BMO Financial Group

Via Email

September 30, 2016

Canadian Securities Administrators
comments@osc.gov.on.ca, consulation-en-cours@lautorite.qc.ca

Re: Canadian Securities Administrators Consultation Paper 33-404

BMO Wealth Management, on behalf of BMO Asset Management Inc., BMO Investments Inc., BMO InvestorLine Inc., BMO Nesbitt Burns Inc. and BMO Private Investment Counsel Inc., welcomes the opportunity to comment on the CSA's Consultation Paper.

We offer our clients a wide range of wealth management products and services, including in-person and online advice, discretionary investment management and online self-directed investing.

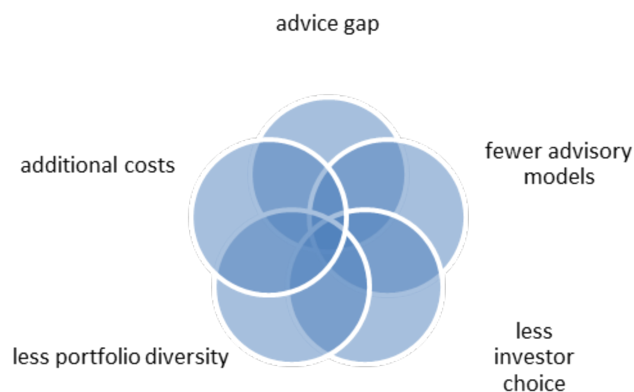
We support the overall investor protection objectives of the proposed reforms, which seek to better align the interests of registrants with the interests of clients, improve outcomes for clients and clarify the nature of the client-registrant relationship. We agree the proposed reforms will change how we engage with our clients. While some investors will benefit from the reforms, we are concerned many will not.

We direct the CSA to the industry association letters for each of the Canadian Bankers Association, Investment Funds Institute of Canada, Investment Industry Association of Canada and Portfolio Management Association of Canada, all of which highlight potential consequences of the proposed reforms.

To further assist the CSA, we discuss below potential unintended consequences and what the CSA can do to avoid them while still achieving the CSA's overall objective.

Impact on investors

The proposed reforms may negatively impact investors in the following ways:



The CSA should assess the benefits of the reforms against these impacts to investors:

- a mandated one-size fits all advisory model – *can this meet all investor needs?*
- additional investment management costs – *how will this impact investors?*
- reduced range of product choice – *will this impact investor outcomes?*
- less diversity in investment portfolios – *will this impact investor outcomes?*
- loss of access to investment advice – *which investors will be left out and at what cost?*

With the exception of the order execution-only service model, the proposed reforms do not accommodate different types of investment products and service models. A one-size fits all advisory model, similar to that of an in-person financial planner or portfolio manager, which is effectively being mandated by the reforms, changes the existing, flexible regime. These wholesale changes to the client-registrant relationship will cause dealers and advisers to assess the cost of compliance against the viability of various parts of their businesses.

For example, firms may choose to reduce their product shelf to facilitate compliance and reduce potential liability associated with additional know-your-product and suitability obligations. Firms will be selective in how they reduce their shelves. Firms may also be reluctant to recommend innovative products or products higher up the risk/reward continuum. Finally, firms may shift costs to clients, or impose minimum account size or fee requirements, with less affluent clients being unwilling or unable to satisfy those requirements. This will cause an advice gap.

To avoid these impacts and ensure equal access to a broad spectrum of investors, the CSA should tailor the proposed reforms to continue to enable a variety of advisory models. The reforms should clearly recognize that new, different and innovative advice models currently exist and should be allowed to develop further. The CSA must be careful not to impose unnecessary obligations, restrictions and potential liabilities on these models which could chill digital solutions and innovation, like our adviceDirect, which provides online advice, and BMO SmartFolio, which provides access to professionally-managed ETF portfolios.

Impact on the Capital Markets

In addition to impacting investors, the CSA should also consider what consequences the targeted reforms could have on the Canadian capital markets. If firms reduce their product shelves, it will impact market liquidity, in particular where firms shift to proprietary-only products. The reduction could also impact the types of products offered, with a shift away from higher risk products. A move by product manufacturers to lower risk products based on demand will negatively impact capital markets as lower risk products draw less investment (including foreign investment) into the system.

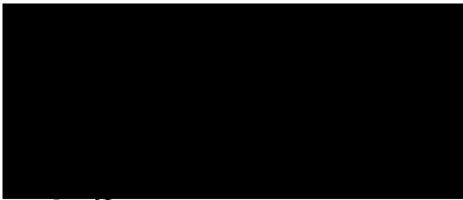
Need for impact assessment

We urge the CSA to consider the impact (beneficial and harmful) of the proposals on stakeholders and capital markets. This should include a full assessment of recent reforms (such as the recently announced multi-year research project to measure the impacts of CRM2 and POS). The CSA should also consider pending reforms, such as the proposed mutual fund fee reform, and the experience of other jurisdictions with similar reform initiatives. We note the UK is now considering how to address the advice gap created by its recent reforms.

Best Interest Standard
We agree with the concerns expressed by the majority of CSA members on the proposed regulatory best interest standard. Any such reform should be harmonized across the country.

Moving forward
We appreciate the opportunity to comment on the proposals and look forward to participating in upcoming roundtable discussions to provide further input. We also invite members of the CSA to meet with us to learn about our diverse products and services. Understanding how we operate today will help the CSA assess the appropriateness and potential impact of the reforms on investors, registrants and the capital markets. Please see Appendix A which provides some suggestions on how the CSA can tailor the proposed reforms to help address our concerns.

Regards,



Gilles G. Ouellette
Group Head, BMO Wealth Management

APPENDIX A

- *Modify the reforms to retain flexibility for traditional advisory models*

    - Clearly support the current graduated framework that permits different advisory models.

    - Remove or refine those areas of proposed reform which contribute to one standard. These include:

        - KYC and suitability reforms relating to non-securities strategies, targeted rate of return and client tax position. In addition to creating one model of advice, these may also mislead clients into thinking they are receiving full financial planning and tax advice when they are not.

        - KYC and suitability reforms relating to annual refreshes. These annual refreshes will be extremely costly and cumbersome. To mitigate this, and related consequences, the CSA should preserve flexibility for registrants in refreshing client and investment information. This should continue to be tailored for different advisory models.

        - Suitability obligations for “holds”. The CSA should clarify that a suitability obligation for “holds” only arises on client direction or registrant recommendation to hold.

- *Modify the reforms to align with existing SRO enhanced standards*

    - Many SRO requirements already enhance the dealer/adviser obligations in National Instrument 31-103. The CSA should consider using these requirements to provide any further enhancements to meet its policy objectives and to minimize the cost of compliance across registrants. For example:

        - Consider IIROC’s and the MFDA’s approach to conflicts management which are well established and understood by relevant firms and do not have the same ambiguities as the proposed reforms.

        - Consider IIROC’s and the MFDA’s suitability rules.

- *Consider / clarify how the targeted reforms impact online advisory models*

    - Online platforms are relatively new advisory models, and innovation in this area will only increase. It is important to consider how the reforms impact these models or may prohibit further innovation in this area.

- For example, online platforms collect KYC information to ensure clients are suitable. This usually results in assessing client information to determine suitability to a model investment portfolio. KYC or suitability obligations that prohibit this type of classification and/or require assessments outside of securities transactions (such as debt repayment) may not align with online platforms.

- *Clarify that the business model of an integrated mutual fund dealer and manufacturer is permitted*

  - It is unclear how the conflict of interest and KYP proposals permit this model.

- *Refine KYP and suitability reforms to maintain flexibility for registrant due diligence*

  - In assessing suitability, registrants with large shelves cannot know every product to the detail required by the proposed reforms and they cannot do the product comparison the reforms impose.

  - To avoid firms restricting their shelves, the CSA should remove this requirement or modify it. For example, the requirement could be refined to require registrants to understand and have compared the recommended product relative to a sample of other similar products on the firm's shelf (not the entire shelf).

- *Titles*
  - The CSA should be sensitive to the range of advisory models in Canada and use titling to assist clients in understanding services provided by different types of advisors.

  - The titling reforms should not prevent representatives who provide financial planning services from having that term in their title. If the reforms do so, they will create confusion rather than clarify it.

- *Role of UDP / CCO*

  - Consider whether clarifying UDP and CCO responsibilities is necessary. Sections 5.1 and 5.2 of National Instrument 31-103 are broadly worded to cover these responsibilities. Specific tailoring to reference oversight with a particular obligation may create confusion and seems unnecessary.