual funds sector. The client might then mistakenly believe that the advisor’s overall disciplinary history was clean.

Advocis strongly believes that consumers should have a one-stop access point for reviewing a prospective advisor’s complete disciplinary history that is not limited to the domain of one sector’s regulator. It must also capture those individuals who offer advice and planning without the sale of product who are therefore not registered with any existing regulator. That is, rather than being based on today’s *ad hoc* and largely archaic regulatory structure, this critical consumer tool must be reconceived at the level of the advisor-client relationship, in order to properly ensure regulation is informed by the consumer’s perspective as seen from the practical reality of day-to-day consumer experience.

These four major shortcomings of the existing regulatory framework expose consumers to unnecessary and unacceptable risk. They arise from the fact that current regulation does not reflect the modern, holistic and cross-sectoral approach to financial advice and planning that most consumers want, require and receive. But these risks are largely addressable with minimal disruption to the retail financial services sector if the proper regulatory solution is put in place. It is to such a solution that this submission now turns.

The solution: Raise standards and make financial advice a profession

Fortunately, the solution to these problems is simple, straightforward, and does not require significant government resources to implement. What it does require is a willingness to fundamentally re-think the regulation of financial advice, taking it away from its product-based roots and aligning it with the client relationship-centric model that is the reality of how most consumers now access financial advice and products.

The solution envisions recognizing the provision of financial advice as a true profession, through the creation or accreditation of a professional body that regulates financial advisors and the practice of financial advice in the public interest. The professional body would be responsible for the licensing, registration, standard-setting, investigation and disciplining of financial advisors. This would be akin to how other professional bodies operate, such as the College of Physicians and Surgeons of Ontario and the various provincial law societies.

The following is a high-level overview of the defining characteristics of the professional body.

(i) Mandatory membership.

Just like the professional bodies for engineers or accountants, the solution requires that anyone who holds himself out as a financial advisor, or who is in the business of offering financial advice or planning services to the retail public, be a member in good standing of the professional body for financial advisors.[6] The membership requirement would cross traditional product sector boundaries, capturing everyone who offers retail-level financial products and services – thus introducing a unified oversight of all retail client-facing advisors, including financial planners. The professional body would establish initial and ongoing proficiency standards required to achieve membership. In contrast, the CSA's recommendations would continue to leave advisor oversight under the auspices of organizations such as the MFDA, IIROC, the OSC, and other sector regulators, thus maintaining much of the current *status quo*.

(ii) Meaningful titles and designations.

As noted above, we recommend that the terms "financial advisor" and "financial planner" and a number of today's leading designations be defined and granted proficiency recognition by the professional body. The professional body would be able to develop categories and subcategories for membership, as conceptualized in Figure 1, which would recognize the areas of specialization reflected, for example, in designations such as the CFP®, CLU® and CH.F.C®. The basic principle should be that an advisor cannot hold him- or herself out to the public in a manner that deceives or misleads – or could reasonably be expected to deceive or mislead – a client or prospective client with regard to the advisor's proficiency, qualifications, and product or service offering.

(iii) Enhanced proficiency and continuing education requirements.

We recommend the establishment of a mandatory minimum baseline of skills, education and other competencies which all financial advisors, including financial planners, would be obligated to meet.

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[6] Certain exemptions could apply to the mandatory membership requirement, such as professionals licensed by another recognized body that offer financial advice as ancillary to their main service offering, such as lawyers or real estate agents. It may also be desirable to distinguish between the holistic full-service financial advisor and those who purely offer one-time transactional services, such as discount brokers. The number of service providers falling into this latter group would likely be relatively small.

The professional body would develop harmonized and universal requirements for advisor skill and competency regardless of product sector, instead of leaving responsibility for their oversight dispersed across various regulatory, self-regulatory and industry bodies. Continuing education would be a mandatory requirement, including content dedicated to topics on professionalism and ethics. The professional body would administer, monitor and enforce continuing education requirements designed to ensure that all financial advisors maintain a high standard of proficiency. It would also require member advisors to maintain errors and omissions insurance to protect the clients they serve. Advisors should be required to have errors and omissions insurance for <u>all</u> products and services that they offer.

(iv) An enforceable code of conduct.

The professional body would have, at the cornerstone of its commitment to professionalism, a code of conduct that inculcates ethical norms in individual advisors and an ethical culture in their firms. The code would include, *inter alia*: the prioritization of the client's interests; the duties surrounding conflicts of interest; the duty to provide competent service; the duty to act with honesty and integrity; the duty to preserve and protect client confidentiality; and the duty to cooperate with the professional body and regulators.

The code of conduct would be backed by a complaints, investigation and disciplinary process that empowers the professional body to suspend or cancel the advisor's membership. What is unique about this is that because membership in the professional association is mandatory across product sectors, discipline or suspensions are not limited to one product sector. Instead, they address the more serious issues of negligence, incompetence or fraud directly.

(v) An accessible, consumer-facing central registry.

The professional body would maintain a public-facing database whereby consumers can conduct a "one-stop" check of a prospective advisor's credentials and disciplinary history. Unlike the registries maintained by existing regulators and SROs, which only contain information pertaining to the advisor's activities in the regulator's or SRO's respective sector, the professional body's registry would be based on the conduct of offering advisory services to the retail public. It would therefore transcend product sectors, addressing the "sector hopping" problem of miscreants. This focus on scope of work and conduct would also capture those advisors and planners who are currently not registrants of any regulator.

(vi) Specializations within general financial advice.

In their response to the Consultation Paper, some stakeholders may argue for professionalization of the industry as we have, but may wish to restrict it to financial planners. From our perspective, it is evident that a broad, rather than a narrow, approach is needed: it is in the best interests of consumers that all individuals who offer financial advice to the retail public be included. If the CSA focuses on financial planners exclusively, it will fail to address the consumer protection concerns that are the impetus behind the Consultation Paper.

We are able to provide a unique perspective on this matter: our association consists of members who have acquired financial planning designations (amongst other advanced designations) and members who do not have such designations. We have concluded that financial planning is unavoidably and inextricably a part of the larger practice of providing financial advice. This is clear upon even a cursory review of the requirements stipulated in the rules, policies, bulletins and notices of provincial securities regulators, the MFDA, and IIROC.

We do not assert that all financial advisors are engaged in financial planning at the same high level as those who have attained specialized designations. But the reality is that a financial advisor must perform certain basic planning components whether or not he or she also has a financial planning designation as part of the existing Know Your Client ("KYC") and Know Your Product ("KYP") rules, as well as the various prescribed suitability requirements. In fact, the reforms in the Consultation Paper would further strengthen the planning components that all advisors must undertake.

Beyond financial planning, within the broad pool of financial advisors, there exist many other industry-developed designations which enable a financial advisor to further specialize in the more detailed aspects of various dimensions of financial advice, such as taxation, estate planning, and health insurance, for example. The financial advice sector is depicted in Figure 2. All financial advisors (the largest of the Venn circles) must possess a basic skill level to engage in the provision of financial advice to the retail public.

Within the total advisor population, we see the ongoing development of more stringent specializations with respect to certain sub-fields of advice; these sub-groupings reflect specializations which go beyond the benchmark of skills which the average financial advisor would be required to meet. These specializations are useful to many consumers – and at times are necessary for those clients who present their advisors with more complex advice and planning goals and objectives.

So, within the overall group of financial advisors, there are smaller subgroups of specialists who operate in advanced disciplines. Such specialization is common in established professions; indeed, it is analogous to the medical profession, where all doctors must meet a minimum standard to be called a medical doctor or MD. But within the field of MDs, there are smaller groups who have specialized. Every member of the profession is a doctor, but only those who have completed additional training and coursework are allowed to use designations which identify their specialization, such as cardiologist and oncologist.

To further the analogy, consider a proposal to regulate only the subgroup of advanced specialists, as opposed to the entire group of medical doctors. Such an option would be a wholly inadequate policy response: the risk to consumers would be overwhelming if anyone could hold out as a doctor and operate largely or completely unregulated. Similarly, to regulate only financial advisors who have completed a specialized designation program would be a wholly inadequate policy response, as this too would expose consumers to risk.

FIGURE 2: FINANCIAL ADVISORS AND SPECIALIZATIONS.

A depiction of the interrelationship between the total population of financial advisors and prominent specialist subgroups. For example, advisors who are CLU®, CH.F.C.® or CFP® designation holders are members of specialized groups within the larger population of financial advisors. Overall, the field of financial advice in Ontario is populated with a range of designations, including a number of popular, long-standing financial planning designations.

(vii) Advisor representation in their own regulation.

One of the hallmarks of a true profession is involvement of members in their own regulation – this is true of lawyers, doctors, dentists, architects and so on. Involving members allows the professional body, including the government to which the body ultimately reports, to leverage the vast accumulated knowledge and real-world experience of the membership to set policy in a way that is more likely to achieve its objectives.

Financial advisors are currently "regulated without representation." The proposals in the Consultation Paper would unfortunately maintain advisor oversight in the hands of the MFDA, IIROC, and so on, so that advisors would continue be regulated by entities that do not consider the

advisor-client relationship as merit-worthy of the same level of regulatory scrutiny as is applied to the lawyer-client relationship or the social worker-client one. Indeed, these organizations often do not fully understand what advisors do in their day-to-day client interactions.[7] Finally, advisors lack true standing and "voice" in these organizations. For example, neither the MFDA nor IIROC mandate the presence of advisors on their boards of directors.

The professional body would have a board of directors comprised of financial advisors, members of the public, and government appointees, among other persons. The mandate of the body would be, first and foremost, the regulation of financial advisors and the provision of financial advice in the public interest. The professional body, through its board, would report directly to the provincial finance minister, rather than indirectly through a product regulatory body. As financial advice has evolved into a true profession, it is time to give professional financial advisors a dedicated voice in their own regulation.

In summary, the solution provides benefits to all market participants: first and foremost, consumers would benefit from knowing that all advisors meet baseline proficiency requirements, just as they do with their architects or engineers. They would also benefit from the simple way to verify their advisor's credentials and disciplinary history without having to navigate the maze that is the current regulatory landscape. Finally, they would enjoy the support of a disciplinary system with teeth: it would be a system that actually protects the public, rather than potentially off-loading one sector's problem onto another sector and a new set of unsuspecting consumers.

Financial advisors would also benefit from enhanced public trust, status and confidence as true professionals, and we know that our members would be very supportive of unethical colleagues who tarnish their collective reputation being removed once and for all. The government would benefit from enhanced consumer outcomes, including reduced public financial reliance, and the expertise and support of the professional body in crafting and implementing their policy agenda. Product providers and distributors would benefit from the professionalism of the advisors who represent their companies to the public on a day-to-day basis.

4. Targeted Reforms to NI 31-103

We now turn our attention to addressing the questions posed in the Consultation Paper in regards to the proposed targeted reforms to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (the "Targeted Reforms").

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[7] While branch managers and other dealer staff receive and review paperwork documenting the advisor-client interaction, it is usually only the advisor that has a direct relationship with the client. As with any in-person, face-to-face interaction, there are many nuances that are difficult or impossible to distill into writing. The advisor's ability to understand the "human" elements in a client interaction is critical to the quality of that relationship.

Conflicts of interest – general obligation

1) Is this general approach to regulating how registrants should respond to conflicts optimal? If not, what alternative approach would you recommend?

Generally, this approach to regulating conflicts of interest points in the right direction – it is described in high-level principles that speak of "specific and clear disclosure" of the conflict, and having "a reasonable basis for concluding that the client fully understands" its implications. However, the problem with the approach is not the general message, but that it would create a situation where each firm develops and executes its own conflict management system. The guidance speaks to enforcing the "tone at the top", which is not necessarily consistent from firm to firm. The efficacy of the conflict system would then be evaluated by regulators that are many levels away from the actual client experience and not necessarily in a position to judge whether the conflict was appropriately managed.

Approaching conflict management in this manner will exacerbate the problem of consumers having very different experiences that are dependent on the particular firm that they deal (with significant variances likely between larger and smaller firms, with larger firms having the resources and scale to develop robust conflict management systems) with or the particular product regulator that governs that firm. We believe that regardless of the product they purchase or the firm that they purchase from, consumers should experience a consistent, high-quality approach to conflicts management.

In our view, conflicts management is an integral part of advisor professionalism. After all, conflicts are recognized and managed, first and foremost, at the client-advisor level. The best way to ensure the quality and consistency of consumer outcomes is to ensure that the client-facing advisor is a true professional, possessing a high degree of proficiency and bound by a uniform code of professional conduct. The advisor's compliance with conflict management principles should be judged by the professional body that would enforce uniform standards across the industry and have the practice knowledge to best evaluate whether the conflict avoidance or mitigation steps taken were appropriate.

2) Is the requirement to respond to conflicts "in a manner that prioritizes the interest of the client ahead of the interests of the firm and/or representative" clear enough to provide a meaningful code of conduct? If not, how could the requirement be clarified?

The words are straightforward enough, but they do not (and cannot) inform the content of the code of conduct alone. If each firm can establish their own procedures and standards, then the application of these codes of conduct across the industry will be fraught with inconsistencies, and consumers will suffer for it.

The way to make a code of conduct meaningful is to make its enforcement consistent in practice and applicable industry-wide, to all retail-facing advisors, regardless of what product is sold or

through which firm. This could be done through the professionalization solution discussed in Part 2. The professional body would evaluate the advisor's actions in the context of its real-world knowledge and practice-proven experience, and its enforcement would be meaningful and effective, as membership in good standing would be required to remain active in the industry.

3) Will this requirement present any particular challenges for specific registration categories or business models?

The requirement could pose a challenge for the embedded compensation sales model. The CSA should make it explicit that it is not intending to eliminate this client choice through the Targeted Reforms addressing conflict of interest. This is because it is possible to characterize embedded compensation as being an inherent conflict of interest. This issue is further discussed in the questions to Appendix A, but in brief, the way to overcome this perceived conflict is to (i) ensure the professionalism of the advisor involved; and (ii) enhancing disclosure through initiatives such as Point of Sale and CRM-2.

The requirement could also pose a challenge for proprietary business models, as the inherent relationship between the advisor, firm and product make it plainly more difficult for the registrant to demonstrate that the conflict was resolved and the proprietary product is suitable. We caution the CSA from taking actions that have the unintended consequences of harming specific business models, or championing one model over another, unless that it is its specific (and publicly stated and consulted) objective.

Know your client

Our general view of the Targeted Reforms in this section is that they will make it very cumbersome for retail investors to execute a "routine" trade – *i.e.* a trade that is clearly in the normal course of the investor's behavior, such as repeated contributions into retirement plans at regular intervals. Even absent any material changes to the client's situation, the Targeted Reforms would require advisors to conduct detailed reviews of the client's risk profile, investment objectives, asset allocation and personal circumstances for each transaction, creating considerable "red tape" without any substantive benefit to the investor.

The CSA's intentions could be better achieved by leveraging a duly qualified advisor's professional judgment to determine the degree of KYC information that needs to be refreshed. This is an example of how professionalization of the advice-giving sector would be preferable to the creation of prescriptive rules that will make the seeking and provision of financial advice less desirable for clients and their advisors, respectively.

4) Do all registrants currently have the proficiency to understand their client's basic tax position? Would requiring collection of this information raise any issues or challenges for registrants or clients?

No, not all registrants currently have the proficiency to understand the client's basic tax position. But they should – we believe that understanding basic tax issues is a key element in providing holistic investment advice, and an important and worthwhile skill for advisors to offer their clients. In order to provide this service, the proficiency of advisors must be enhanced, as it would in our professionalization solution discussed earlier.

Even if registrants obtain the proficiency to address basic tax strategies, some clients may nonetheless be unwilling to provide this information to their advisor in a desire to maintain their privacy and keep their tax affairs separate. Disclosure of this sensitive information should be done on a voluntary basis and clients should not be required to provide tax information on their application forms in order to obtain professional financial advice.

5) Should the CSA also codify the specific form of the document, or new account application form, that is used to collect the prescribed KYC content?

No, the CSA should not codify a specific form. It can produce guidance that capture the key principles the CSA wishes to articulate and make clear the CSA's expectations in regards to KYC, but given the variety of business models in the market, it should not produce one prescriptive form and require all businesses to be able to adopt it.

6) Should the KYC form also be signed by the representative's supervisor?

No – we suspect that the intention behind this suggestion is to explore alternative ways to enhance the accountability of the representative who collects the KYC information. But obtaining the signature of a representative's supervisor, who does not directly meet with the client and obtain first-hand information, will simply become compliance overhead that does not improve consumer outcomes.

The way to improve accountability is to ensure the professionalism of the registrant obtaining the KYC information directly from the client – namely, the financial advisor. It is by elevating standards, enshrining a commitment to professional conduct and creating accountability to a professional body that the CSA's policy objective will be achieved.

Know your product – representative

7) Is this general approach to regulating how representatives should meet their KYP obligation optimal? If not, what alternative approach would you recommend?

The general approach is sensible, but it seems that it really only applies to firms and representatives that offer investment funds, rather than securities in general. That said, we recognize that investment funds are the most popular product choice for the type of retail investors that are at the core of the mindset driving the Targeted Reforms.

However, instead of a requirement to "understand the specific structure, features, product strategy, costs and risks of *each* product their firm trades or advises on", it would be more workable if the requirement entailed an understanding of each asset class of product the representative's firm trades or advises on. A firm often has thousands of products on its product list and many are often very similar, so it would not be reasonable to expect a representative to have intimate knowledge of the nuances that distinguish the slightly-different products within a class.

Representatives should have thorough knowledge of whatever specific products or strategies are ultimately being recommended to the client. More generally, we believe that proficiency standards must be bolstered before all representatives will have the knowledge intimated by the CSA in this reform.

Know your product – firm

8) The intended outcome of the requirement for mixed/non-proprietary firms to engage in a market investigation and product comparison is to ensure the range of products offered by firms that present themselves as offering more than proprietary products is representative of a broad range of products suitable for their client base. Do you agree or disagree with this intended outcome? Please provide an explanation.

We agree with this intended outcome. If a firm holds out that it offers a mixed or non-proprietary shelf, it is reasonable for consumers to expect that the firm offers a diverse array of products that are suitable for the firm's targeted client base.

However, the CSA must be mindful that the targeted "typical" client can vary widely from one firm to the next: some firms concentrate on the mass market, others focus on the high net worth segment, some focus on scholarship plans, and so on. The CSA should encourage and support diverse business models that specialize in unique client needs, rather than inadvertently encouraging a "one size fits all" model.

Firms should have reasonable discretion as to what products they offer and what client objectives they address – this is simply about finding competitive niches in an open marketplace. Therefore, the product shelves of two different mixed/non-proprietary firms can look very different even if both of those firms are compliant with the CSA's intended outcome.

9) Do you think that requiring mixed/non-proprietary firms to select the products they offer in the manner described will contribute to this outcome? If not, why not?

The principles articulated will contribute to the outcome. They are of general applicability in ensuring that firms undertake effort in reflecting on whether the products they offer can achieve the investment objectives of the types of clients they expect to serve.

10) Are there other policy approaches that might better achieve this outcome?

Fundamentally, the CSA should ensure that it is taking a principles-based approach to this policy objective. We are concerned with some of the language in the potential guidance, which militates towards prescriptive, burdensome and costly directions regarding how a firm can satisfy the stated policy objective in the CSA's eyes.

11) Will this requirement raise challenges for firms in general or for specific registration categories or business models? If so, please describe the challenges.

This requirement could raise serious challenges for smaller, independent firms. From the potential guidance, it is unclear what constitutes a review of a "reasonable" universe of products – and depending on the interpretation, the CSA could be mandating that firms retain third party research entities to develop reports that influence firms' product shelves. This would be a very costly exercise that could not be borne by smaller independent firms. Implementing this requirement would effectively result in the CSA gifting large, bank-dominated firms with a significant competitive advantage.

For proprietary firms, we caution the CSA that the labelling of a firm as "proprietary" could unfairly carry negative connotations for that firm. By definition, a proprietary business model restricts the range of products that consumers can access through that business to products that are related or connected to that business. While it is fair and appropriate for regulators to be wary of this restriction in regards to how it affects investors, and investors should be made aware in clear language that the business only offers proprietary funds, it is not necessarily a given that the firm cannot effectively fulfill their investors' needs. In fact, most firms that develop proprietary products begin with large, balanced investment funds that are suitable for the mass market.

12) Will this requirement cause any unintended consequences? For example, could this requirement result in firms offering fewer products? Could it result in firms offering more products?

This requirement will likely result in mixed and non-proprietary firms offering fewer products, as each product on the shelf will be subject to a rigorous review and monitoring processes on a product-by-product basis. This added overhead will necessarily result in the paring down of the number of products under consideration.

With the consequent reduction in competition, bank-owned firms would also be likely to narrow the range of funds they offer. Banks already enjoy a dominant position, and the Targeted Reforms will create additional compliance costs that will disproportionately burden independent firms with fewer resources to respond to the changes. With independent firms exiting the market, bank-owned firms will feel less competitive pressure to offer a diverse product range. All this would make retail investors worse off.

13) Could these requirements create incentives for firms to stop offering non-proprietary products so that they can fit the definition of proprietary firm?

Yes, depending on the CSA's expectations regarding the establishment and use of the market investigation, product comparison and optimization processes. All of these will create additional compliance obligations that place mixed or non-proprietary firms at a competitive disadvantage vis-à-vis proprietary firms. The CSA must be cognizant that each market intervention creates incentives, including unintended ones.

14) Should proprietary firms be required to engage in a market investigation and product comparison process or to offer non-proprietary products?

Proprietary firms should not be required to offer non-proprietary products – the CSA should be careful not to eliminate specific business models, so long as competition in the marketplace remains healthy and consumers have the opportunity to make an informed choice between a proprietary or non-proprietary firm.

15) Do you think that categorizing product lists as either proprietary and mixed/non-proprietary is an optimal distinction amongst firm types? Should there be other characteristics that differentiate firms that should be identified or taken into account in the requirements relating to product list development?

We agree with the policy objective of ensuring that the products on the shelf of any particular firm represent a diverse array of options that are suited to the type of client targeted by the firm, and we agree that consumers should be made aware, in writing through clear language, whether a firm offers proprietary products only or a mixed/non-proprietary shelf. But more importantly, there should be strong KYP principles that are applicable to all firms, and through the increased professionalism of client-facing representatives, the CSA can be assured that consumers are being presented product options on their merit and suitability for that particular client, regardless of whether the product is proprietary.

As we have discussed above, issues associated particularly with proprietary products/business models, such as conflicts of interest or incentives arising from commission grids, can and should be addressed directly, rather than indirectly through the labelling of firms and their product lists.

Suitability

16) Do you agree with the requirement to consider other basic financial strategies?

Yes – as long as the relationship between the advisor and client is intended, at the outset, to be one based on holistic, long-term advice, rather than a discrete, transaction-based one. The former type of relationship should require the services of a full-service professional advisor that possesses the proficiency and is bound by the ethical duty to consider other basic financial strategies.

We have long held that advisors, to provide professional service to clients, must conduct a baseline level of financial planning in order to develop appropriate investment strategies. This necessarily includes an assessment of basic financial suitability and a determination of whether the purchase of a securities or insurance product, or another course of action, is best suited for the client's particular circumstances.

However, merely transactional relationships should not attract this level of service, and the limitations of these types of relationships should be made clear to clients before they decide to proceed.

17) Will there be challenges in complying with the requirement to ensure that a purchase, sale, hold or exchange of a product is the "most likely" to achieve the client's investment needs and objectives?

We have reservations with the CSA's use of the phrase "most likely". The decision to purchase, sell or hold a security is a forward-looking decision that is made based on an analysis of the available information at the time of the decision. While objective criteria such as fees should undoubtedly be considered, subjective, qualitative elements play just as large a role in determining which course of action is best – such as whether the product's structure and investment strategy are suitable for the client, or a consideration of the fund manager's experience and past performance. The analysis of these qualitative factors is an area where investors can really benefit from the professional judgment of a duly qualified advisor.

If later down the road, the investor believes the recommendation was not in his or her best interest, an *ex post* review of an advisor's determination of what was "most likely" to achieve the client's investment objectives becomes susceptible to hindsight bias that prevents a fair and proper analysis. The qualitative judgment of the future unknowns tends to be under-appreciated, and more weight given to more objective, foreseeable elements such as cost.

That is, in hindsight, the advisor is not likely to receive credit for successfully avoiding qualitative risks because something that does *not* happen (such as a product's swap counterparty not defaulting) is a "non-event" that does not rise to the level of consciousness. But if that superior product comes with a slightly higher product cost, it is that objective cost difference that is likely to be heavily scrutinized.

The CSA has explicitly stated that product cost is not intended to be a sole determining factor of whether a product is suitable, but there is a real risk that it would serve as a *de facto* proxy of suitability in a hindsight review. The CSA also states that it does not "necessarily mean that there is only one best strategy or product, as applicable, for the client" –while we agree, we believe that this consideration could easily be dismissed and would not be persuasive in an *ex post* argument about the significance of skillful qualitative judgment managing "non-events".

The decision of a professional advisor acting in good faith to exercise his or her judgment in recommending a product or strategy should be accorded respect, and not easily and unfairly

second-guessed after-the-fact based on an argument that it might not have been the “most likely” to achieve a particular result. We would suggest foregoing the phrase “most likely” entirely to something that acknowledges the decision was made in the context of subjective factors that were present at the time. Perhaps something such as “likely in the context in which the decision was made” would be more appropriate.

18) Should there be more specific requirements around what makes an investment “suitable”?

No – the determination of whether any particular investment is suitable is through an analysis of a multitude of factors of both the client and the product. The number of permutations to consider are too great to realistically or helpfully reduce to writing. The CSA’s guidance should be principles-based, at a high level. Instead, the determination of suitability must be made by a professional advisor who has the requisite proficiency and is accountable to a professional body for any failings to properly exercise the requisite professional judgment.

19) Will the requirement to perform a suitability assessment when accepting an instruction to hold a security raise any challenges for registrants?

Suitability assessments should not be required when the instruction is to merely hold the security – e.g. maintain the *status quo* – unless there has been some other material change that warrants a review of the client’s overall investment strategy. This could include a material change to the client’s KYC profile, significant external events affecting capital markets, or a material change in the risk profile of the issuer. Otherwise, suitability assessments for holding a security add unnecessary red tape without adding meaningfully to consumer protection.

20) Will the requirement to perform a suitability analysis at least once every 12 months raise challenges for specific registrant categories or business models? For example, a client may only have a transactional relationship with a firm. In such cases, what would be a reasonable approach to determining whether a firm should perform ongoing suitability assessments?

Generally, we believe an every 12-month suitability requirement is excessive, absent material changes to the client’s profile. Rather than requiring annual KYC updates, an annual reminder on a client statement of their current KYC responses should suffice, accompanied by a request to contact their advisors should anything now need updating.

The requirement will raise particular issues for business models that do not offer the client with holistic advice, but which are more discrete and transaction-focused. It is important that the CSA recognize the different roles that different advisors play. For example, not all of the suitability proposals should apply where a client has only a transactional or one-off relationship with a registrant.

21) Should clients receive a copy of the representative’s analysis regarding the client’s target rate of return and his or her investment needs and objectives?

Yes, clients should be able to receive a copy of the representative's analysis of the client's situation upon request. This is all part of the holistic advice that professional advisors provide. However, we are concerned with the CSA's overt focus on the client's target rate of return: while many clients are targeting a certain rate of return, other clients have somewhat different targets, such as a certain amount of income or cash flow or expected longevity of drawdown. This is one of the pitfalls of the CSA being overly prescriptive with the proposed reforms.

Further, we caution the CSA to be careful in how it positions the target rate of return in investor communications; it is very easy for investors to conflate "target rate of return" with a guaranteed rate of return. If the CSA is to make the target rate of return more prominent, appropriate consumer-facing guidance is required to explain its utility and limitations.

22) Will the requirement to perform a suitability review for a recommendation not to purchase, sell, hold or exchange a security be problematic for registrants?

This requirement could become very onerous. If representatives are required to document the reasoning behind every decision to *not* take some action, there is theoretically a limitless number of decisions that would have to be documented. We recommend that proper suitability reviews be limited to the reasoning behind positive actions.

Relationship disclosure

23) Do you agree with the proposed disclosure required for firms registered in restricted categories of registration? Why or why not?

We do not agree with the proposed disclosure. Section 14.2(2) of NI 31-103 already requires comprehensive relationship disclosure, including a description of the products and services the registered firm offers to the client. We take issue with the CSA's proposed new language, which we view as strongly and unnecessarily negative – phrases such as "the firm does not consider a full range of securities products" and it "is unable to consider whether such other types of products are better, worse or equal" will simply and unfairly cast the firm in a damaging light.

The wording suggests that the firm cannot ably address the client's investment needs solely because of a restricted registration, which is not necessarily true. Consider a "restricted" firm like a mutual fund dealer – many of these firms provide access to literally thousands of products, with an extremely high probability of being able to construct a diversified portfolio that is well-suited for the client. In fact, even the use of the term "restricted" seems to connote regulatory bias and favour one dealer channel over another.

We would be supportive of a more neutral message that makes consumers aware that restricted categories exist – something along the lines of "Based on their category of registration, the firm and its representatives may not be able to offer all types of securities" would be a more appropriate

statement that conveys the facts but does not create unfair and unsubstantiated implications about the fitness of the firm.

As discussed earlier in this submission, we believe it may be helpful for there to be disclosure regarding the expectations of client service. In the OSC's 2004 Fair Dealing Model, the client was to select one of three relationship types at the outset: (i) a self-managed relationship, where the advisor does not provide any advice but instead executes orders as directed by the client; (ii) an advisory relationship, where the advisor provides insight and expertise, but does not have discretionary control – any decisions are ultimately made by the client; and (iii) a managed-for-you relationship, where the client is completely reliant on the skill and judgment of the advisor.[8] Types (ii) and (iii) should require the services of a duly-qualified professional advisor.

24) Do you agree with the proposed disclosure required for firms that offer only proprietary products? Why or why not?

We agree that there is value in consumers knowing whether a firm offers proprietary products only, or a mix of proprietary products or non-proprietary products. Again, though, we believe the CSA must be careful to not cast any particular business model in an unfairly negative light – there are proprietary firms with large and diverse product shelves that can ably service the vast majority of the market. A neutral and factual statement such as "This firm offers only proprietary products" would suffice, without adding tones of regulatory judgment.

25) Is the proposed disclosure for restricted registration categories workable for all categories identified?

Yes, we would be supportive of neutral language attached to the four identified restricted registration categories.

26) Should there be similar disclosure for investment dealers or portfolio managers?

Yes, in the interests of a level playing field, consumers should know that certain restrictions apply to all registration categories – this is just a fact of our regulatory system.

27) Would additional guidance about how to make disclosure about the relationship easier to understand for clients be helpful?

We believe that the relationship disclosure requirements already existing in NI 31-103 are comprehensive. We support the addition of neutral and factual relationship information as discussed above.

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[8] *Supra*, note 1.

Proficiency

28) To what extent should the CSA explicitly heighten the proficiency requirements set out under Canadian securities legislation?

As discussed in Part 2 of this submission, we believe that the advisory profession needs to be professionalized – and that high initial and ongoing proficiency requirements are a cornerstone of professionalism. We fully support the notion that standards must be elevated for all client-facing representatives. But we do not believe that the CSA is the right entity to implement these increased standards.

Instead, like law, accounting and medicine, it should be the professional body governing financial advisors that sets proficiency requirements and maintains accountability by ensuring its members' compliance with these standards. In our view, the CSA is too far removed from the core advisor-client relationship to effectively understand, set and enforce proficiency standards at the retail level; instead, it should maintain its focus on fair and efficient capital market infrastructure, products and product issuers and the efficacy of the dealer self-regulatory organizations it has already recognized.

29) Should any heightening of the proficiency requirements for representatives be accompanied by a heightening of the proficiency requirements for CCOs and UDPs?

Yes – in the mutual fund registration category, while the CCO oversees policy development and compliance oversight, most dealers have registered Compliance Officers (COs) who complete the tier two supervision and often contact advisors with account queries. That is, they have substantial dealings with client-facing accounts. For this reason, we believe that COs, including CCOs, would benefit from enhanced proficiency and annual CE requirements. This will also ensure that CCOs remain close to the advisor and core industry activities related to providing professional financial advice.

Titles

30) Will more strictly regulating titles raise any issues or challenges for registrants or clients? *- and -* 31) Do you prefer any of the proposed alternatives or do you have another suggestion, other than the status quo, to address the concern with client confusion around representatives' roles and responsibilities?

We believe that greater clarity is needed in this area. Currently, consumers encounter a mish-mash of titles that lead to unnecessary confusion, as many consumers understandably but mistakenly

believe that the professional title used by an advisor is a meaningful certification of skill and knowledge. The fundamental cause of this problem is that, across Canada (other than Quebec), anyone may hold out as a financial advisor without obtaining any education or demonstrating a requisite level of proficiency. (This, and other major concerns with the current regulatory framework are discussed in greater detail in Part 2 of this submission.)

As a part of making the provision of financial advice a true profession, the area of titles must be reformed. But we disagree with the CSA's proposed options which, in many of the scenarios outlined, would cast advisors as "salespersons" – this characterization harkens back to a much earlier time when advisors were primarily the retail-level sales conduits for the product manufacturers, often based on one-time transactions, and ignores the reality that the role of the advisor has evolved over the past few decades.

Today, advisors are much more than gateways to product. Modern professional advisors act first and foremost to serve their clients by providing holistic advice and maintaining relationships that span years and decades. Advisors help ensure their clients are financially prepared for major life events by analyzing their clients' financial position and objectives. Plans are adjusted and course-corrections made as years pass and milestones are reached. The sales of financial products are means to achieving clients' goals, rather than goals unto themselves.

This is the role of today's professional advisor, and it is starkly different from the characterization that the CSA proposes with its "salesperson" titles. We believe that there should only be one authorized title for advisors who offer full-service, holistic advice – namely that of "financial advisor" – and its use should be restricted to those who are in good standing with the new professional body governing advisors. This professional title would be protected, just like the titles of lawyer, doctor or landscape architect are protected by those respective self-governing professions.

The title of "salesperson" could apply to all those representatives who work on a business model that is purely execution-based and transactional, with no exercise of skill or judgment regarding the suitability of the client's investment choice. These representatives would not be members of the professional body.

Additionally, it is of crucial importance that title reform not be only about the use and misuse of specific titles. Such reform would be merely cosmetic, and of little lasting value. Rather, reform in this area must encompass both the title and the scope and function of the work. The basic principle should be that an advisor cannot hold him- or herself out to the public in a manner that deceives or misleads – or could reasonably be expected to deceive or mislead – a client or prospective client with regard to the advisor's proficiency, qualifications, and product or service offering.

32) Should there be additional guidance regarding the use of titles by representatives who are "dually licensed" (or equivalent)?

No. As far as most consumers are concerned, both securities and insurance products are “financial products”, and innovation, increasing complexity and convergence in both sectors have resulted in offerings that can serve as complements or substitutes of each other. Most consumers do not know the regulatory “origin story” of a particular product, and in the interests of professionalism, consumer protection, and the elimination of product arbitrage, it should not matter to the consumer’s experience.

Therefore, the title of “financial advisor”, granted and monitored by a professional self-regulatory body of advisors, is appropriate for both single- and dual-licensed individuals. The only criteria should be whether the representative purports to offer holistic financial advice to the retail public.

Designations

33) Should we regulate the use of specific designations or create a requirement for firms to review and validate the designations used by their representatives?

Designations can serve as useful indicators of advanced financial education that can help consumers access the specialist that they require (such as an estate or tax specialist) and can be a competitive advantage for advisors to stand out in a crowded field. But in recent years, there has been a proliferation in the number of designations, giving rise to consumer confusion as to which designations are meaningful and hard-earned.

Some designations, such as the CLU and the CFP, are well-known and respected within the industry, while other impressive-sounding designations have seemingly popped up out of nowhere and are attainable with very few hours of self-study. What is important is that consumers are able to distinguish the “wheat from the chaff”, so we support stronger regulation of designations.

However, rather than being regulated by the CSA, we believe the regulation of designations should be within the ambit of the new professional body that governs financial advisors. Designations are an extension of proficiency, and are a natural fit to be overseen by the professional body. For example, there are baseline requirements to be a member of the Law Society of Upper Canada (J.D. or LL.B. degrees as proficiencies), and that professional body then maintains “certified specialist” programs as designations for members who achieve advanced proficiency in areas such as family law or labour law. As discussed in Part 2 of this submission, the profession of financial advice offers many opportunities for specialization, and it should be the professional body that determines the relevancy of a designation in certifying an advisor thusly.

Role of UDP and CCO

34) Are these proposed clarifying reforms consistent with typical current UDP and CCO practices? If not, please explain.

We do see the reforms as largely consistent with typical UDP and CCO practices. But we would like to see a minimum number of CE credits be earned annually by all compliance staff, including UDPs and CCOs, with half of those required to be the same courses completed by advisors. In many dealers, these positions do not appreciate the ongoing courses taken by advisors.

Statutory fiduciary duty when client grants discretionary authority

35) Is there any reason not to introduce a statutory fiduciary duty on these terms?

Where the client grants discretionary authority to the registrant, the common law fiduciary duty is already triggered in the vast majority of cases. It is unclear what ascribing the duty into statute would achieve here, but we have no particular opposition to it.

5. Regulatory Best Interest Duty

Proposed framework

36) Please indicate whether a regulatory best interest standard would be required or beneficial, over and above the proposed targeted reforms, to address the identified regulatory concerns.

37) Please indicate whether you agree or disagree with any of the points raised in support of, or against, the introduction of a regulatory best interest standard and explain why.

38) Please indicate whether there are any other key arguments in support of, or against, the introduction of a regulatory best interest standard that have not been identified above.

We agree with the spirit of what the CSA is trying to accomplish, but in our view, the creation of a regulatory best interest standard ("Regulatory BIS") by provincial securities regulators is the wrong approach.

Through what has been proposed in the Targeted Reforms, it is evident that the CSA recognizes the importance of the advisor-client relationship and its centrality to the investor experience with the securities industry – in fact, many of the Targeted Reforms seek to enhance investor protection through the enhancement of advisor proficiency and professionalism. But the CSA's vision to improve advisor professionalism (a goal which we completely agree with and for which we have been advocating for many years) cannot be accomplished within a regulatory structure that still largely considers advisors as an afterthought, as mere salespersons in the distribution chain for their dealers.

A regulator-imposed best interest duty would be unworkable and unfair

Certain members of the CSA are proposing that a Regulatory BIS be implemented, and compliance therewith judged, by regulators who are distinctly separate and uninvolved with the day-to-day

operation of providing retail investors with financial advice. Given this detachment, it is our position that provincial securities regulators do not understand the work that advisors do and are therefore not in a proper position to apply "best interest" principles to an advisor's daily practice. This is not intended to be a slight; this is just the reality that provincial securities regulators are naturally, and correctly, focused on "macro" issues of laying the groundwork for healthy, functioning and fair capital markets.

A "best interest" duty is a professional standard of care meant to ensure that a client receives the utmost quality in their advisor's care and judgment, driven by an underlying ethical responsibility to do what is "right" for that client. It necessarily involves subjective assessments that take into account the client's objectives, risk tolerance and financial position, as well as the market conditions known at the time and projected out into the (sometimes distant) future. The breaching of a best interest obligation carries significant ramifications for the client, advisor, and the reputation of the industry as a whole, so a fair hindsight determination of whether a decision was in the client's best interest requires an understanding of the real-world practice dynamic in play when the advisor made that decision.

It is manifestly unfair to apply a best interest duty to a professional group while failing to involve them in their own regulation. Critically, we draw attention to the fact that there is no other profession, whether it be law, medicine, or so on, whose members are subject to a best interest duty but who are not accorded professional standing and given a voice in their own regulation. Senior regulators or ministries in those other industries recognize that they have an important role to play in setting the regulatory framework, but they cannot, should not and do not attempt to regulate the nuances of the day-to-day professional-client relationship or judge whether a professional practitioner's actions were in the best interests of the client. Instead, they wisely and respectfully leave professional proficiency and conduct regulation to accredited self-regulatory bodies, such as the College of Physicians and Surgeons or the association of Chartered Professional Accountants.

A Regulatory BIS introduced at the CSA level, being so far removed from the actual practice of delivering advice, would create enormous uncertainty about its content and how it would be interpreted and applied in practice. Some of this confusion is evident, even from the outset. For example, the Consultation Paper says that the Regulatory BIS is not meant to be a restatement or formulation of a fiduciary duty, but will be "comprehensive and tailored". But a duty of care that purports to take some ambiguous middle ground, being something less than fiduciary but more than the current standard, cannot be comprehensive and tailored without the development of principles based on real-world precedents that make clear exactly what the Regulatory BIS actually entails.

These principles will have to be developed over many years through costly litigation to develop a body of case law that will lead to the emergence of principles that will elucidate how the CSA would enforce the Regulatory BIS – and, in our view, those principles will very likely end up being similar to those which have been articulated in our common law fiduciary duty. This raises the question of

just what is to be gained by trying to supplement or eliminate the current common law duty with the Regulatory BIS.

The Consultation Paper says that securities regulators can "appropriately express" a Regulatory BIS, with the regulator imposing the existence and the content of the standard. With respect, if Appendix H is any indication, this belief is not well-founded. In fact, in the Consultation Paper, the BCSC recognizes that the Regulatory BIS will create uncertainty, calling it "broad, sweeping and vague" – and we cannot think of a more caustic description when it comes to regulation of any sector or industry and particularly when it is attached to something as important as a best interest duty.

Interestingly, at the same time, the OSC and FCNB convey that the Regulatory BIS is to act as a guide to address situations that fall between specific rules or are novel – this "benefit" directly contradicts the claim that regulators can appropriately inform the content of the standard. In fact, we agree with this latter position that there will always be areas of ambiguity that must be addressed by governing principles, rather than prescriptive rules – it is simply a fact that securities rules are always going to trail market developments.

Further, we are disturbed by the OSC's and FNCB's statement that it is a Regulatory BIS that would catalyze the professionalization of advisors. If the OSC and FNCB are serious about creating a financial advisory profession, it should recognize that nearly all professions are self-regulated by their own professional bodies, such as doctors, lawyers or engineers. Provincial securities regulators having responsibility for professional advisors would be akin to provincial ministries of health directly regulating doctors; while they certainly have an important role to play in the overall functioning of the system, it is plainly obvious that such a structure would be inappropriate as the ministries do not have the contextual knowledge to perform competent professional regulation. Respectfully, securities regulators should be cognizant of their limitations and focus on their areas of expertise.

In short, our issue is not with a best interest duty – Advocis has such a duty embedded in its own *Code of Professional Conduct*[9] – but we are opposed to a best interest duty that is interpreted and applied by regulators that are not connected with the client-facing work of advisors and therefore are not positioned to understanding the nuances of an advisor's real-world practice.

A professional association is best suited to implement a best interest duty

The best way to achieve our shared investor protection objectives is through a fundamental reset of how advisors are regulated. It is time to make a clean start by establishing a regulatory structure for professional advisors that is flexible; contextual; principles-based; and client-centered. The most effective, fair and common-sense approach is to establish the professional body for advisors

[9] Advocis *Code of Professional Conduct*, http://www.advocis.ca/pdf/Advocis-CPC.pdf.

detailed in Part 2 of this submission and embedding the duty to act in a client's best interest as the core element of the professional body's code of conduct.

A significant feature – indeed, perhaps the defining feature – of the "best interest" concept is its moral ambition, which lies in the expectation by the client of true good faith on the part of the advisor. In this light, the ultimate focus of the duty is trained on the advisor's motives and actions in advancing the client's overall interests, and not merely on the state of the client's accounts at any given point in time. Embedding a best interest obligation in the code of conduct will make for a more robustly interpreted and applied obligation in the financial services sector – which is of course an outcome very much in any client's best interest.

In interpreting and enforcing the best interest duty, the professional body would be enriched by the first-hand knowledge of its practicing member advisors, some of whom would serve as members of the professional body's hearing tribunals. As in the case of any profession, it is the professionals within it who best understand how the best interest concept must be applied to the practices at which they work. Because of the involvement of active practicing members, the knowledge and understanding of the professional body (and its tribunal) would be constantly refreshed and in tune with the practices of the day. This flexible and evolving approach would be the superior way to address novel situations or evolving market conditions.

6. Impact on investors, Registrants and Capital Markets

Impact on investors, registrants and capital markets

39) What impact would the introduction of the proposed targeted reforms and/or a regulatory best interest standard have on compliance costs for registrants?

- and -

40) What impact would the introduction of the proposed targeted reforms and/or a regulatory best interest standard have on outcomes for investors?

- and -

41) What challenges and opportunities could registrants face in operationalizing:
(i) the proposed targeted reforms?
(ii) a regulatory best interest standard?

Both the Targeted Reforms and the Regulatory BIS would significantly increase compliance costs. We have discussed throughout this submission how several of the Targeted Reforms introduce prescriptive burdens that do not provide any clear benefit for investors, or would be inefficiently operationalized within an outmoded regulatory system. Many of the Targeted Reforms bizarrely expect advisors to exercise professional skill and judgment for their clients without affording them

professional trust, status or recognition from the regulator, instead bombarding them with additional compliance overhead to “prove” they acted professionally.

As discussed in Part 4 of this submission, the impact of a Regulatory BIS would be particularly severe, as there will necessarily be an enormous volume of litigation to determine the exact substance and content of the standard. It is unrealistic to believe that the Regulatory BIS will not be litigated in the same manner as the common law fiduciary duty has been over several decades. Even if it is only adjudicated before an administrative tribunal and not the courts, it will almost certainly take on many of the same features of the common law fiduciary duty – which would be a very expensive route to bring us essentially back to where we are today.

Moreso, while the OSC and FCNB state that the Regulatory BIS is not intended to guarantee investors’ outcomes or always result in the lowest cost product being recommended, we believe that this is greatly underestimating the hindsight bias that will impinge upon any *ex post* review of the advisor’s recommendations that is performed by securities regulators. The concept of subjectivity and the importance of managing qualitative risk in forward-looking decision making is discussed in our response to Question 17.

The Regulatory BIS would embed the retrospective evaluation of advice and transactions, many of which are inherently uncertain, into the regulatory process. It would invite a high degree of second-guessing with the benefit of hindsight as to whether a decision was in the "best" interest of a client, with the likely outcome being that the determination of what is "best" will largely be boiled down to the one objective *ex ante* criteria available: a determination of which product among a group of suitable products was the least costly to the consumer.

While advisors know that price should be one of many aspects to consider, under a Regulatory BIS, making a qualitative judgment of a product's other attributes could result in legal liability. By creating this amorphous standard, the CSA would likely increase the volume of litigation brought against advisors and dealers (including nuisance claims), create enormous new compliance obligations that could overwhelm the industry and, finally, cause significant uncertainty regarding the interpretation of the duty.

From the consumer’s perspective, the increase in costs created by the Targeted Reforms and the Regulatory BIS are ultimately borne by consumers. As a result, financial advice would become less accessible, which runs counter to the public policy objective of promoting personal financial independence and retirement readiness. A decrease in access to advice will leave consumers worse off, as studies have consistently proven that consumers derive substantial benefits from professional advice.

For example, a 2012 study by the Center for Interuniversity Research and Analysis of Organizations found that based on data compiled from over 10,000 households, advised households have up to

almost three times the median assets of non-advised households.[10] The CIRANO Study was updated in 2016, reaffirming "the strong positive effect on the amount and the value of assets in advised households", and "provid[ing] the foundation for an exceptionally strong key message about the value of financial advice."[11] Separately, a 2014 study by PricewaterhouseCoopers LLP found that advised households save up to 4.2 times more than non-advised households.[12]

Given the tremendous benefits of financial advice to investors, the CSA should be careful to avoid creating compliance burdens that will put advice out of reach for millions of consumers. As we have stated, we agree with the investor protection policy objectives motivating the Targeted Reforms and Regulatory BIS – but we do not agree with the plan to implement them within the existing regulatory framework. The CSA's objectives could be achieved on a more efficient and cost-effective basis through the advisor professionalism model discussed in Part 2.

42) How might the proposals impact existing business models? If significant impact is predicted, will other (new or pre-existing) business models gain more prominence?

We believe this question has been answered already in response to the other questions in the Consultation Paper. In general, some of the Targeted Reforms could place certain business models at a disadvantage (e.g. proprietary firms or restricted firms) by requiring them to take certain actions that are of dubious value to the investor and/or which presumptively cast the business model in a negative light. The total volume of the Targeted Reforms will require significant time and money to implement, which clearly places bank-owned firms at an advantage vis-à-vis independent firms as they will have the resources and the scale to implement them in a manner that is operationally economical. This will reduce competition the marketplace, which ultimately harms the retail investor.

We caution the CSA to avoid inadvertently picking "winners and losers" in pursuing the Targeted Reforms, or any regulatory initiatives for that matter. Every regulatory intervention creates consequences, some intended, others not. Part of the CSA's core mission is to foster healthy competition in the marketplace but the Targeted Reforms represent a real risk to the viability of smaller participants.

43) Do the proposals go far enough in enhancing the obligations of dealers, advisers and their representatives toward their clients?

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[10] The Center for Interuniversity Research and Analysis of Organizations, *Econometric Models on the Value of Advice of a Financial Advisor* (July 2012), http://www.cirano.qc.ca/pdf/publication/2012RP-17.pdf (the "CIRANO Study").
[11] The Center for Interuniversity Research and Analysis of Organizations, *The Gamma Factor and the Value of Financial Advice* (2016 Working Paper), http://www.cirano.qc.ca/files/publications/2016s-35.pdf.
[12] *Supra*, note 3.

The general intent behind the CSA's initiative is positive – but the question should not be about whether the proposals go "far enough", but rather if the CSA is going about it in the most sensible and effective way.

We believe the answer is NO; to truly achieve the CSA's investor protection objectives, it must be willing to reform the way that advisors are regulated by granting them a pathway to professional status and giving them say in their own regulation.

7. Potential Guidance

Appendix A: Conflicts of interest

Conflicts, generally

44) Is it appropriate that disclosure by firms be the primary tool to respond to a conflict of interest between such firms and their institutional clients?

Yes, disclosure is the appropriate primary tool vis-à-vis institutional clients. Institutional clients have the means of accessing professional financial and legal advice to ensure their interests are well protected.

45) Are there other specific situations that should be identified where disclosure could be used as the primary tool by firms in responding to certain conflicts of interests?

Disclosure that provides sufficient detail to allow the client to make an informed decision should be the primary tool to respond to conflicts of interest in most situations. But *who* provides the disclosure makes a difference to its efficacy – the reality is that many investors do not readily understand the meaning of the disclosure. So fulsome disclosure should be delivered by registrants who have demonstrable proficiency in the subject matter and so are able to explain complex concepts in plain language to the retail investor, and are bound by a code of conduct that ensures the client's understanding of the disclosure is a priority. In short, it is important that the registrant making the disclosure is a professional and possesses the professional judgment needed to ensure that the consumer's interests are protected.

46) Is this definition of "institutional client" appropriate for its proposed use in the Companion Policy? For example: (i) where financial thresholds are referenced, is $100 million an appropriate threshold?; (ii) is the differential treatment of institutional clients articulated in the Companion Policy appropriate?; and (iii) does the introduction of the "institutional client" concept, and associated differential treatment, create excessive complexity in the application and enforcement of the conflicts provisions under securities legislation? If not, please explain and, if applicable, provide alternative formulations. *- and -*

47) Could institutional clients be defined as, or be replaced by, the concept of non-individual permitted clients?

We see that the definition of “institutional client” closely mirrors the definition of “permitted client” in NI 31-103. We agree that this is an appropriate starting point for the Companion Policy. However, we are concerned that the introduction of additional definitions and specific financial thresholds create excessive complexity that is not warranted by its level of benefit. We would suggest that a concept of a non-individual permitted client would be the preferable approach.

Guidance on specific conflict of interest situations

48) Are there other specific examples of sales practices that should be included in the list of sales practices above?

No, the examples of sales practices are broad and generic and capture the concept of both direct and indirect compensation to the registrant in connection with the distribution of securities that are meant to skew incentives for purposes not related to their suitability to the client. We do share reservations with incentive practices such as commission grids that differentiate between proprietary and non-proprietary products and we believe these practices warrant greater scrutiny. However, further to the guidance’s discussion on compensation practices, we wish to make clear that it is important that the guidance avoid policy language that could inadvertently result in the outright elimination of the embedded compensation option.

In regards to conflicts of interest arising from embedded compensation, ultimately, there is necessarily a business aspect to the advisor-client relationship, and registrants must be afforded the opportunity to make a living. This does not mean that there should be any tolerance for unethical behavior that harms the investor to benefit the advisor. But the very fact that professional advisors derive revenue from their clients (which occurs directly or indirectly, regardless of the model of compensation) means that there is inherently some conflict that must be addressed by clear and meaningful disclosure.

In Advocis’ view, the embedded compensation model should remain an option for those consumers who wish to access advice in that manner. Eliminating this option would cut off the ability of many consumers (particularly low-income consumers) to access professional advice and investing services. Concerns normally associated with embedded compensation, such as its potential to inappropriately influence the advice dispensed, can be effectively addressed by improving transparency and disclosure through CRM-2 and by increasing professional standards, including through the implementation of an enforceable code of conduct by a professional governing body of practicing advisors.

49) Are specific prohibitions and limitations on sales practices, such as those found in NI 81-105, appropriate for products outside of the mutual fund context? Is guidance in this area sufficient?

- and -

50) Are limitations on the use of sales practices more relevant to the distribution of certain types of products, such as pooled investment vehicles, or should they be considered more generally for all types of products?

Prohibitions and limitations on sales practices should be based on principles: they should express the overarching desired policy objectives. The CSA should advance interests of fairness, integrity, competence and diligence – ultimately, this is about professionalism. As a result, it is appropriate for products outside of the mutual fund context. The only determining factor should be whether the product is retail-facing.

51) Are there other requirements that should be imposed to limit sales practices currently used to incentivize representatives to sell certain products?

The proposed requirements canvass the field of direct and indirect incentives that could put the sales practice on unequal footing.

52) What type of disclosure should be required for sales practices involving the distribution of securities that are not those of a publicly offered mutual fund, which are already subject to specific disclosure requirements?

Disclosure for securities other than publicly-offered mutual funds should mirror that for mutual funds to the extent possible. This should be evaluated on a principles basis, out of respect for the diversity of products and sales practices in the marketplace.

53) Should further guidance be provided regarding specific sales practices and how they should be evaluated in light of a registrant's general duties to his/her/its clients? If so, please provide detailed examples.

Further guidance is not required; no prescriptive guidance can possibly anticipate every situation or permutation of client, registrant and product in the marketplace. Guidance in respect of sales practices must fundamentally be principles-based, and the evaluation of a registrant's compliance with his/her/its duties must be done by a professional body that is capable of understanding the context of the events that have transpired.

Appendix B: Know your client

54) To what extent should the KYC obligation require registrants to collect tax information about the client? For example, what role should basic tax strategies have in respect of the suitability analysis conducted by registrants in respect of their clients?

The KYC obligation's expectations regarding the collection of tax information should be limited to a very basic level, such as an expectation that the advisor inquire regarding the client's employment status, current income, expected future income (including expectations regarding retirement or leaves of absence from remunerative activities) and investment holdings (including status of registered tax sheltered or tax deferred accounts and expectations of income from investments in non-registered accounts).

We do not wish to understate the importance of tax planning but the challenges are two-fold: i) taxation is a complicated area that demands an area of advisory specialization in its own right; and ii) given this complexity, in order to perform a fulsome tax analysis, the advisor would have to have complete knowledge of the client's tax situation. This is very challenging to accomplish, not least of which is because many clients are reticent to provide their complete tax information to their advisor as they (erroneously) view taxation as a private and separate matter from investment advice.

55) To what extent should a representative be allowed to open a new client account or move forward with a securities transaction if he or she is missing some or all of the client's KYC information? Should there be certain minimum elements of the KYC information that must be provided by the client without which a representative cannot open an account or process a securities transaction?

The minimum KYC elements that should be required in any event include client age, income, investment objectives and investment timeframe – that is, those elements that are needed to establish a basic risk profile. The advisor should have knowledge of these fundamental, overarching aspects of KYC details but transactions should be permissible even if the advisor is missing some or all of the client's KYC particulars. This is an area of professional judgment, which is once again why it is so important to professionalize the advisory sector, raise standards in the industry and establish a code of conduct, compliance to which is reviewable by a professional body.

56) Should additional guidance be provided in respect of risk profiles?

In the potential guidance, the CSA explicitly emphasizes the key role of the advisor's professional judgment in developing risk profiles – we completely agree with this sentiment, but if the CSA expects advisors to use the skill, care and judgment that is normally associated with professionals, we would also like to see the CSA commit to modernizing the regulatory framework so that financial advisors can organize as a true profession.

In terms of the necessity of additional guidance, the assessment of a client's relationship to investment risk requires a holistic review of the client's investment sophistication, objectives, timeframe and many other factors. It is not something that can be detailed in six bullet points that remind representatives of things to consider.

Further, it often seems to be implied in consultation papers such as these that it would be preferable to direct clients towards guaranteed products or high interest savings accounts;[13] while these products have a role for certain consumers (particularly with very short investment timeframes), these products pose a major risk of their clients running out of money due to their poor returns; this is particularly so if these products are considered for use in a retirement investment vehicle.

57) Are there circumstances where it may be appropriate for a representative to collect less detailed KYC information? If so, should there be additional guidance about whether more or less detailed KYC information may need to be collected, depending on the context?

Context does matter, and there will be situations where more or less detailed KYC information is appropriate. For retail clients, the overarching principle should be to collect sufficient KYC information so that the client can "tell their story". Some stories may need lesser detail – such as in the case of a scholarship plan where the objectives and timeframe are readily-understood, or an execution-only transactional relationship where the service is intended to be discrete – but the principles underpinning the KYC exercise are relevant in all retail-facing scenarios.

Again, we point out that to achieve its policy intentions regarding KYC, the CSA would do best to leverage the judgment of a professionalized advisory force. The real-world "context" of individual client situations cannot be adequately anticipated at the regulator level – it is a case-by-case evaluation, so the CSA should ensure that the front line "evaluators" (advisors) have the proficiency and ethics to perform the task.

Appendix D: Know your product – firm

58) Should we explicitly allow firms that do not have a product list to create a product review procedure instead of a shelf or would it be preferable to require such firms to create a product list?

The CSA should allow for a principles-based product review procedure. The creation of a specific product list would be a time-consuming and onerous procedure, and that product list would quickly become obsolete given the frequent product development cycle in the industry. In fact, the creation of a static product list could incentivize firms and representatives to overemphasize products that

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[13] For example, the Consultation Paper specifically mentions that firms must identify clients that are "suited to placing their money in cash deposits or guaranteed products because they are unwilling or unable to accept the risk of loss of capital" (at 39 OSCB 3983).

have already been vetted to make it onto the list, rather than encouraging them to keep an open mindset and consider new products on an as-needed basis.

59) Would additional guidance with respect to conducting a "fair and unbiased market investigation" be helpful or appreciated? If so, please provide any substantive suggestions you have in this regard.

We believe the guidance needs clarification. The obligation that the firm and representative have an understanding of the impact of the role of any given security in the client's broader portfolio is problematic, as clients may maintain accounts with more than one firm and representative. In such cases, it is very unlikely that the firm or representative will have knowledge of the contents of those other accounts and will therefore be ill-equipped to understand the impact of any one particular security on the client's broader portfolio. The extent of the firm or representative's analysis is necessarily limited to the portfolio that a particular client maintains with that firm or representative.

60) Would labels other than "proprietary product list" and "mixed/non-proprietary product list" be more effective? If so, please provide suggestions.

The proposed labels are straightforward and their implications would be easily understood by most consumers. However, as voiced in our response to question 15 above, we do not believe the distinction between proprietary and mixed/non-proprietary firms should be the focus of the CSA's efforts, if the policy intention is to ensure that firms investigate product options and offer broad choices suitable for their client base. Neither being proprietary or mixed/non-proprietary is determinative of whether a firm satisfies the CSA's policy intention.

61) Is the expectation that firms complete a market investigation, product comparison or product list optimization in a manner that is "most likely to meet the investment needs and objectives of its clients based on its client profiles" reasonable? If not, please explain your concern.

No, as proposed in the potential guidance, this is not a reasonable expectation. In regards to the market investigation, the CSA states that it need not take into account the entire universe of products that the firm is registered to advise on and/or trade in. But then it suggests that firms source external research that will be mandated to ostensibly do that very thing – in our view, anything less than a comprehensive, or at least very wide-ranging, review of the universe of products runs a very strong risk of being found to be deficient by the CSA, particularly as the CSA will be making its judgment on an *ex post* basis.

This type of comprehensive external research is likely to be beyond the financial resources of independent firms and will create market conditions that strongly favour the larger, bank-dominated investment dealers that have the resources and scale to make the commissioning of external reports (and consequently, compliance with the CSA's guidance) viable.

Appendix E: Suitability

Product selection suitability

62) What, if any, unintended consequences could result from setting an expectation in the context of the suitability obligation that registrants must identify products both that are suitable and that are the most likely to achieve the investment needs and objectives of the client? If unintended consequences exist, do the benefits of this proposal outweigh such consequences?

The CSA's guidance on product selection suitability creates implications in situations where a client order involves a specific security that is outside the firm's or representative's category of registration. This could include a client asking his or her mutual fund representative to purchase an exchange-traded fund or exempt product. In some situations, the firm or representative may not have the requisite knowledge of the product to make the expected assessment because they do not normally deal in that product.[14]

It would be unprofessional for representatives to purport to have the knowledge to make an assessment based on a cursory review of the product – so they should not be pressured into making such assessments through the setting of expectations in the proposed guidance. Further, it is unreasonable for the CSA to expect that the firm or representatives undertake thorough due diligence on every one-off product that they are asked about so long as there are products on the firm's approved product list, within the firm's category of registration, that are suitable and likely to meet the client's investment needs and objectives.

General suitability guidance and frequency

63) Should we provide further guidance on the suitability requirement in connection with ongoing decisions to hold a position?

As stated in our response to question 19 above, we believe that suitability assessments in regards to holding a position are unnecessary, absent material changes to other factors that would put the continued validity of the suitability assessment performed at the time of acquiring the security into question.

64) Should we provide further guidance on the frequency of the suitability analysis in connection with those registrant business models that may be based on one-time transactions? For example, when should a person or entity in such a relationship no longer be a client of the registrant for purposes of this ongoing obligation to conduct suitability reviews of the client's account?

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[14] We recognize that many mutual fund dealers and IIROC firms do offer exempt products and will be offering ETFs in the near future. However, the general point is that not all dealers and firms can offer products outside of their "traditional" registration category.

As stated previously, from our perspective, consumers should be made aware of and understand the distinction between business models that are based on one-time transactions and those that are based on holistic, long-term advisor-client relationships. The CSA should undertake efforts to ensure consumers' understanding that in the former business model, the quality of the suitability assessment will realistically be limited to that point in time (i.e., the time of the purchase or sale transaction). Only in the case of holistic advice relationships does it become feasible to maintain an ongoing obligation that is adjusted over time as clients' needs and objectives evolve.

Appendix H: Proposed regulatory best interest standard

65) Should the Standard of Care apply to unregistered firms (e.g., international advisers and international dealers) that are not required to be registered by reason of a statutory or discretionary exemption from registration, unless the Standard of Care is expressly waived by the regulator?

Our response to this question is not in regards specifically to a Regulatory BIS, which we do not support for the reasons discussed in Part 4 of this submission, but in regards to standards applicable to all financial services intermediaries serving Canadian retail investors generally. We believe that regardless of whether the intermediary is international and otherwise exempt from Canadian registration, if that intermediary is normally in the business of serving Canadian retail investors, the intermediary should be required to adhere to the same standards as their domestic counterparts.

66) Do you believe that the Standard of Care is inconsistent with any current element of securities legislation? If so, please explain.

It is unclear how the Regulatory BIS will interact with other standards currently in effect; the CSA's guidance that "to the extent of any overlap between complying with the Standard of Care and complying with any other regulatory requirement under securities legislation, firms and representatives must comply with both…" may sound fine in the guidance, but it is uncertain how these varying standards will operate collectively in day-to-day practice.

If the Regulatory BIS is supposed to be a "foundational standard of conduct" that informs other core activities such as KYC, KYP and suitability, it is unclear how it modifies, or whether it modifies at all, the standards set for registrants that are already subject to a fiduciary duty, such as portfolio managers, or MFDA or IIROC registrants, the latter two SROs having expressed their own form of best interest duty that is, like the Regulatory BIS, intended to be something less than a full fiduciary duty.

For example, the MFDA has expressed its view that approved persons should take "the most conservative approach and act in the best interests of the client"[15] and Rule 2.1.4 requires conflicts of interest to be "addressed by the exercise of responsible business judgment influenced only by the best interests of the client."[16] However, the MFDA does not enforce these concepts as fiduciary duties.

IIROC Dealer Member Rule 42 is a principles-based rule which is periodically supplemented by guidance.[17] According to the rule and accompanying guidance, IIROC members must address material conflicts of interest that do, or could, arise "in a fair, equitable and transparent manner and considering the best interests of the client or clients." Further, "[a]ny existing or potential material conflict of interest that cannot be addressed in that manner must be avoided."[18]

In a recent commentary on Rule 42, IIROC is at pains to stress how member firms and their representatives are to manage conflicts of interest vis-à-vis the "best interest of the client":

> This principle is also specifically reflected in our rule that requires a firm's *representatives* to address material conflicts of interest – whether existing or potential – in a manner that is consistent with the best interest of the client. Recognizing that *firms* must balance the interests of multiple clients simultaneously, our rule requires them to address such conflicts in a manner that *considers* the best interest of the client.[19]
>
> (Emphases in original)

The obligation that the registrant address the conflict (i) by considering; and (ii) in a manner that is consistent with the best interest of the client is significant because consideration of, and consistency with, do not automatically mean that the IIROC member, to satisfy the best interest obligation, must always act <u>solely</u> in the client's best interest. Rule 42 is therefore not an absolute — in other words, it is not a full-blown fiduciary obligation. Indeed, in response to a comment that Rule 42's reference to the "best interests of the client" may be interpreted as creating a fiduciary duty, IIROC stated that:

> IIROC does not believe that the phrase "best interests of the client" on its own creates a fiduciary duty relating to existing or potential material conflicts of interest, and it is not IIROC's intention to do so. Whether or not a fiduciary duty exists in an account relationship depends on the facts of each case, including, among other things, the services being provided to the client and the degree to which the client relies on the firm/adviser in

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[15] MFDA Staff Notice MSN-0069, *Suitability*. Online at: http://www.mfda.ca/regulation/MSN/MSN-0069.pdf.
[16] MFDA Rule 2.1.4, *Conflicts of Interest*. Online at: http://www.mfda.ca/regulation/rules/RulesJul15-16.pdf.
[17] IIROC Guidance Notice 12-0108, "Client Relationship Model – Guidance," March 26, 2012.
[18] IIROC Guidance Notice 16-0068, "Managing Conflicts in the Best Interest of the Client," April 6, 2016.
[19] *Ibid.*

> making investment decisions. While the standard of conduct established by the proposal is not as high as the fiduciary standard, it is intended to strengthen investor protection by clarifying IIROC's expectations on how existing or potential material conflicts of interest are to be addressed as between the Approved Person and the client, as well as between the Dealer Member and clients generally.[20]

Although IIROC has stated that its intention is not to create a fiduciary duty, the conflict of interest rule applicable to Approved Persons suggests a higher standard than the rule applicable to the Dealer Member (which only requires "considering" the client's best interest).[21] So, while Rule 42 does not create a fiduciary duty, it is clearly intended to impose a very high standard that falls just short of fiduciary duty.

In short, it is unclear where the Regulatory BIS falls on the spectrum of existing duties, how it interacts with those other duties and how it is to be understood and utilized by firms, advisors and clients. It is difficult to conceptualize and onerous to comply with these varying standards that seem like their only true differences come down to the interpretation of the particular regulator invoking the duty – and none of these regulators have any connection to the real-world practice of financial advice. For advisors, the prospect of all of this is greatly worrying.

67) Do you agree that the Standard of Care should not apply to the underwriting activity and corporate finance advisory services described above? If not, please explain.

If these activities are not to attract the same standard of care, there should be at a minimum a client-signed acknowledgement that the IIROC underwriting team is “operating under an exemption from Regulatory BIS requirements.” In other words, there should be full disclosure. Every accountant and lawyer working on the file has professional standards. We do not understand why an exemption without disclosure would fit here and not for some individual clients.

68) Do you think this expectation is appropriate when the level of sophistication of the firm and its clients is similar, such as when firms deal with institutional clients?

As stated in our response to Question 44, we believe that there is a clear distinction between retail investors and institutional investors, with the latter having the sophistication (or the resources to hire external advisors with the sophistication) to independently protect their interests in regards to

[20] “IIROC response to comments on Client Relationship Model Rules and amendments to IIROC Dealer Member Rules 200 and 1300,” March 26, 2012. Online at http://www.iiroc.ca/Documents/2012/A6F10441-3A89-4BFD-8BB1-D9B7C7119D88_en.pdf.
[21] Canadian Securities Administrators, Consultation Paper 33-403: *The Standard of Conduct for Advisers and Dealers*, p. 9569, at note 55.

the interpretation of laws and agreements. Therefore, for institutional investors, there should be no biased initial starting point for interpretation principles.

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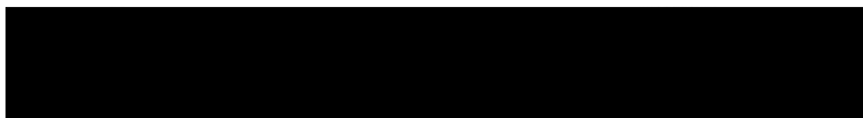
We look forward to working with the CSA as it proceeds with modernizing the regulatory structure governing the advisor-client relationship – including the fundamental re-thinking of the existing regulatory framework from an antiquated product-centered one to a modern client relationship-focused framework. Should you have any questions, please do not hesitate to contact the undersigned, or Ed Skwarek, Vice President, Regulatory Affairs and Public Affairs at 416-342-9837 or eskwarek@advocis.ca.

Sincerely,



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