The Bank of Nova Scotia
Wealth Management
40 King St. W., 13th floor
Toronto, Ontario
Canada M5H 1H1

BY EMAIL: comments@osc.gov.on.ca; consultation-en-cours@lautorite.qc.ca

September 30, 2016

Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Financial and Consumer Services Commission (New Brunswick)
Financial and Consumers Affairs Authority of Saskatchewan
Manitoba Securities Commission
Nova Scotia Securities Commission
Ontario Securities Commission

Attention:

Robert Blair
Acting Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor
Toronto, Ontario M5H 3S8

Me Anne-Marie Beaudoin
Corporate Secretary
Autorité des marchés financiers
800, square Victoria, 22e étage
C.P. 246, tour de la Bourse
Montréal (Québec) H4Z 1G3

Dear Sirs/Mesdames:

CSA Consultation Paper 33-404 – Proposals to Enhance the Obligations of Advisers, Dealers, and Representatives toward their Clients

We are writing to provide you with comments on behalf of *Scotia Capital Inc.*[1], *Scotia Securities Inc.*[2] *and HollisWealth Advisory Services Inc.*[3] (collectively, "Scotia" or "we") with respect to the Canadian Securities Administrators ("CSA") Consultation Paper 33-404 – *Proposals to Enhance the Obligations of Advisers, Dealers, and Representatives Toward their Clients* published on April 28, 2016 (the "Consultation Paper"). The Consultation Paper puts forward a regulatory best interest standard and a set of regulatory amendments to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (the "Targeted Reforms") to "better align the interests of registrants with

[1] Scotia Capital Inc. is an investment dealer and a member of the Investment Industry Regulatory Organization of Canada. Its divisions include HollisWealth, ScotiaMcLeod, and Scotia iTRADE.
[2] Scotia Securities Inc. is a mutual fund dealer and a member of the Mutual Fund Dealers Association of Canada.
[3] HollisWealth Advisory Services Inc. is a mutual fund dealer and a member of the Mutual Fund Dealers Association of Canada.

the interests of their clients, to improve outcomes for clients, and to clarify the nature of the client-registrant relationship for clients."

We fully support the CSA's stated objectives to enhance standards of conduct in the industry, to better align investor expectations and the products and services that are being provided by their investment professional. The industry is being transformed by technology and innovation, and the changing economic and business environment have presented new challenges for all of us – regulators, investors and the industry. Our industry is built upon trust and, at its core, is the relationship between the advisor and the client. We and the regulators have the same goals – we want our clients to achieve their financial goals. At Scotia, we believe that our clients have a right to be better off. We, therefore, support high standards of conduct and a regulatory regime that promote investor protections while maintaining fair, efficient and competitive capital markets.

We support principle-based regulation and acknowledge that prescriptive and overly narrow rule-making does not accommodate different business models and individual client situations. We urge the CSA to enact reforms that will address investor expectations and provide the industry with a clear roadmap to compliance, through the adoption of objective, measurable standards and the provision of clear guidance to complement principle-based regulation. In order for rule-making to achieve stated objectives and outcomes, resulting in meaningful investor protections, rules and concomitant guidance must provide the industry with consistency, clarity and certainty.

We acknowledge that securities legislation, which categorizes registrants into "advisors" and "dealers" and SRO Rules governing "dealers", would benefit from "modernization". Over the decades in which the investment industry has evolved, the line between trading and advising has blurred to the extent that personal investment advice is foundational to the dealer service offering. Clients rely on this advice. The advisor-client relationship is built on trust and clients already expect that this advice will be made in their "best interest". However, "best interest" can be understood quite differently depending on what assumptions are made that constitute "best interest". What the regulators and dealers believe is in the "best interest" may be different than what the client thinks is in his/her best interest, which is inevitably a subjective measure for each client.

Our advisors are not merely "salespersons" when they provide advice and recommendations. We acknowledge that a regulatory regime that regulates dealers as "salespersons" does not offer adequate investor protection when dealers are acting as advisors. The key to the reforms should, therefore, be on how dealers should be regulated when they act as advisors. We commend regulatory efforts in the Client Relationship Model (CRM) and Point of Sale reforms which have been adopted to address this gap. We urge the CSA, in considering further reforms in this area, to focus on when and how advice/recommendations are provided that best ensures an outcome that strengthens investor protection, preserves investor choice and that is capable of implementation in a practical and timely way by the industry.

TARGETED REFORMS

Proficiency & Titles

Investors are relying on their investment advisors and the advice that they are receiving to make the most important financial decisions of their lives. We support high standards of proficiency and professionalism

in the industry and robust proficiency requirements that will allow advisors to better serve their clients. To this end, these requirements should at the very least be tailored to the registrant's registration category.

We acknowledge that how advisors hold themselves out and market their services is an element (although not determinative) of the building of the trust relationship. We, therefore, support greater consistency in titling and reducing the number of titles in use to better assist investors in understanding who they are dealing with. To this end, consistency by the dealer community is important. Titles should, however, be meaningful to investors and allow them to distinguish among representatives based on criteria that are significant to them. The current registration categories were not meant to be meaningful to investors and this was not the objective of registration reform. We look forward to working with the CSA and the SROs to further discussions on proficiency and titling.

Client Interactions

In order for the proposed regulatory reforms to have the highest likelihood to achieve the objective of aligning investor expectation with industry practices, the advisor and the firm must know with clarity and certainty what they must do differently in order to meet this enhanced standard. The standard must also be communicated to the client in a clear and meaningful way and supported by advisor conduct that is consistent with this standard.

Conflicts of Interest

Conflicts to be disclosed and controlled in a manner that prioritizes the interests of the client ahead of the interests of the firm and representatives or to be avoided

To effectively address concerns regarding conflicts of interest, the CSA should provide specific guidance on the types of conflicts that are so great that they must be avoided and cannot be addressed through disclosure. These scenarios would be in addition to where current rules and/or guidance already ban or limit where conflicts are too great to manage (i.e. personal financial dealings with clients). Prohibitions would not be appropriate in circumstances where the conflict could be managed through other means. We also ask the CSA to provide examples of measures that may be taken to control conflicts "in a manner that prioritizes the interest of the client". It is also important for the CSA to acknowledge that certain activities will continue to be permitted, including research, market making, principal trading and underwriting and corporate finance activities.

Disclosure of all outside business activities of the firm and applicable representatives

We support the disclosure of information that is relevant to clients and will assist clients in understanding the conflicts that may arise in the course of the relationship. We question the purpose of this particular requirement, as many representatives have outside business activities that have no bearing on the client relationship. Clients may be confused about the relevance of this information and it may further exacerbate the concerns identified by the CSA regarding disclosure. The CSA should consider narrowing this requirement to outside business activities that relate to the client-registrant relationship.

Reasonable basis for concluding that client fully understands

We support disclosure that is clear and meaningful, allowing clients to "fully understand" the information provided. However, the conclusion that a client does indeed "fully" understand is the result of a

subjective assessment that can be challenging to articulate. Guidance is required to clarify how firms and representatives could evidence having met this requirement. Firms and representatives should be able to obtain and rely on a signed acknowledgment from clients.

Know Your Client

Information about client's financial circumstances

We support initiatives to better know clients, to clarify regulatory expectations regarding KYC and to further define terms used in the industry. We are concerned, however, by proposed requirements that are not demonstrably tied to advising or trading in securities and that will contribute to the investor expectation gap. Investors, when faced with questions regarding their assets and debts and their tax position, may misunderstand the nature of the services to be provided and assume they are receiving a form of financial planning. Furthermore, this information being highly sensitive, investors may refuse to provide it, particularly if the information is not clearly relevant to the particular service they are seeking. We urge the CSA not to adopt a one size fits all regime. The KYC should be tailored to meet the client's specific needs. The type of service offering may range from a transaction-based, one-off security trading model to a full advisory model where there is periodic or ongoing advice coupled with complex financial planning. Regulatory reforms should accommodate the different business models and fee structures so long as the type of account is clear and consistent with contractual terms.

KYC update at least every 12 months

We agree with the policy objective underlying this requirement that there should be greater clarity when advisors are expected to reach out and interact with clients in a meaningful way after account opening. Is advice ongoing, episodic or one-time? It should be clear to clients what to expect. This is an area of reform that reflects the evolution of the relationship from dealing to advising. We agree that firms or advisors should make reasonable attempts to contact their client in order to refresh the client's KYC information during the lifecycle of the relationship. This attempt would be a positive act to reach out to the clients in the manner that has been authorized and is consistent with client communication (i.e. electronic means). While there has been regulatory guidance from time to time, there is no current requirement imposed by law to update KYC on a specific schedule other than the limited circumstances to review the account/portfolio under CRM. Typically, the account agreement places the obligation on the client to contact the firm if there are material changes or events in their lives that could impact their KYC. Where a firm is required under MFDA Rules to annually request in writing to clients whether there have been material changes, dealers have typically included this request in the disclosure at the end of client statements which may not be prominent to clients.

We agree that greater consistency in updating KYC will lead to better outcomes for investors as well as being a good business practice. However, we believe that a one size fits all approach with a requirement to contact the client at least every 12 months is not appropriate for all client relationships, particularly in light of the operational significance of this undertaking. Firms should be required to establish criteria that would impose KYC updating from 1 to 3 years that take into account a number of risk-based criteria within the context of the service offering. We propose that the KYC form should set out clearly and prominently that in the absence of contact by the client, the KYC will be updated by the advisor every 1, 2 or 3 years or such more frequent period as may be indicated and agreed to by the client. CRM already requires that a copy of the KYC be provided to clients and positively acknowledged and this should

include any updated KYC. This practice will better clarify to clients when they should expect to be contacted by advisors and when advice/recommendation will be rendered.

Know Your Product

Representatives must understand and consider the structure, product strategy, features, costs and risks of each security on the firm's product list

The firm currently has obligations to conduct product due diligence and ensure that products on the firm's list are suitable for retail investors. We do not believe that it is practical or necessary for advisors to be familiar with all products on their firms' shelves, given the size of most, if not all, firms' shelves. In order to provide clients with access to a wide range of securities, a large firm could have over 110,000 security codes, including 1500 mutual funds. Advisors must certainly know the product that they are recommending to clients and the features of those products as set out in the proposal. It is important that regulatory reform continues to recognize that the advisor is an investment professional and he/she should be able to undertake an investment strategy in select securities upon which his/her advice is predicated. If the proposed requirement is imposed, firms would have no choice but to limit the list, decreasing client's access to a wide range of financial products and services, with the unintended consequences of impacting competition, capital formation and market efficiency.

Shelf of products "most likely to meet the investment need and objectives of its clients"

This "most likely" standard will increase regulatory uncertainty for firms, as it is not objectively measurable. The merit of a security is a complex investment management determination. Even very highly-skilled experts and experienced portfolio managers can and often have different views in the consistently changing landscape of financial products and services. Market forces will determine which financial products and services appeal to investor sentiment and needs. It is not possible to design a policy and procedure framework and a product line-up that will provide reasonable assurance on an ongoing basis that this standard is being complied with. It will not be practical for firms to meet this obligation without limiting their product shelves and/or categorizing clients for eligibility in certain products or services. There will be a menu of choices and the firm's decision will replace that of the individual advisor. Firms may choose, as a result, to reduce their offerings of riskier or more unusual products, despite investor demand or their suitability for certain investors. These are not positive outcomes for investors and the Canadian capital markets generally.

Suitability

Basic financial suitability

Requiring representatives to consider "basic strategies beyond transacting in securities", including whether paying down debt, directing funds into a savings account or purchasing insurance or banking products is preferable, goes well beyond the parameters of the current regulatory framework. Representatives would be providing a service akin to financial planning which is currently not contemplated by the different registration categories and their associated proficiency requirements. This significant shift in the role of representatives should not be mandated without a clear understanding of investor expectations. In light of the wide array of existing business models, we struggle with the notion that all investors should expect to receive financial planning type services and advisors obligated to

provide them. Different service offerings come with different costs. Accounts are large and small and some clients are just starting their investment savings. We support transparency and informed clients. It should be clear to clients what they are paying for, what products and services are being delivered and reporting for the client to assess whether the firm and the advisor have met their obligations. We should ask questions that are reasonably required to know our clients and to service their account type. Regulatory reforms should be flexible enough to be applied differently in client circumstances and to different business models.

Investment strategy suitability: target rate of return

We are also concerned by the proposal to have representatives calculate a target rate of return, as it will likely exacerbate the expectations gap that the CSA is trying to address. Clients may misunderstand the target rate of return's role as a suitability tool, believing instead that it is a guaranteed rate of return. Furthermore, the calculation of the target rate of return itself will create significant challenges for representatives, both in terms of obtaining the necessary information and having the skills for such a calculation.

Product selection suitability: "most likely to meet the client's investment needs and objectives"

We have laid out our general concerns with respect to this standard in our discussion of the Know-Your-Product proposal. At the representative level, the uncertainty around this standard may lead representatives to choose clients whose investment needs and objectives are easily and clearly identifiable. In order for the firm and the advisor to have reasonable assurance that this obligation is met, firms will have a menu of choices upon which advisors may make a recommendation to a specific category of client, thereby limiting investor access to advice and to choice of financial products and services.

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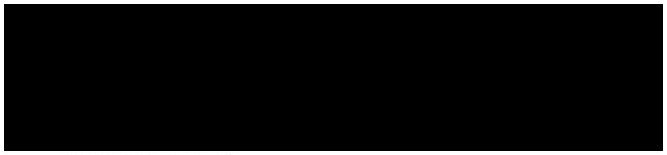
In conclusion, we support regulatory reforms to enhance the advisor and client relationship. Innovation and adaptability have been the hallmarks of the investment industry and core to the evolution of the Canadian capital markets. Regulatory reforms should preserve the characteristics that have allowed different business models to flourish, ensuring the availability of a wide range of financial products and services for investors to choose from. Research has highlighted that investment advisors provide significant value to clients and regulatory reforms should have as one of its goals maintaining client access to financial advice.

We support regulatory reforms that provide consistency, clarity and certainty – this is vital in order for us to make business decisions on how to implement these new standards given our advisor teams, technology, operations, service offerings and business models and to maintain a robust supervisory and compliance framework that provides us with reasonable assurance that we have discharged our regulatory obligations.

We urge the CSA to adopt rule-making with clear principles, supplemented with specific rules, and clarified through guidance, which will have the highest likelihood of achieving positive investor outcomes and stated policy objectives. We and the regulators are very much aligned in this regard. Looking after our clients is our top priority.

We appreciate this opportunity to provide comments on these proposed regulatory reforms that may inform the CSA's work in this important area. We look forward to continuing to work with CSA to achieve these important goals.

Yours truly,



Glen Gowland

Senior Vice President & Head, Canadian Wealth Management