

By email
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Montréal, July 17, 2020

Me Philippe Lebel
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Me Lebel,

Re: CSA Notice and Request for Comment – Proposed Amendments to Enhance Protection of Older and Vulnerable Clients

On March 5, 2020, the Canadian Securities Administrators (CSA) issued a Notice and Request for Comments relating to Proposed Amendments to Regulation 31-103 and to Policy Policy 31-103 (“Notice of Consultation”) to enhance protection of older and vulnerable clients.

You will find below the comments I make in the context of this consultation as a Full Professor and Chair in Business Law and Governance at the Faculty of Law of the Université de Montréal (www.droitdesaffaires.ca).

1. General Comments

1.1 The Proposed Amendments to National Instrument 31-103 and to Companion Policy 31-103CP (“Proposals”) address an issue of great importance that is central to the investor protection mandate of the CSA. Indeed, as many studies and reports have pointed out, the vulnerability of investors is unfortunately exploited by registered and unregistered persons, causing losses which have disastrous consequences for the financial security of these investors.¹ In this context, we welcome this initiative by the CSA, which is in addition to a series of measures put in place in recent years and to which the Notice of Consultation refers.

¹ Raymonde CRÉTE et Christine MORIN, « La protection juridique des personnes âgées contre l’exploitation financière », (2016) 46 Revue générale de droit 5 (hors série); FONDATION CANADIENNE POUR L’AVANCEMENT DES DROITS DES INVESTISSEURS, Rapport sur les investisseurs vulnérables : maltraitance envers les personnes âgées, exploitation financière, abus d’influence et aptitudes mentales diminuées, novembre 2017; INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSION, Senior Investor Vulnerability, Final Report, FR03/2018, Mars 2018.

1.2 As the International Organization of Securities Commissions (IOSCO) suggests, it is possible to distinguish the abuses committed towards vulnerable investors according to the status of the people who commit the wrongdoings.²

1.3 On the one hand, we find abuses committed by unregistered individuals. These abuses consist of financial exploitation maneuvers generally perpetrated by relatives or people of confidence. Abuse can also take the form of financial fraud by third parties who offer the purchase of highly speculative securities or participation in fraudulent financial schemes.

1.4 On the other hand, registrants can engage in financial fraud or even participate in financial abuse harming vulnerable investors. In addition, they can offer investment products that are not suitable for them in view of their investor profile, by focusing on elements such as poor financial literacy, product complexity and pressure selling techniques.

1.5 We understand that the Draft Amendments primarily target the first type of abuse, i.e. those committed by unregistered individuals. They also address the issues raised by the diminished cognitive capacities of elderly investors. Recognizing the role of sentinels of registered individuals and companies, the CSA Notice of Consultation identifies two specific changes to strengthen the protection of vulnerable investors.

1.6 The first amendment would require that registrants take reasonable steps to obtain the name and contact information of a trusted contact person from each of their clients and their written consent to communicate with them. Under the proposed amendment, Companion Policy 31-103NP would clarify that registrants who are concerned about a client's financial exploitation or mental capacity should tell them about their concerns about their account or well-being before to communicate with anyone else, including the trusted contact person. In addition, Companion Policy 31-103NP states that if consent has been obtained, "a registrant might contact a TCP if they notice signs of financial exploitation or if the client exhibits signs of diminished mental capacity which they believe may affect the client's ability to make financial decisions" [emphasis added].

1.7 Although it is a relevant protective measure, it is possible to question the regulatory strategy chosen to implement it. The wording of the proposed amendments to National Instrument 31-103 suggests that the added obligation would be limited to obtaining the contact details of the support person. The steps to be taken in the event of a concern relating to the vulnerable investor would be found in Companion Policy 31-101CP, which does not have the same normative value. In addition, as recognized in the CSA Notice and Requestion for Comments, Policy Policy 31-103 is limited to providing guidance on their expectations regarding the use of a trusted contact person. In order to achieve the objectives pursued, it would seem preferable to state in National Instrument 31-103 the conduct expected of the registrant in such a context. Such precision would also improve legal predictability for companies and registrants.

1.8 The second amendment would add a new provision relating to temporary holds. Specifically, section 13.19 would state that nothing in the legislation or regulations prevents the registered firm or the registered individual whose registration it sponsors from imposing a temporary hold when the firm reasonably believes that one of the following two situations applies: i) the firm reasonably believes that a vulnerable customer is being exploited financially; or ii) in relation to an instruction he has given, the client does not have the mental capacity to make financial decisions.

² INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSION, Senior Investor Vulnerability, Final Report, FR03/2018, March 2018.

1.9 This is an important protective measure. With respect to its scope of application, it seems appropriate that temporary holds any form of operation as currently proposed by the proposals. Indeed, it seems that a protective provision like the one proposed should be broad and inclusive in order to achieve the objectives pursued. Similarly, the two main situations triggering the application of the new obligations relating to temporary holds are relevant.

2. Vulnerable Client

2.1 The following definition of “vulnerable client” is proposed. It is closely related to that of “financial exploitation”.

“vulnerable client” means a client of a registered firm or a registered individual, who may have an illness, impairment, disability or aging process limitation that places the client at risk of financial exploitation;

“financial exploitation” means, in respect of an individual, the use, control or deprivation of the individual’s financial assets through undue influence or wrongful or unlawful conduct;

2.2 There is no definition of vulnerable investor (client) in the academic literature. In the common sense, the vulnerable person as “one who can be easily reached, who has difficulty defending himself, who is fragile”.³ In this perspective, the vulnerable investor is the person who uses the services of a financial intermediary and who is in a situation where he finds it difficult to defend his own interests. Investor’s vulnerability can result from personal characteristics, as well as relational elements. Thus, the diversity of factors contributing to vulnerability means that there is no such thing as a “typical type” of the vulnerable investor.

2.3 Nevertheless, in the light of our literature review, we have identified four main criteria relevant to qualify an investor as vulnerable, namely age, state of health, visible minority status and level of knowledge.⁴

2.4 We note that the definition of vulnerable investor retained by the proposals only refers to two of these four main criteria. In addition, the definition seems to link the vulnerability of the investor to financial exploitation. This choice is probably explained by the limited nature of the proposed modifications which target specific situations of potential abuse.

2.5 We believe it is necessary for the CSA to go further in their efforts to put in place a regulatory framework that protects vulnerable investors. Among the initiatives to be considered is a more fundamental reflection on the definition of the vulnerable investor who would target the entire management of the financial sector under the CSA’s umbrella.

2.6 In particular, it is suggested that the CSA work with self-regulatory organizations to develop a common definition of a vulnerable investor.⁵ By establishing a common definition of vulnerability, regulators would create a frame of reference that highlights the fundamental elements of this issue. In addition to facilitating exchanges, adopting a definition common to regulators would help to ensure that the components of vulnerability are recognized regardless of the forum where the vulnerability is present. Similarly, the definition would allow decision-

³ Marie-Hélène DUFOUR, « Définitions et manifestations du phénomène de l’exploitation financière des personnes âgées », (2014) 44 *Revue générale de droit* 235, 245.

⁴ Stéphane ROUSSEAU et Damien HALLÉ-HANNAN, *Investisseurs vulnérables et application des lois: analyse de la jurisprudence disciplinaire des organismes d'autorégulation*, Montréal, Observatoire du droit des marchés financiers, 2020 <<https://www.droitdesaffaires.ca/publications/investisseurs-vulnérables-et-application-des-lois-analyse-de-la-jurisprudence-disciplinaire-des-organismes-d'autoregulation/>>.

⁵ *Ibid.*, p. 98-99.

making bodies to have guidelines for identifying this aggravating factor. Finally, this definition could be used by intermediaries as part of their own initiatives to prevent abuse by vulnerable investors.

In closing, I would like to thank the CSA for the opportunity to provide comments on this important regulatory initiative.

Yours truly,

A handwritten signature in blue ink, appearing to read 'Stéphane Rousseau', with a stylized flourish at the end.

Me Stéphane Rousseau, Ad. E.
Professor and Chair in Business Law and Governance
Université de Montréal