Via email

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Mr. Robert Blair, Secretary (Acting)
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Me Anne-Marie Beaudoin, Corporate Secretary
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September 30, 2016

Dear Me Beaudoin and Mr. Blair,

Re: Consultation Paper 33-404 – Proposals to Enhance the Obligation of Advisers, Dealers and Representatives Towards Their Clients

This comment letter is being submitted on behalf of the following RBC entities: RBC Dominion Securities Inc.; RBC Phillips, Hager & North Investment Counsel Inc.; Royal Mutual Funds Inc.; RBC Global Asset Management Inc.; RBC Direct Investing Inc.; and Phillips, Hager & North Investment Funds Ltd. We are writing in response to the Canadian Securities Administrators' ("CSA") request for comment on Consultation Paper 33-404, published on April 28, 2016 ("Consultation Paper").

Introduction

Our clients and their investment success are a cornerstone of RBC's purpose to help clients thrive and communities prosper. Earning the right to be our clients' first choice for financial services is a core value of RBC. This and other values, such as accountability and integrity, guide, unite and inspire us to do what's right for our clients.

In keeping with these values and practices, we welcome the CSA's efforts to improve retail clients' understanding of their relationship with their representative. We agree that the interests of clients should be of paramount importance while ensuring access by investors to the financial services they want and need to achieve their investment goals. We believe it is essential for reforms that are ultimately implemented to appropriately support clients' desire for choice in the level of service they need at the price they are willing to pay. We caution against implementing any reform that could detrimentally impact any client's access to affordable investment advice.

We support the CSA's approach to review industry and public input before deciding whether, and the extent to which, the targeted reforms may be adopted, and we view this Consultation Paper as an important step in the consideration of these complex and important issues. The preliminary analysis and commentary on relevant international developments contained in the Consultation Paper serve as a good starting point for this consultation, which should be reviewed within the broader context of recent and ongoing regulatory changes. We would like to take this opportunity (i) to outline our general views concerning the desirability and feasibility of adopting the ten key targeted reforms and the manner in which we believe they may be adopted; and (ii) to provide our views on the proposed introduction of a regulatory best interest obligation.

Proposed Targeted Reforms

In our view, an effective and efficient policy solution should build on current regulatory requirements. It is expected that current efforts to implement various regulatory developments, as well as other recent regulatory initiatives which have been implemented since the previous consultation by the CSA on this matter, would result in increased transparency for investors and encourage registrants of all categories to enhance their existing practices. Of note, retail investors are currently provided with relationship disclosure documents under Client Relationship Model ("CRM") rules and are more fully informed of, among other things, their client account relationships, applicable fees and charges, suitability assessments and material conflicts of interest between investors and the registrant. Similarly, the Point of Sale Disclosure ("POS") requirements are intended, in part, to inform clients of charges and applicable fees related to mutual fund securities, as well as to provide product information in order to educate clients. Further, CRM requirements, soon to be implemented, will provide clients with detailed information in respect of the performance of their investments and compensation received in connection therewith. Given that the regulatory objectives of CRM and the POS project were to "raise the bar on industry professionalism and bolster investor confidence", consideration for adding further layers of requirements should take into account the actual incremental benefits that investors will experience in practice. To that end, the recent announcement by the CSA of a multi-year project to measure the impact of CRM2 and POS on investors and the industry is timely. We submit that it may be beneficial to complete this review before any further changes in these areas are made.

Any further regulatory change should ideally be harmonized and implemented consistently by each member of the CSA so as to avoid uncertainty and inefficiencies. For registrants subject to supervision in more than one jurisdiction, harmonisation of regulation is of paramount importance to ensure equal regulatory support for clients as well as consistency of standards and regulatory expectations.

Increased transparency for clients should also be tied to efforts to educate consumers in order to maximize the benefits. Further, it should be recognized that a "one-size-fits-all" regulatory approach to clients is inconsistent with the varied interests of clients. There are clients who choose a managed account because they want to benefit from the services of an experienced professional with minimal or no involvement on the part of the client in the day-to-day handling of the account. There are also clients who want a commission based or execution only account, making all investment decisions with little or no direction from a representative and with limited willingness for a relationship with a representative or for additional disclosure documents from a registrant. There are clients who fall somewhere in between. Investors should not be disadvantaged by the imposition of heightened regulations, which may prevent them from receiving advice that assists with meeting basic goals, such as saving for education. It should also be recognized that registrants have different business models and different value propositions (even within a single dealer). Accordingly, we submit that this likely requires a more tailored approach by the CSA to addressing the different experiences, needs and wants of a diverse investing population.

We feel there is a need for a differentiated regulatory approach which acknowledges the diversity of client experience and needs as well as the variety of relationships that clients have with their representatives. There is a long held acceptance of the different experiences and investing objectives of institutional and other sophisticated investors compared to retail investors, which is reflected in the differing regulatory regime applicable to institutional investors. This graduated approach to regulation should be extended and applied to a variety of client types. Those in most need of support will receive higher levels of regulatory protection than those with a stated preference for greater autonomy in their dealings with a registrant. The implementation of a comprehensive regulatory regime should not address only one segment of the investing public at the potential expense of others; rather, the interests of all differing types of clients must be understood and taken into account.

Finally, there are potential unintended consequences of the proposed targeted reforms as drafted. The creation of additional policies, processes and procedures that will be required to demonstrate compliance with the targeted reforms will likely involve significant additional time and expense, at the time of implementation and on an ongoing basis, in order to comply with the various new requirements. This in turn may lead to a reduction in investment products made available to clients in order to reduce the significant cost and compliance burdens associated with offering a broader suite of investment products. In the case of the proposal that registrants identify as having a proprietary or mixed list of products, it may drive some registrants to adopt a restricted proprietary model with fewer available products which would mean reduced choice for clients.

In respect of each of the targeted reforms we have the following comments. We have added footnotes to reference the specific questions asked by the CSA, where appropriate.

1. Conflicts of Interest – General Obligation

We believe that this would be better articulated as a requirement that any disclosure provided to clients be provided in a "client friendly" manner, using plain language rather than imputing an expectation of meaningfulness to the client[1]. A minimum expectation that a conflict of interest will be addressed in a fair, transparent and equitable manner and permitting registrants to apply client-friendly disclosure which recognizes its own unique client base will benefit both the investing public and the industry. The expectation that a registrant has a "reasonable basis for believing that clients fully understand" and has provided "informed and specific consent" suggests a requirement to demonstrate compliance by way of an acknowledgement of receipt signed by a client. While such an acknowledgement may seem like a useful tool to evidence understanding, we are of the view that the downsides outweigh any upside; it is an administrative burden to clients, and unreflective of a typical communication pattern within a client relationship which frequently relies on telephone or email. We also believe such an acknowledgement would be perceived by clients as adding limited value to the client. A plain language requirement which may, if necessary, be explained by the representative to the client to facilitate understanding, dovetails well with the requirement for an "effective disclosure" as well as an overall expectation of transparency and fairness in dealing with clients. Unless prescribed otherwise, we would view "effective disclosure" as being a disclosure written in plain, client-friendly language.

[1] Questions 1 and 2

Appendix A

Responding to conflicts of interest:
Further guidance is needed to understand what will be regarded as a “material conflict of interest” and “materially opposed” (in the case of guidance with respect to institutional clients). Currently the processes and disclosures proposed by the CSA hinge on the threshold of materiality. Where the threshold is set too low, administration by the industry will be cumbersome. Moreover, as currently recognized in NI 33-103CP there are certain conflicts of interest which are obvious to clients and do not require disclosure to clients (e.g., mutual funds managed by an affiliate where the names of the registrant and affiliated issuer are sufficiently similar). We recommend the continued applicability of such exceptions as well as the addition of similar common sense exceptions, e.g., structured notes and ETFs issued by an affiliate where the names of the registrant and affiliates issuer are sufficiently similar.

We question the expectation that overall performance should be used as a basis for selecting or evaluating a registrant. The past performance of a registrant is not necessarily an indication of its future performance, and a client should be dissuaded from basing an important decision on the past performance of a firm. With respect to the expectations of the CSA around disclosure, we note that the proposed disclosure of all outside business activities of the firm and applicable representatives may become an extremely onerous task involving potentially a considerable volume of disclosure documentation for clients. It should be noted that there are existing IIROC, MFDA and provincial securities regulator requirements and associated processes for the approval of outside business interests and we would recommend that a similar process be utilized under this targeted reform.

With respect to the guidance provided for institutional clients, we recommend consistent use of regulatory terminology and definitions and are therefore opposed to the introduction of another definition to add to that which is already in place for institutional or permitted clients[2].

2. Know Your Client

The KYC obligation is among the most fundamental obligations owed by a registrant to its client. It requires a meaningful dialogue with the client to obtain a solid understanding of the needs and objectives of the client as well as to explain a proposed strategy and how it will be suitable for the client given the client’s needs and objectives. When undertaken properly it allows a representative to collect a wide variety of information in order to create a holistic picture of the client which may then be applied in the recommendation of products to ensure compatibility of client and product.

It should be recognised that the representative in performing the KYC assessment is doing so in his/her capacity as an individual registrant and not as a tax or other specialist. Although basic tax or insurance information may be obtained, it is done solely for the purpose of building that KYC picture. The suitability and KYC proposals assume a representative will have a 360 degree viewpoint of the client encompassing all investment accounts, insurance and other banking arrangements. Although a client may be willing to disclose the fact that there is a loan outstanding or that there is a brokerage account held at another financial institution, the client may not be willing to disclose the precise terms of the loans or even be able to disclose in detail the assets held at another institution. There are many reasons for such reluctance to disclose, for example, privacy concerns, a clients’ view that such information is irrelevant to the provision of the level of investment services provided by the representative or the fact that the client

[2] Questions 46 and 47

may already have tax and accounting professionals performing work that is extraneous to the client's relationship with the registrant. Recognizing this, we advise our clients to consult with independent legal or tax advisors. Any tax driven investment strategy should be driven by the client in consultation with a tax specialist with knowledge of all of the client's tax circumstances

Many clients do not want advice which extends beyond their relationship with the representative (whether discretionary, advisory, commission based or execution only), either because it is unnecessary in the context of their account type or relationship type or because it involves a cost they are unwilling or unable to afford. Even where the representative may have been informed of the constituents of a client portfolio held elsewhere, the information may have been inaccurate or, as a portfolio is dynamic and evolving through ongoing investing, the information may rapidly become outdated. Similarly clients may not alert representatives to the fact that an insurance policy has changed or a loan has been taken or repaid[3]. As such, the exclusion of such details from the KYC assessment should not lead one to assume that care has not been taken in the performance of the assessment. More importantly, the exclusion *by the client* of such information means that a representative could never perform the level of assessment mandated by this proposal[4].

The proposed targeted reforms also fail to recognize the need to be able to offer, at the client's option, specific goal-oriented investment advice, such as for education, vacation, home repairs/remodels or to supplement existing retirement plans available through employers.

In respect of the proposal to codify a KYC form, we are of the view that such a codification by the CSA would be duplicative of existing requirements. Further, the codification in itself would by necessity become a lengthy and difficult process if it were to reflect accurately the different business models of registrants as well as the diverse nature of the investing public[5].

The requirement to complete a KYC form (and to have it signed) does not reflect the common situation where a client may disclose material changes during a telephone conversation with the representative or by way of email. We believe that flexibility is required to recognize the various means by which clients choose to communicate with their representatives. A more practical approach would be to allow for alternative evidence of approval, consistent with common practice.

Further guidance is needed as to what is meant by it being "reasonably apparent" that a client's information is not complete or accurate. As mentioned, clients are frequently reluctant to disclose information they feel is unnecessary to the investing relationship.

3 And 4. Know Your Product – Representative and Firm

We have significant concerns with the proposals to require (1) a representative to understand and to consider the structure, product strategy, features, costs and risks of each security on the registrant's product list, or (2) a registrant to identify as having a proprietary or mixed/non-proprietary list.

The former creates difficulty for those representatives associated with registrants which may have tens of thousands of products available on the registrant's product shelf. Registrants already have available for

[3] Question 16

[4] Questions 4 and 54

[5] Question 5

their representatives various tools which allow a representative to understand and to explain why a product is suitable for a particular client, including (i) dedicated internal research or educational teams, (ii) third party research materials and (iii) risk rating tools. Most registrants will also have a product approval committee comprised of business, legal and compliance representatives to review and to advise on whether a product should be added to a registrant's shelf. Such committees undertake a due diligence review of factors such as product structure, strategy, risks, costs and liquidity. It is on the basis of this due diligence review that a product will or will not be added to a shelf. The creation of additional tools to allow the level of comparison sufficient to demonstrate compliance with this proposal will involve significant cost and time expenditure by registrants and may not provide sufficient benefits so as to justify the efforts and expense required to comply[6].

The requirement to identify having a proprietary or mixed/non-proprietary list fails to contemplate sufficiently various business models, which may include different channels within a single registrant. In our view a mixed offering of proprietary and non-proprietary products is frequently made available to cover gaps in a proprietary offering or simply to offer greater product choice to clients. This requirement may also have the unintended consequence of limiting client mobility. A client choosing to move an account from a non-proprietary dealer to a proprietary dealer could be hindered from exercising that choice and be required to dispose of assets which do not form part of the proprietary firm's shelf and potentially incurring a tax liability in doing so. Clients move between registrants for many reasons, including relationship, price, quality of service or convenience. This proposed targeted reform should not act as a barrier to client mobility.

The proposal that a registrant perform an annual review of client profiles, particularly given the range of clients and client types as well as differing business models, is not likely to add much value but will impose significant administrative burden on registrants.[7] The administrative and cost burden which will result from compliance with this proposal may force some registrants to adopt a restricted proprietary model. Overall this could result in reduced choice and poorer quality choice of products within the industry[8].

Further, we recommend order-execution only firms be exempt from this requirement. In accordance with current regulatory requirements, such firms collect minimal KYC information; thus the benefit of conducting an annual review is questionable. Clients who make their own investment decisions without receiving advice or recommendations from registrants will naturally gravitate to the firms that offer the products they are interested in purchasing.

The proposal that a firm should identify products "most likely to meet the investment needs" sets an impossibly high bar, and may result, for some registrants, in reducing the number of investment products they offer and to offer a narrower range of low-risk products. We suggest amending the requirement to account for reasonable professional judgment applied at the time of recommendation. Otherwise, this proposal is likely to result in retrospective standards in considering the suitability of a recommendation previously made.

Requiring a written report, which describes internal processes for a market investigation, including the use of research reports, to demonstrate that such a meaningful market investigation has occurred in

[6] Question 7

[7] Question 14

[8] Questions 8, 9, 12 and 13

choosing products, will add little value and operates only to duplicate the due diligence review undertaken by product approval committees. This proposal also fails to recognize commercial reality where products are frequently added to the shelf, following an extensive due diligence review, which may be on the basis of a request from a motivated investor or a diligent representative[9].

5. Suitability

When the KYC process has been undertaken properly it allows a representative to collect a wide variety of information in order to create a holistic picture of the client and to advise upon an investment strategy for the portfolio as a whole. It is that holistic picture which may then be applied by the representative in the recommendation of products to ensure compatibility of client and product. The inclusion of the consideration of basic financial strategies as well as matters such as basic asset allocation in the suitability assessment is unnecessary as this information should already form part of the overall investment strategy recommended by the representative in performing KYC and advising on portfolio construction. Consideration of basic financial strategies as well as matters such as basic asset allocation needs to form part of the client's overall portfolio strategy. Looking at these matters at the time of an individual transaction is too late – the holistic picture should inform overall investment strategy. A requirement to assess these matters at the time of a transaction suggests that an entire KYC assessment may be needed each time a client wants to transact, which is a significant administrative burden for clients.

The suitability and KYC proposals each fail to recognise the full spectrum of clients and the wants and needs of such diverse clients. This is clear from the expectation that representative "reasonably should have known" that a client's information has materially changed. Many clients, for reasons which may include privacy, fail to disclose information to the extent necessary to allow a representative to gauge whether there have been changes to that client's circumstances. Accordingly, further guidance is needed as to the obligation imposed upon a representative, where that representative "reasonably should have known" that a client's information has materially changed. As mentioned within the paragraphs in which we discuss the targeted reform pertaining to KYC, clients are frequently reluctant to disclose information they feel is unnecessary to the investing relationship; accordingly, unless the representative has specifically been informed of a matter, he/she cannot reasonably infer that the matter has materially changed.

Further, as previously discussed, the application of a "most likely to achieve the client's investment needs and objectives" standard sets an excessively high bar. As a result, this may simply result in low risk products being made available by certain registrants to the investing public with the resulting cost to clients of poorer investment choice and returns. It is important to note that cost is just one of the factors to be considered in assessing whether a product and client are compatible[10].

6. Relationship Disclosure

We are supportive of disclosure to clients using plain language in a client-friendly manner. However, applying a general standard, with uncertain application, which may then be adjudicated retrospectively, is not in the best interests of either the client or registrant. Instead a requirement to provide client-friendly

[9] Question 58

[10] Questions 17 and 62

disclosure which takes into account a registrant’s own unique client base will benefit both the industry and the investing public[11].

We do not understand the policy purpose underlying the proposal to disclose the proportion of proprietary products offered by a firm offering a mixed/non-proprietary platform. The proportion may change frequently and we question the utility of such disclosure in the first place. If the policy objective is to ensure that a firm describing itself as an open architecture firm is truly that, there are other more practical ways to achieve this objective. The proposal to require proprietary firms or firms in restricted registration categories to disclose to clients that non-proprietary products do not form part of a suitability analysis and whether such non-proprietary products are better, worse or equal in meeting client needs and objectives would require an extensive ongoing review and comparison of products. We cannot see how this proposal enhances transparency for clients or furthers their best interests[12].

We also do not understand the proposed disclosure required for firms registered in restricted categories as we are of the view that it may create regulatory arbitrage; the proposed disclosure seems to imply that some registrants are inherently better than others by virtue of their registration category[13].

7. Proficiency

We are supportive of the proposed heightening of the proficiency requirements and encourage the CSA to harmonize proficiency requirements across different regulatory platforms including continuing education requirements, provided that such requirements align with IIROC’s existing proficiency requirements.

8. Titles and Designations

We are supportive of the use of descriptive plain language business titles that are not misleading to clients. However, we are concerned that an overly-prescriptive approach to business titles would be ineffective in reducing client confusion and, in the case of the proposed alternatives set out in the Consultation Paper (as discussed below), potentially counter-productive to the goal of investor knowledge and understanding. We would also caution against the use of industry jargon, including terms such as “securities” in titles as it will be unclear to clients who lack the necessary industry knowledge and are more likely to understand the term “investment”. We believe that a principled but flexible approach to business titles which demands the use of simple, intuitive and non-misleading terminology, combined with effective client disclosure, would be preferable. We would point out that in the case of IIROC member firms, regulatory guidance on this issue has been provided by way of IIROC Notice 14-0073 (March 24, 2014), and we agree with IIROC’s functional approach to business titles and designations, which also requires effective public disclosure as well as policies and procedures in support of the goal of transparency to potential and existing clients, particularly more vulnerable and less sophisticated clients.

Rather than making changes to the client-facing business titles we recommend instead that the relationship disclosure document be used as a tool to educate clients about the precise role and responsibility of the registered persons with whom the client will deal at a registrant. We are of the view

[11] Question 23

[12] Question 24

[13] Question 23

that this approach aligns more closely with the proposals for effective disclosure elsewhere in this Consultation Paper and provides a more appropriate learning tool for clients.

With respect to the proposed title changes put forward, we are of the view that with respect to Alternative 1, the emphasis on "client", rather than "clients", suggests that an individual who has both discretionary and non-discretionary clients may need to provide a separate business card to each category of clients. With respect to discretionary management, the title "portfolio manager" would be preferable and less confusing than "securities advisor – portfolio management", although in either case it would remain unclear, without further guidance, as to what is expected of an individual with both discretionary and non-discretionary clients. We are generally concerned that the use of the term "securities" in the proposed titles of Alternative 1 amounts to industry jargon, and would be less clear and meaningful from the perspective of a retail client than a term such as "investment" – e.g., a title such as "investment advisor" or "investment counsellor" would be preferable to the title "securities advisor" as its meaning will likely be more intuitive to an average investor than "securities advisor". Moreover, the use of the word "securities" in a title fails to contemplate that representatives also advise on insurance products, e.g., segregated funds, and those issued under the Bank Act, e.g. principal protected notes. For those professionals with broader full-service financial planning acumen, a title such as "wealth advisor" might more fittingly align with the expectations of certain clients who seek holistic wealth management services.

With respect to Alternative 2 there does not seem to be a recognition that a representative of a dealer whose clients hold non-discretionary accounts is still providing investment advice and is servicing clients as considerably more than a salesperson; accordingly, the business title "salesperson" does not provide sufficient clarity to a client and devalues the types of services being provided. Also the use of the title of "advisor" in Alternative 2 may confuse clients familiar with the use of that title for non-discretionary relationships. This title also does not reflect the high proficiency standards and experience required for individuals to provide discretionary investment management services. We are generally concerned that the proposed titles of Alternatives 2 and 3 are lacking in descriptive impact and would therefore not be sufficiently meaningful to clients. For example, we do not think that the use of individual categories of registration (Alternative 3) would resonate with clients as they may find such industry terminology to be meaningless.

We are in agreement that a registrant should have policies and procedures in place to validate the designations used by their representatives[14].

9. Role of UDP and CCO

We support the proposed clarification of the roles of the UDP and CCO in NI 31-103, which is generally aligned with existing SRO guidance with respect to the compliance function and oversight at the member firms. We would appreciate further guidance in connection with the enhanced responsibilities of the UDP and CCO in order to assess the impact on the establishment and monitoring of supervisory and compliance systems.

Further, in managing conflicts of interest we support a principles-based approach which would allow firms to develop processes that are reflective of the size and type of business, including periodic testing and reporting on effectiveness of the framework.

[14] Question 33

10. Statutory Fiduciary Duty When a Client Grants the Firm Discretionary Authority

At this time it does not appear to us that the CSA has identified a regulatory gap which necessitates a statutory codification of the well-articulated and well-understood concept, which derives from common law, of a fiduciary relationship. Continued reliance on the common law concept allows for the necessary differentiation which arises in the case of institutional clients as well as for client relationships where the client does not wholly rely on the advice of the representative and instead seeks to exercise discretion or to provide direction in respect of the purported discretionary portfolio. We believe that this proposed targeted reform is unnecessary – the benefit of harmonization of a fiduciary standard has already been achieved at common law. Furthermore we view as problematic the blanket application of a statutory fiduciary standard to client relationships which by virtue of the exercise of discretion by a client or the levels of sophistication of the client are missing the necessary element of reliance to make it a truly discretionary relationship[15].

Proposed Regulatory Best Interest Standard

While we are not opposed in principle to the application of a regulatory best interest standard in appropriate circumstances, we share the concerns of the *Jurisdictions with Concerns about a Best Interest Standard* (as identified in the Consultation Paper). As proposed in the Consultation Paper, the regulatory best interest standard raises the following significant issues:

- It does not appropriately reflect the scope of registration categories under securities laws;
- It is not clearly defined so as to avoid excessive uncertainty on the part of regulators, the Courts, and registrants, which could in turn result in higher costs and increasingly restrictive practices being adopted by registrants, which may negatively impact clients' access to affordable investment advice; and
- It has the potential to disrupt the common law application of "fiduciary duty" possibly diluting otherwise available legal remedies.

In our view, for a regulatory best interest standard to be successfully implemented, it ought to be done by way of a harmonized approach, uniformly applied in all jurisdictions; the lack of universal support within the CSA for this proposal increases our concerns about this proposition.

We appreciate the opportunity to provide comments on this important initiative and welcome the opportunity to discuss the foregoing with you in further detail. If you have any questions or require further information, please do not hesitate to contact the undersigned.

Sincerely,

"Doug Guzman"	*"Jennifer Tory"*
Doug Guzman Group Head, Wealth Management & Insurance	Jennifer Tory Group Head, Personal and Commercial Banking

[15] Question 35

cc. David Agnew, Chief Executive Officer, RBC Dominion Securities Inc.
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