PMAC
PORTFOLIO MANAGEMENT ASSOCIATION OF CANADA
Advancing Standards™

VIA E-MAIL October 23, 2020

British Columbia Securities Commission
Alberta Securities Commission
Saskatchewan Financial Services Commission
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission of New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Superintendent of Securities, Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
Superintendent of Securities, Nunavut

Me Phillippe Lebel
Corporate Secretary and Executive Director,
Legal Affairs
Autorité des marchés financiers
Place de la Cité, tour Cominar
2640, boulevard Laurier, bureau 400
Québec, (Québec) G1V 5C1
Fax: 514-864-6381
consultation-en-cours@lautorite.qc.ca

The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor
Toronto, Ontario M5H 3S8
Fax: 416-593-2318
comments@osc.gov.on.ca

Re: CSA Consultation Paper 25-402 *Consultation on the Self-Regulatory Organization Framework*

Background

The Portfolio Management Association of Canada (**PMAC**) is pleased to have the opportunity to provide written feedback to the Canadian Securities Administrators (**CSA**) on CSA Consultation Paper 25-402 *Consultation on the Self-Regulatory Organization Framework* (the **Consultation**). PMAC represents over 285

investment management firms registered to do business with the various members of the CSA as portfolio managers (**PM**s). Approximately 65% of our members are also registered as investment fund managers (**IFM**s). PMAC's membership is comprised of firms of varying sizes and models, ranging from one-person firms to international and bank-owned firms. In total, our members manage assets in excess of $2.9 trillion for institutional and private client portfolios. Our members also range from the more traditional models to online advisers.

Portfolio Managers

PMAC's mission statement is "advancing standards". We are consistently supportive of measures that elevate standards in the industry, enhance transparency, improve investor protection and benefit our capital markets as a whole. We are also cognizant of the global market in which many of our mid-size and large members operate and are sensitive to any regulatory changes being misaligned with other international capital market jurisdictions.

This Consultation has generated discussion and debate among numerous stakeholders, which we view as a positive development. Some recent proposals, notably from the Capital Markets Modernization Taskforce (**CMMT**) and Mutual Fund Dealers Association (**MFDA**) contemplate the creation of a single self-regulatory organization (**SRO**) that covers all advisory firms, including PMs, exempt market dealers (**EMD**s) and scholarship plan dealers (**SPDs**). As we noted in our response to the CMMT, we believe that PMs, IFMs and EMDs should remain under the oversight of the CSA.

Throughout our submission, we will draw attention to the ways in which PM firms are unique from other registrant categories and we urge the CSA to take these unique features into account in considering reforms to the SRO framework. We believe that a failure to acknowledge the differences in registration categories, advice model and duty to investors could result in inappropriately prescriptive regulation that impedes a PM's professional judgement, hampers competition and innovation and, over the long term, does not benefit investors.

In addition, throughout our submission we will highlight the fact that the majority of PMs are also registered as IFMs; these two categories are intertwined and should remain under the same umbrella of regulation. They also often operate internationally, and are predominantly regulated under principles-based, direct government regulation in other jurisdictions. Any shift by Canada to a prescriptive, self-regulatory model fraught with burdensome rules-based regulation would put Canadian PM registrants at a significant competitive disadvantage globally.

PMAC members believe that direct regulation of PMs by the CSA is and historically has proven to be extremely effective and we fail to see how changing direction would better serve investors. CSA staff have developed a deep understanding and institutional knowledge with respect to the PM firms they oversee; the principles-

based approach to PM regulation is appropriate and effective and aligned with international regulation, and provides the flexibility required to respond to and promote the wide variety of business models and types of investors served by PM firms. Furthermore, we believe that direct regulation of PM firms by the CSA better serves the investing public, in contrast to delegation of regulation to an SRO.

KEY RECOMMENDATIONS

We note that the Consultation questions are heavily focused on products and distribution-based regulation. We have framed our responses to focus on what we view as significant public interest and investor protection matters. We provided the following key recommendations with respect to the future of SRO regulation in response to the CMMT Report and believe these are equally relevant to the CSA's Consultation. We will address each of these in greater detail below.

1. **Maintain regulation of PMs under the CSA:** We defer to others in the industry to opine on whether a merger of the two current SROs makes sense. PMAC strongly opposes PMs being regulated by a single or merged SRO; we believe the current regulation of PMs by the CSA is effective and that it is in the public interest to maintain direct regulation of these registrants versus delegating to an SRO.

2. **Address governance weaknesses inherent within SRO structures:** Improving governance and oversight of the SROs by the CSA will inspire confidence in the regulatory framework and Canadian capital markets.

3. **Prioritize the national/cooperative regulator with PMs and IFMs directly regulated by this entity:** Establishing the Cooperative Capital Markets Regulatory System (**Cooperative System**) is essential to harmonizing regulation across Canada, strengthening the global competitiveness of our markets, fostering a strong national economy and managing systemic risk.

General Consultation Questions

We have considered the questions in the Consultation and have used these to structure our comments. Please note that we have only referenced those questions on which our members provided specific feedback.

B. Are there other issues with the current regulatory framework that are important for consideration that have not been identified? If so, please describe the nature and scope of those issues, including supporting information if possible.

There are two issues which we believe are of paramount importance in considering the future of SROs in Canada that have not been specifically identified in the Consultation. The first is to continue to prioritize the Cooperative System and the second, to keep the regulation of PMs with the CSA. These will be discussed in turn below.

Prioritize the Cooperative Capital Markets Regulatory System

We commend the steps taken by the CSA in recent years to prioritize nationally harmonized securities regulation and believe that further progress toward this goal will have a variety of beneficial impacts on investors, registrants and the capital markets.

We believe that a national regulator such as the Cooperative System should be prioritized. PMAC has been a strong supporter of, and vocal advocate for, a national securities regulator since the association's inception in 1952. In recent letters to the Ontario and British Columbia Ministers of Finance, PMAC reiterated our support for the creation of the Cooperative System.

We believe that a national regulator is a better first step towards improving the regulatory system; for the reasons set out below, this is preferred over the creation of a new all-encompassing SRO. In our view, direct regulation is stronger regulation and better serves the public interest. Establishing the Cooperative System would be the most effective path to improving the regulatory framework. The Cooperative System would increase harmonization and enhance investor protection, and would reduce regulatory burden for the benefit of both investors and market participants.

Canada is the only developed country in the world without a national securities regulator, which puts Canada at a significant disadvantage in the global capital markets, due to the inefficiencies of the current model. Nine participating governments have signed on to the national regulator initiative and we are as close as we ever have been to the goal, but we need the provinces to make it a priority.

The Cooperative System would be capable of developing and implementing harmonized law and policy more quickly and efficiently than the current fragmented system. This is highlighted by the recent experience during the COVID-19 crisis, where blanket orders were required to be issued in multiple CSA jurisdictions to provide urgently needed relief to registrants. Harmonized rules across the country are in the best interests of issuers, registrants, and investors. Investor protection would increase with the benefit of a better framework to manage systemic risks and improve coordination with enforcement on a national and global scale.

Systemic risk considerations are a critical aspect of the health of our economy and the well-being of investors. We believe that systemic risk must be monitored and managed through seamless cooperation between the provinces and territories and that, to ultimately be nimble and effective, it must be overseen at the Federal level.

Regulation of Portfolio Managers should not be delegated to an SRO

Some voices in the current debate over the future of SROs in Canada, including the CMMT and the MFDA, have recommended a merger of the two existing SROs. We leave it to other industry participants to determine whether such a merger makes sense. Although the Consultation does not directly pose the question, the CMMT report suggested that, as part of Phase II of the SRO merger, PM regulation would be brought under the new SRO; the MFDA also supports having all registrants regulated by a single SRO. PMAC is strongly opposed to delegating the regulation of PMs from the CSA to an SRO.

Quite simply, regulation of PMs and IFMs by the CSA is working. CSA staff have the long-term experience in overseeing PMs and the specialized expertise to understand the unique features of the PM business and the fiduciary duty of care owed by PMs to their clients. The CSA's principles-based regulation is effective and appropriate for the variety of business models employed by PMs, whether they be investment counsellors, robo-advisers, family offices, global asset managers or large PM/IFMs. No market or investor protection reasons have been raised in support of delegating this effective regulation to an outside body, and we question the efficiency of doing so.

The SROs' regulatory structures were developed to work well with the investment dealer model, where firms are focused on distribution, and client relationships are based primarily on specific securities transactions. The prescriptive nature of SRO regulation is inappropriate for, and incompatible with, the business models and client types served by PM firms. This is recognized in the U.S., where a proposal for the SRO responsible for broker-dealers (the U.S. equivalent of securities dealers), the Financial Industry Regulatory Authority (FINRA) to take over oversight of investment advisers (the U.S. equivalent of PMs) was rejected, and oversight remains with the Securities Exchange Commission (**SEC**). Implementing a one-size-fits-all framework is complicated and will not improve investor protection at any level.

In our view, expanding the mandate of the SROs to include PMs would only serve the interests of the SRO, and not investors. Direct regulation is strong regulation – it minimizes conflicts of interest, and there are issues with investor outcomes that need to be solved before any consideration of mandate changes for the SROs. Mergers are not a magic bullet. Although a merger of the SROs may provide cost savings to affiliated dealers and with respect to the regulatory oversight of dealers, due to the economies of scale of a single SRO, it is not clear that costs savings would result if PMs and EMDs were included. We believe the CSA should consider what changes to the regulatory framework as a whole are necessary to ensure a sustainable system in the long term, and that assessment must take into account investor protection, systemic risk, market changes, technology, and future global trends.

Over time, CSA regulation has come more in line with international regulation, which is critical for maintaining Canada's competitiveness. As noted in the Consultation, many PM firms are also registered as IFMs and/or EMDs, all of which are directly overseen by the CSA. About 65% of PMAC membership is registered as both PMs and IFMs, and many are part of international firms. Reform proposals have been silent on the oversight of IFMs. PMs and IFMs are intertwined; dividing their regulation between a new SRO and the CSA would increase costs and regulatory burden, which is not in the best interests of investors and runs counter to the overall objective of any of the proposals.

Although some commentators point to the fact that there are IIROC firms in the business of discretionary management ("managed accounts"), in 2020, these amounted to only 15 out of 173 IIROC firms.[1] This is compared to approximately 850 PM firms registered with the CSA.[2] As set out in the Consultation, there are currently a total of 257 firms registered with the MFDA and IIROC, compared to over 1000 CSA-registered firms.[3] It is not clear how an SRO could more than triple in size (if PM, EMD and SPD regulation were moved to the SRO) and yet provide effective oversight of registered firms. However, the more important question is *why*?

We question the policy rationale for having an SRO oversee PM firms. In addition to needed reforms to the current SRO structure (as set out below in our comments on Question 6), it will be in investors' best interests for the regulation of PMs to remain with the CSA and, eventually, with a national regulator. We do not view the existing SRO regime as having been more effective in terms of investor protection compared with direct regulation by the CSA, and we are concerned that regulation of all registrants through a "Super" SRO risks lowering standards across the industry rather than elevating them. For example, while PMs represent 59% of Ombudsman for Banking Services and Investments (OBSI) members, complaints against them were only 3% of the total complaints regarding investments in 2019.[4] Currently, PMs are subject to the highest proficiency standards in the industry and subject to a fiduciary duty. We are concerned that a single SRO responsible for all registrants will result in a "one-size-fits-all" model of regulation, with the potential for proficiencies to be lowered over time if PM firms were to be included. We do not believe this to be in the best interests of investors. Regardless of which regulator oversees them, individuals managing client money on a discretionary basis should continue to evidence the highest levels of professionalism and educational experience to carry out the responsibilities that clients entrust them with.

---

[1] See IIROC Dealer Members by Peer Group, September 2020, "managed accounts" category: https://www.iiroc.ca/industry/Documents/PeerGroupList_en.pdf

[2] Note this number includes IFMs registered as PMs. See Consultation at Appendix C

[3] *Ibid* at Appendix C

[4] OBSI Annual Report 2019, available at https://www.obsi.ca/Modules/News/Search.aspx?feedId=c84b06b3-6ed7-4cb8-889e-49501832e911&lang=en

There are a large variety of business models that are directly regulated by the CSA and a significant portion involve managing assets for pensions, foundations and other institutional clients. This is in contrast to SRO-regulated businesses being primarily focused on distribution and directed at retail clients. To continue to effectively serve investors and meet their evolving needs, regulation of PMs needs to be flexible and must accommodate a variety of business models. Having all of these entities regulated by a single SRO would add complexity and costs.

We encourage the CSA to carefully consider the business models employed and clients served by firms in different registration categories to determine which regulatory model will best promote the public interest and investor protection goals (including investor choice), as well as regulatory efficiency, harmonization and burden reduction. For PM firms, we strongly believe that the SRO model would be inappropriate.

C. Are any of the CSA targeted outcomes listed more important from your perspective than other outcomes? Please explain.

In addition to our comments above, we are of the view that issues of regulatory arbitrage (discussed under Question 3 below), investor confusion (discussed under Question 4 below) and public confidence (discussed under Question 6 below) are of paramount importance. Based on extensive public comment in response to this Consultation, the CMMT Report and papers by IIROC[5] and MFDA[6], it is clear that the current system is in need of improvement. There has been a significant rise in investment fraud during the COVID-19 pandemic.[7] The economic consequences of the pandemic will make firms, individual registrants and investors alike more vulnerable.[8] Increased use of technology has the potential to make investors more susceptible to abuse.[9] The same is true with respect to Canada's aging population.[10] Such risks may undermine confidence in the capital markets. Canadians are increasingly suspicious of public institutions.[11] Strong regulation with a public interest and investor protection mandate will be imperative if regulators and registrants are to continue to function for the benefit of Canadian investors.

---

[5] IIROC, *Improving Self-Regulation for Canadians* (**IIROC Paper**), June 2020, available at https://www.iiroc.ca/Documents/2020/IIROC_consolidation_FNL.pdf

[6] MFDA, *A Proposal for a Modern SRO* (**MFDA Paper**), February 2020, available at https://mfda.ca/wp-content/uploads/MFDA_SpecialReport.pdf

[7] See CSA, Canadian Securities Regulators Provide Update to Investors in Response to COVID-19, Press Release dated May 21, 2020; CSA, Investor Education in Canada 2020, at p. 8

[8] See Bank of Canada, Remarks by Governor Tim Macklem, Economic Progress Report: a very uneven recovery, September 10 2020

[9] See CSA, Investment fraud on the Internet

[10] See CSA, Investor Education in Canada 2020, *ibid* at p. 9

[11] See Edelman Trust Barometer 2020, Global Report, which measures trust in government, business, NGOs and media; CTV News, *Only 53 per cent of Canadians trust core institutions, report says*, January 20, 2020. Note that since the pandemic, there has been an increase in levels of trust in public institutions, but such gains are generally lost a year later: see Edelman Trust Barometer 2020, Spring Update, Trust and the Covid-19 Pandemic at p. 7

D. With respect to Appendix F, are there other documents or quantitative information / data that the CSA should consider in evaluating the issues in light of the targeted outcomes noted in this Consultation Paper? If so, please refer to such documents.

We refer you to the OBSI 2019 Annual Report referred to above, and previous OBSI Annual Reports for statistics with respect to complaints against PMs, which have averaged only 4% of total investment firm complaints in the last four years.

Specific Questions

Consultation Questions on Duplicative Operating Costs for Dual Platform Dealers

> Question 1.1: What is your view on the issue of duplicative operating costs, and the stakeholder comments described above? Are there other concerns in respect of this issue that have not been identified? If possible, please provide specific reasons for your position and provide supporting information, including the identification of data sources to quantify the impact or evidence your position.

In addition to a merger of the existing SROs, the MFDA Paper included a recommendation that PMs be brought under the same self-regulatory umbrella with investment dealers and mutual fund dealers. We strongly oppose this suggestion.

Although a small percentage of PMs have affiliated or related dealers overseen by IIROC, a significant number of PMs are also registered as IFMs and EMDs, all directly regulated by the CSA. Moving these multi-registered PMs to SRO regulation would create a duplicative regime, resulting in added regulatory burden, operational complexities and additional costs. For example, a PM/IFM would be subject to regulation by an SRO as well as the CSA.

As noted above, less than 10% of IIROC dealers operate as a managed account business. IIROC dealers may have individuals registered as Portfolio Managers in order to advise managed accounts at the dealer. The firm continues to operate as a dealer; in addition to advising managed accounts, the same registered individuals may conduct trades for clients on a commission basis. The account opening documents and KYC processes are subject to the prescriptive rules of the SRO. This is in contrast to PM firms, which act as a discretionary manager of client portfolios, with a fiduciary (portfolio-based) focus. These firms are subject to more principles-based rules; the investment mandate may be set out in an investment policy statement and investment management agreement which are customized to the client; the fiduciary duty permeates the entire firm culture, guiding every decision affecting a client, because the entire firm bears responsibility for decisions made on behalf of the client. This fiduciary duty is of utmost importance to investors.

Moreover, our members note that PMs could not function if they were required to adhere to prescriptive rules – this simply would not work for their business. For example, many PMs operate internationally under a CSA-type principles-based regime; any move to a more prescriptive SRO-governed model would not be aligned with these international regimes, and would likely lead to significant loss in the international competitiveness of these Canadian firms. Another example arises in the context of the recent amendments to National Instrument 31-103, the Client Focused Reforms (**CFRs**). PMAC referenced in our submissions on the CFR consultations specific examples where a prescriptive approach would be incompatible with certain PM models, such as the prescriptive KYC requirements. While these requirements are clearly beneficial with respect to retail investors, they are unworkable for conducting KYC with a global pension plan that has hired a PM firm for a specific asset class mandate. A carve-out for non-individual permitted clients was included in the final CFR publication. This is simply one example of many that could be provided of prescriptive rules designed to protect retail investors that add compliance costs without corresponding investor protection value for pension, foundation and other institutional clients. Maintaining the principles-based CSA regulation for PM firms is the best outcome.

Similar distinctions can be made between PMs with EMD registration (usually for the purpose of managing and offering proprietary funds to clients of the PM) and a firm registered solely as an EMD, for the purpose of selling exempt product to clients. Again, the presence of a fiduciary culture within the PM firm is an essential aspect of the business and the firm's relationship to its clients. We believe that it is important to carefully delineate the various business models, client types and offerings that various registration categories – and combinations of registration categories – bring to the Canadian markets and investors.

The Consultation refers to the availability of investor protection to IIROC and MFDA clients through CIPF/IPC. It is important to note that, since PMs don't have custody of the client assets, CIPF protections are available via their IIROC-regulated custodians and OSFI-regulated entities used by PMs. PMs (other than those principally registered in Quebec) are also obligated to make OBSI's complaints and dispute resolution services available to their non-permitted clients.

<u>Consultation Questions on Product-Based Regulation</u>

> Question 2.1: What is your view on the issue of product-based regulation, and the stakeholder comments described above? Are there other concerns in respect of this issue that have not been identified? If possible, please provide specific reasons for your position and provide supporting information, including the identification of data sources to quantify the impact or evidence your position.

d) How has the current regulatory framework, including registration categories contributed to opportunities for regulatory arbitrage?

To best serve the public interest, it is key that proficiency and regulatory standards remain high, regardless of the product, and regardless of the consumer demographic. There should be as much harmonization as possible in terms of product and distribution standards across various types of registered firms. All investors are entitled to expect their investment service provider to have appropriate proficiency and to act with integrity. We believe that discretionary advising should be limited to individuals with the highest proficiency, and must be subject to a fiduciary duty. However, investor protection is about more than establishing registration categories and required proficiency – it is about effectively overseeing compliance and addressing registrant misconduct.

According to IOSCO, "Regulators should seek to remove opportunities for regulatory arbitrage by looking for ways to reform their laws and powers, raise their own standards and foster better and deeper ways of collaborating."[12] To address regulatory arbitrage, it is imperative that regulatory standards be applied uniformly across the CSA and the SRO(s), both with respect to firms and individual registrants. Standards should be harmonized to the highest possible standard. A recent example of this is the CFRs, where requirements are being harmonized among the CSA and SROs, without regard to the distribution channel.

Regulators should have access to similar tools and these should be employed in a similar manner by all regulators. The CSA should design its SRO oversight program to evaluate whether the tools are being employed uniformly. This includes whether compliance deficiencies, including significant and/or repeat deficiencies, are being appropriately dealt with at the firm level. IOSCO states:

> … an SRO without robust and committed regulatory infrastructure can undermine a regulator's efforts to promote credible deterrence. Regulators should consider having regular dialogue with SROs, and/or inspections of SROs, to ensure they fulfil their regulatory mandates and provide information, on a timely basis, about suspected misconduct. Regulators could also encourage SROs to strengthen their governance and the quality of their compliance and risk management arrangements in ways that would enhance deterrence…[13]

In its letter regarding the scope of the CSA's SRO review, FAIR Canada states, "IIROC and the MFDA rarely discipline investment firms or senior management in cases where investors suffer. They generally settle for a sanction against the salesperson even where it appears that the firm's policies or standards of supervision were in question. In such cases there is a lack of transparency in decisions, notices etc. on settlements about the potential culpability of the dealer member and its senior management, including whether issues such as the

[12] IOSCO Publication: *Credible Deterrence in the Enforcement of Securities Regulation* (**IOSCO publication**) available at https://www.iosco.org/library/pubdocs/pdf/IOSCOPD490.pdf, at page 14

[13] *Ibid* at page 19

adequacy of supervision of salespersons were considered, and what the related findings were."[14]

This is contrary to IOSCO's observation that "[s]ecurities laws and regulations that require regulated entities to monitor compliance within their own institutions can be an important force for deterrence. Regulated entities are likely to be well-placed to know where risks exist for their employees and/or clients to engage in misconduct. Laws and rules that require entities to construct and monitor controls systems can be strong deterrents to misconduct."[15]

In order to curb issues of regulatory arbitrage, we urge the CSA to carefully consider the public interest and investor outcomes in determining what changes may be required with respect to the regulatory tools available to SROs, their deployment of those tools and the CSA's oversight of SROs.

Consultation Questions on Regulatory Inefficiencies

> Question 3.1: What is your view on the issue of regulatory inefficiencies and the stakeholder comments described above? Are there other concerns in respect of this issue that have not been identified? If possible, please provide specific reasons for your position and provide supporting information, including the identification of data sources to quantify the impact or evidence your position.

a) Describe which comparable rules, policies or requirements are interpreted differently between IIROC, the MFDA and/or CSA; and the resulting impact on business operations.

Please see our comments under Question 2 and Question 5. We agree that clients should have choices in terms of the products available to them; however, we believe that the focus of the question should not be solely on the product being offered, but rather on the *quality of service* and duty of care to which clients are entitled in their interactions with registrants.

In the consultations that gave rise to the CFRs, PMAC called for a fiduciary standard of care across the industry. However, many industry participants rejected not only the fiduciary standard, but also the proposed regulatory best interest standard. As a result, we are concerned that without appropriate vigilance, standards may be pulled downward across the industry. All regulators must require the same high standards from registrants. As FAIR Canada noted, "the case needs to be made that SROs are able to carry out the regulatory responsibilities in question at least as

[14] FAIR Canada, *Submission to CSA on the Proposed Scope of the Review of Self-Regulatory Organizations*, March 27, 2020 (**FAIR letter**) available at https://faircanada.ca/submissions/submission-to-csa-on-the-proposed-scope-of-the-review-of-self-regulatory-organizations/, at para. 24

[15] IOSCO publication, at pages 19-20

effectively – if not more effectively – as the statutory regulators would be able to perform them."[16]

As noted in OSC Staff Notice 31-715 *Mystery Shopping for Investment Advice*, which looked at compliance with regulatory expectations for advisory practices among various registrant categories including registrants regulated by the CSA, IIROC and MFDA, "the results show a range of practices in use – best practices, compliant practices and non-compliant practices were all found…. Greater emphasis must be placed on improving the investor experience in the advice process through advisor practices that make it more accessible and understandable… Investors must be given better tools and support to seek out and receive good advice."[17]

Clients are entitled to information, resources and protection when things go wrong. The regulatory framework and recourse available to clients should not be overly complex. Products and services change rapidly, and the regulatory framework must have the flexibility to adapt to ensure consumer protection.

Consultation Questions on Structural Inflexibility

> Question 4.1: What is your view on the issue of structural inflexibility, and the stakeholder comments described above? Are there other concerns in respect of this issue that have not been identified? If possible, please provide specific reasons for your position and provide supporting information, including the identification of data sources to quantify the impact or evidence your position.

As noted above, new products, services and methods of delivery are continuously being introduced to the marketplace. The regulatory framework must be flexible to evaluate and regulate new products, services and delivery methods as they emerge. More importantly, industry participants must understand the products they offer and the implications of how they deliver their services. According to the Consultation document, stakeholders had the following feedback regarding Structural Inflexibility:

- "the current regulatory structure is creating succession planning challenges for mutual fund dealers and their representatives due to the limited product shelf they can offer to clients";
- "investment dealers are limited in their ability to grow their business by attracting mutual fund dealer representatives due to the additional proficiency requirements";
- "in respect of the IIROC proficiency upgrade rule requirement that requires an individual to be qualified within 270 days of approval as a

[16] FAIR letter, at para. 5

[17] OSC Staff Notice 31-715 *Mystery Shopping for Investment Advice,* Conclusions 3, 7 and 8, at pages 8-9 and pp. 32-33

representative on the IIROC platform, that: (i) the requirement is a burdensome barrier…"; and,

- "the current regulatory structure prohibits mutual fund dealers from trading for clients on a limited discretionary basis which has prevented mutual fund dealers from creating certain business models".

In our view, lowering proficiency standards to allow registrants to offer additional products is not the answer – the wider the variety of products offered by a registrant, the higher the proficiency standards should be. As stated above, it is our belief that anyone offering discretionary advice must have the highest level of proficiency and be subject to a fiduciary duty.

Access to advice in rural communities and for individuals with smaller accounts is a concern – technology may present opportunities to diminish this gap. Regulators must carefully monitor the use of such technology to ensure investor protection. If only a small number of registrants are operating in a community, regulators' compliance oversight programs should be adapted to supervise these registrants for the particular risks that may arise (such as supervision of outside business activities and other potential conflicts of interest).

Consultation Questions on Investor Confusion

> Question 5.1: What is your view on the issue of investor confusion, and the stakeholder comments described above? Are there other concerns in respect of this issue that have not been identified? If possible, please provide specific reasons for your position and provide supporting information, including the identification of data sources to quantify the impact or evidence your position.

The current regulatory framework is fragmented and complex. Many investors do not understand product availability and the duties owed to them. Investors have little understanding of the securities regulatory system. Although investor education is essential, the complexity of the system will continue to be an impediment to informing and empowering investors. We believe having a single national regulator would significantly improve the situation.

It would be desirable for investors to have more transparency with respect to the registrant they are dealing with. In the U.S., the Form ADV is used by the SEC to collect registration information for investment advisers. This form is published on the SEC's public website and provides this transparency to investors. In addition to information regarding the firm's business, ownership, clients, employees, business practices, affiliations, and any disciplinary events of the adviser or its employees, the form includes narrative sections written in plain English containing information such as the types of advisory services offered, disciplinary information, conflicts of interest, and the educational and business background of management and key advisory personnel. This brochure is the primary disclosure document provided to clients and is publicly available on the Internet, and must be updated annually for

clients.[18] Similar information should be available with respect to Canadian registrants, regardless of which entity regulates them or which products or services they offer.

There is also confusion around the use of titles in the financial services sector. As noted in OSC Staff Notice 31-715 *Mystery Shopping for Investment Advice*, 48 different titles were used by advisors on the four platforms investigated during the exercise.[19] The CFRs have introduced requirements around the use of misleading titles. Although some provinces have proposed legislation to regulate the use of certain titles, there is a lack of harmonization across Canada and it remains to be seen whether such regulation will be effective. In response to recent consultations on this issue, we urged the creation of a national registration regime and a database that can be used by investors to determine where and in what capacity their financial services provider is registered; to be effective, we believe that this database should include historical disciplinary information in plain language so that retail investors are able to understand the nature of the registrant's conduct / omission.

The improvement of systems such as SEDAR+ and making such information available in a user-friendly and accessible manner to the public would be an important step in diminishing investor confusion. We also support continued investor education initiatives and behavioural research studies, such as those undertaken recently by the OSC.

Consultation Questions on Public Confidence in the Regulatory Framework

> Question 6.1: What is your view on the issue of public confidence in the regulatory framework, and the stakeholder comments described above? Are there other concerns in respect of this issue that have not been identified? If possible, please provide specific reasons for your position and provide supporting information, including the identification of data sources to quantify the impact or evidence your position.

PMAC highlighted the following in our submission to the CMMT. We believe that this context is important for this Consultation as well. The SRO model has been slowly disappearing internationally with Canada and the U.S. being among the few to continue to utilize SROs. If they are going to continue to exist in Canada, the inherent flaws with the SRO model need to be addressed. Our comments are not intended to be a criticism of IIROC or the MFDA, but rather what we would consider to be best practices with respect to the governance of SROs generally and in the securities industry in particular.

Investor protection and the public interest must be the primary mandate and focus of regulators, including SROs. The SROs' governance and accountability

[18] See SEC website: https://www.sec.gov/fast-answers/answersformadvhtm.html

[19] OSC Staff Notice 31-715 *Mystery Shopping for Investment Advice*, September 17, 2015, Conclusion 2 at page 8

frameworks should be significantly enhanced to address inherent weaknesses to which SROs are vulnerable, such as lack of transparency and the potential for conflicts of interest.

As we noted in our response to the CMMT report, we supported the following CMMT proposals with respect to the SRO's governance:

- SRO directors should have investor protection experience
- the number of independent directors should be higher than the number of directors from member firms
- the SRO Chair would be required to be an independent director

There is a concern that industry directors may have considerable influence on SRO boards and are, *per se,* in a conflict of interest. They may perceive that they are on the SRO board to represent the industry, and their own firm in particular. They are provided with confidential information that may be used to their advantage. For this reason, we believe that industry directors should not represent more than one third of any SRO board, and that all directors should be appointed jointly by CSA members.

We disagree with the notion of a "cooling-off" period for independent directors. It would be preferable if anyone previously employed in the securities industry is excluded from consideration as an "independent" director.

There is a risk that independent directors' voices can be silenced if they are in the minority. For this reason, as well as having an independent director act as Chair, PMAC would support a requirement that industry directors be prohibited from acting as committee chairs. In addition to directors having investor protection experience, we believe that investors must be independently represented on the boards of SROs.

We believe the above measures would be further enhanced by moving towards the following best practices:

- the definition of the "public interest" should be determined by the CSA
- firm term limits (9 years is suggested) for directors, with no "grandfathering" of terms
- the ability for independent directors to meet *in camera* at every board meeting
- conflicts of interest and codes of conduct to be independently audited
- independent directors to be provided with mandatory annual industry and governance education
- industry directors to be provided with mandatory annual governance education

As discussed above, regulatory oversight of SROs by the CSA must also be enhanced to ensure uniform standards of regulation, to identify and address regulatory gaps, and prevent regulatory arbitrage. We agreed with the following proposals made by the CMMT with respect to SRO oversight, although we believe such oversight should be performed by the CSA and not exclusively by the OSC, as was suggested by the CMMT:

- give the CSA greater tools to oversee the SROs
- link the compensation and incentive structure applicable to SRO executives to the delivery of the public interest and policy mandate
- require SROs to submit an annual business plan covering all activities to the CSA for approval
- provide for a CSA veto on any significant publication, including guidance or rule interpretations
- provide for a CSA veto on key appointments, including the Chair and the President and CEO
- establish term limits for key appointments

We believe that SRO officers and directors must be held to at least the same ethical and conduct standards (including those related to conflicts of interest) applicable to CSA Members (Commissioners).

In addition to these governance changes, we recommend that SROs' committees' and district councils' governance be reviewed and reformed. IIROC District Councils are made up entirely of industry participants in the local jurisdiction, and have considerable influence over registration, exemptions and discipline matters. This gives rise to a significant risk of conflicts of interest compared to direct regulation by the provincial securities commissions. Reforms should ensure that regulatory and disciplinary outcomes are consistent across District Councils, SROs and the CSA. If there is a decision to continue with the use of district councils, their structure should be modified to ensure that their membership is balanced and includes independent members and investor representation. Within the organization, the regulatory function must be culturally engrained – in order to foster public confidence and in order to fulfill its public interest mandate, it must not be viewed (and must not view itself) as an industry body, but rather as a regulatory body with a public interest and investor protection mandate. It must maintain consistent regulatory standards across Canada to effectively implement and enforce securities regulation. Policy development must be transparent and

undertaken from a public interest lens and not subordinated to the industry's interests.[20]

Conclusion

We are pleased that the CSA is taking on this review of the SRO framework and are encouraged by the public discourse that the Consultation has generated. The Consultation is timely given the current market conditions resulting from the COVID-19 pandemic and the challenges these events present to the registrant community and the investing public. This period of profound change represents a significant opportunity to focus on measures that best serve investors and our capital markets.

We urge the CSA to seize this opportunity to consider the changes needed to improve investor protection and market efficiency by strengthening SRO governance and oversight.

We believe that PMs should continue to be directly regulated by the CSA, until such time as the Cooperative System can be implemented. We believe that the Cooperative System will be the best long-term solution for the harmonized regulation of Canadian capital markets, leading to stronger and more resilient provincial and national economies.

PMAC will continue to challenge any suggestion, by any entity, that regulation of PMs should be delegated to a self-regulatory body; we believe that direct government regulation is stronger regulation and is more appropriate for discretionary managed accounts guided by a fiduciary duty. Principles-based regulation is better suited to the variety of business models that exist in the PM space and is aligned with the global asset management industry. It is particularly critical in the institutional asset management sector, where prescriptive retail-oriented rules are nonsensical. A move towards more prescriptive rules-based regulation in the PM sector would add regulatory burden and have a significant negative impact on the competitiveness of the Canadian asset management industry.

[20] See CFA Institute, Self-Regulation in the Securities Markets – Transitions and New Possibilities, available at https://www.cfainstitute.org/-/media/documents/article/position-paper/self-regulation-in-securities-markets-transitions-new-possibilities.ashx?la=en&hash=2AE04650F1747DD0DD372F1C31EDC6F5C9E79613, at page 37

We would be pleased to discuss any of our comments with you at your convenience. Please do not hesitate to contact Katie Walmsley at (416) 504-7018 or Victoria Paris at (416) 504-7491.

Yours truly,

PORTFOLIO MANAGEMENT ASSOCIATION OF CANADA

Katie Walmsley
President

Margaret Gunawan
Director
Chair of Industry, Regulation & Tax Committee,

Managing Director – Head of Canada Legal & Compliance
BlackRock Asset Management Canada Limited