



knowledge**first**
FINANCIAL

October 18, 2019

VIA E-MAIL

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

The Secretary
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Dear Ms. Turcotte & Me. Beaudoin:

**Re: Proposed Amendments to National Instrument 31-103 and Companion Policy 31-103
Client Focused Reforms**

Knowledge First Financial Inc. (“Knowledge First” or “We”) is a nationally registered Scholarship Plan Dealer and Investment Fund Manager and is a wholly-owned subsidiary of the Knowledge First Foundation and Heritage Educational Foundation. Knowledge First has been providing peace of mind

Knowledge First Financial Inc.

FORMERLY
USC EDUCATION SAVINGS PLANS INC.

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education savings solutions to Canadians for over 50 years and currently administers over \$6.2 billion in education savings for over 500,000 customers, through a national network of over 1,400 registered Sales Representatives.

Knowledge First appreciates the opportunity to comment on the Proposed Amendments to National Instrument 31-103 and Companion Policy 31-103 (the “Client Focused Reforms”). Knowledge First also provided comments to the initial iteration of this project, Canadian Securities Administrators (“CSA”) Consultation Paper 33-404, *Proposals to Enhance the Obligations of Advisers, Dealers and Representatives Towards Their Clients*, published April 28, 2016 (the “Consultation Paper”).


We continue to recognize the tremendous significance of the Client Focused Reforms as an important part of the CSA’s efforts to maintain a fair and balanced regulatory environment for market participants and investors alike. As a registered Scholarship Plan Dealer and Investment Fund Manager, we operate in a very specialized niche market within the Canadian securities industry. Our products, Registered Education Savings Plans (RESPs), are highly complex to administer and support, in respect of the regulatory requirements under federal income tax legislation and federal and provincial government grants and incentives related to education savings, in addition to the securities regulatory environment relating to the distribution and investment management of the products. Further, in being directly regulated by the CSA members, we do not have the benefits of a self-regulatory organization to facilitate the development of consistent and transparent rules to support our business.

Therefore, while we do appreciate that the Client Focused Reforms are intended for feedback from all classes of registrants, we encourage you to consider our comments, where indicated, in the context of our standing in the regulatory marketplace as a highly-specialized, niche-market participant and in the furtherance of our business as a viable and successful organization whose singular mandate is to further the successfully post-secondary education endeavors of Canadian students.

Our comments are set out in the Appendix to this letter. We thank you once again for this opportunity to comment on this important proposal and welcome any questions you may have on our comments.

Sincerely,

KNOWLEDGE FIRST FINANCIAL INC.



Darrell Bartlett, CPA, CA, CIA
Chief Compliance Officer

Encl.

cc: R. George Hopkinson
President & Chief Executive Officer

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APPENDIX – COMMENTS ON CLIENT FOCUSED REFORMS

Know Your Client

Client Personal & Financial Circumstances

Knowledge First agrees with the new requirement to gather information on the client's personal circumstances and financial circumstances, as set out in the proposed reforms. Having and using this information will allow registrants to better know and understand the client, allowing for more informed choices when making suitable recommendations.

However, we note certain areas of these new requirements which in our view, could be strengthened.

1. The reforms include specific examples of important information to be collected regarding the client's personal and financial circumstances. However, these examples are contained in the Companion Policy. To provide clear direction to registrants for this new requirement, we suggest including these examples directly within Section 13.2 of the Instrument.
2. The reforms lack guidance on what registrants are to do with the information regarding a client's personal and financial circumstances, once it is collected. In our view, this guidance should include the CSA's expectations for how to analyze this information in the context of the client's existing investment portfolio and any recommended security trades. If the registrant is recommending the purchase, sale or hold of a security, the registrant should consider the client's personal and financial circumstances and assess whether the recommended trade is inconsistent with those circumstances. For example, if the client has a specifically defined liquidity need and the registrant is recommending the sale of one or more of the client's securities that are highly liquid, the registrant should consider whether this recommendation is suitable. As it is difficult to consider all possible scenarios for analyzing personal and financial circumstances, we recommend that this guidance be provided in the Companion Policy in general terms, with a few select examples to illustrate the guidance, such as the example we have provided.

Client Investment Objectives

Knowledge First appreciates the effort of the CSA, as set out in the proposed reforms, to address concerns related to the client's investment rate of return. However, the suggestion in the Companion Policy that *"Depending on the nature of the relationship with the client, and the securities and services offered by the registrant, registrants should take into account whether there are any other priorities, such as paying down high interest debt or directing cash into a savings account, that are more likely to achieve the client's investment objectives and financial goals than a transaction in securities."* is, in our view, unrealistic behavior for registrants to follow. This behavior is better suited for individuals and firms that operate in the financial planning industry. Only a portion of individual registrants also practice financial planning and even a smaller portion of such registrants are formally trained as financial planners. Individual registrants that are not trained in and do not engage in the practice of financial planning, may not be appropriately qualified and/or may not have sufficient information to give advice relating to personal debt or cash flow management.

We suggest instead that, if an individual registrant, in considering the client's investment objectives, personal and financial circumstances, believe the client could benefit from financial planning advice, that the registrant may only provide that advice if he/she is a qualified, practicing financial planner. Otherwise, the individual registrant should recommend that the client seek out the services of a qualified financial planning firm. Giving this advice should not preclude the individual registrant from providing a security recommendation to the client, provided the

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recommendation is suitable in view of the rest of the requirements in the Instrument.

Financial Goals

Knowledge First appreciates that the CSA has identified “investing for the post-secondary education of the investor’s children” as a financial goal that individual registrants should consider when assessing a client’s investment objectives. However, as specialists only in RESPs, Knowledge First is concerned that the proposed reforms establish a broader requirement for individual registrants, including Scholarship Plan Dealer (“SPD”) Dealing Representatives, to inquire about all of the client’s financial goals, as part of a more general requirements to determine investment objectives. Clients seek the services of Knowledge First and other SPDs specifically for assistance with saving for post-secondary education. SPDs already have policies and procedures in place, to collect and assess KYC information in fulfilling suitability requirements. Requiring SPDs to inquire about broader financial goals may only serve to confuse clients, who may wonder why the SPD needs this information. Further, it is not clear how this information would be used as part of the SPD KYC and suitability processes.

Rate of Return

Knowledge First is concerned with the reference in the proposed reforms requiring the registrant to set the investment return that would be required to meet the client’s financial goals, taking into account the client’s risk profile. Knowledge First provides investment solutions that assist clients with saving for post-secondary education. Knowledge First individual registrants are not in the business of, or are trained, to recommend investment solutions that are based on a rate of return. Our Dealing Representatives recommend the scholarship plan that is best suited for the customer considering the products and features of each Plan, as well as the customer’s ability to afford the proposed contributions to be made to their RESP. Whatever amount a customer can afford to contribute to their RESP will help achieve the customer’s financial goal of saving for post-secondary education; the Dealing Representative’s advice should not have to consider how the Plan’s investments are performing. Further, our Plans are each unique in design and are not set up for customers to move between different Plans based on the Plan’s investment performance. We recommend that SPDs be excluded from these requirements.

Client Risk Profile

We note that the requirement to gather information related to and assess a client’s ‘risk profile’ remains an integral part of the proposed reforms, despite the opposition to this requirement noted in ‘Annex D – Summary of Comments on Consultation Paper 33-404 and Responses’. The description in the proposed changes to the Companion Policy of the client’s risk profile and its determination, are a good first step to helping registrants understand this new concept. However, in our view, registrants will require more guidance and prescriptive details to not only understand, but effectively implement this new requirement across different business models. Registrants need a definitive, reliable framework to follow to implement this requirement, one that is easy to understand and ensures consistent outcomes across different business models.

As a result, we recommend that the requirement to prepare and analyze a client’s risk profile be removed from the proposed reforms. Instead, the CSA should work with independent risk management experts, as well as seeking input from registrants, to develop an easy-to-understand and easy-to-implement solution to this complex requirements.

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Updating KYC Information

Knowledge First questions the need for specific timeframes in which registrants would be required to update client KYC information, as set out in section 13.2 of the proposed reforms. If the policy objective is to ensure that registrants are using their best efforts to ensure KYC information is updated as changes occur, establishing an arbitrary time-period to determine if changes have occurred may not meet this objective. Instead, registrants should be asked to establish policies and procedures that the firm and its representatives would follow that would pro-actively make inquiries with the client, as to whether there have been any changes to their KYC information. This could include requests for updates in client trade confirmations, statements of account and other forms of client communication. It could also include such requests through email and other proactive messaging campaigns. This would ensure clients are aware of the importance of keeping their information up to date and avoid unnecessary communication and meetings with clients whose information has not changed.

Know Your Product – Representative

Knowledge First continues to support the proposed reforms that would establish a regulatory framework for KYP obligations for individual representatives. We recommend extending the proposed reforms, as set out in proposed paragraph 13.2.1(3) of the instrument, to include the type of account in which the security will be held. As RESP specialists, we repeatedly hear from customers how other registrants, who do not specialize in RESPs, lack the basic knowledge related to both this type of account and the implications of holding different securities within a RESP. We question whether individual representatives should even be able to offer or recommend securities to be held in a RESP without demonstrating a minimum level of proficiency for this unique and inherently complex product type. Customers from other firms often tell us about the lack of knowledge of non-RESP specialist representatives, regarding the availability of and qualifications for, government grant programs, how to apply and receive such grants, and the rules regarding contributions to and withdrawals from, RESP accounts.

Know Your Product – Firm

Knowledge First continues to support the proposed reforms that would establish a regulatory framework for firm KYP obligations. We do have concerns with the requirement for firms to understand a security in comparison to other similar securities in the marketplace. In our view, this additional requirement expands the KYP obligations to include knowledge of competitors' products, a 'KYCP' obligation. Our concern arises from the fact that it is unlikely a firm will ever be able know its competitors' products to the same level of detail as its own products. While this is not specified as the standard for completing this analysis, we are concerned that this will become the perceived standard for clients, especially those who become aggrieved. We fully support the requirement for firms to know and understand the products it offers, and agree with the rest of the proposed reforms in this area.

As a RESP specialist firm, we also offer the following additional KYP suggestion for firms – that the firm's KYP obligations extend to not only the types of securities offered, but also the types of accounts in which these securities are held. As noted above, we are recommending that individual representatives be required to demonstrate proficiency in RESPs in general before offering this account type to customers. We recommend that proposed paragraph 13.2.1(4) be extended to include not only securities that the sponsoring firm has approved, but also

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account types that the sponsoring firm has approved.

For firms that want to approve and make available to their representatives RESPs as an account type, we also recommend that the firm be required to disclose whether it offers all available government grants and incentives for RESP holders. If not, the firm should be required to compare themselves to other firms that do offer all RESP available grants and incentives. RESP grants and incentives, highlighted by the Canada Education Savings Grant (“CESG”), are an essential component of RESPs. The CESG is administered by Employment and Social Development Canada, who maintains a listing of all approved “Promoters”, those firms that are approved by ESDC to offer RESP grants and incentives. Knowledge First, as a RESP specialist firm, offers all available grants and incentives. Firms offering RESP accounts should be required to identify themselves, or the issuer of the security being recommended for the RESP, and inform customers whether they will be able to apply for available government grants and incentives and if not, identify which grants and incentives the customer will not be able to receive. The list is located at <https://www.canada.ca/en/employment-social-development/services/student-financial-aid/education-savings/resp/resp-promoters-list.html>.

Suitability

General Comments

As Knowledge First identified in our comments to CSA Consultation Paper 33-404, our challenge as non-SRO members is the lack of consistency between Scholarship Plan Dealers for KYC information and resulting suitability analysis. We again encourage the CSA to work with the RESP Dealers Association of Canada (“RESPDAC”) to develop uniform rules and guidance for KYC information suitability assessments that would be applicable to all Scholarship Plan Dealers specifically.

Suitability Determinations

We do not oppose the proposed reforms that would require the firm’s CCO or other senior individual to periodically review a sample of client files to ensure the firm’s suitability process is being followed (page 169 of proposed reforms). However, as a new and very specific directive, we recommend that this requirement be moved from the proposed Companion Policy to the actual instrument itself. This will highlight the importance of this requirement and ensure there is no ambiguity as the authority and enforceability of this requirement.

Portfolio Approach to Suitability

We support the continued shift away from trade-based suitability, moving to portfolio suitability, as the basis for an initial and ongoing suitability determination. However, we question the proposed requirement of the registrant to inquire as to the client’s other investments or holdings at other firms. Clients may not want to disclose this information for fear of putting their relationship with the other firm at risk. Further, it is not clear what standard the firm and its representatives will be held to, or could be held to, if the client refuses to disclose some or all of this information. Will a firm or representatives be required to make multiple inquiries until the information is provided? Will the firm or representative have to provide detailed risk disclosure information to the client if the information is not provided. Does this information form part of required information for KYC purposes that, if not provided, will require the firm to deny service to the client?

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We do not support this requirement as we believe it will create a negative and untrustworthy relationship between the client and the firm, which is not conducive to the firm fulfilling its KYC and suitability obligations. If this requirement is maintained, we recommend it be included in the proposed instrument, rather than the Companion Policy and that it be expanded to address the concerns we have set out above.

Use of Borrowed Funds

Knowledge First believes that one of the leading causes of suitability issues and client losses is the use of borrowed funds to purchase securities. Section 13.3 of the existing NI 31-103 sets out minimum disclosure requirements to be followed when borrowed funds are used. This is also part of the existing Relationship Disclosure requirements described in section 14.2 of NI 31-103. The proposed reforms extend the suitability obligation to situations where leveraging, the use of borrowed funds to purchase securities, exists. We recommend that instead, the CSA prohibit outright the practice of leveraging altogether, and only allow borrowed funds to be used to purchase securities, in connection with a margin account, operating under the existing rules of The Investment Industry Regulatory Organization of Canada.

Conflicts of Interest

Referral Arrangements

We note the revisions regarding permitted referral arrangements in the proposed section 13.8 of the Instrument that require both parties to a referral arrangement are securities registrants. For Knowledge First and other SPDs that currently treat existing agreements with third-parties where the firm receives names and contact information of informed prospective customers in exchange for compensation (“Leads Agreements”), these revisions would eliminate these agreements. The firms who provide information under the Leads Agreements are not in the securities or investment industries and it would be unreasonable to expect that these firms would or could become registrants in order to continue these agreements.

Notwithstanding the proposed revisions in this section, we suggest that Scholarship Plan Dealers who enter into Leads Agreements be exempted from these provisions. These Leads Agreements are not within the intention or the spirit of the existing referral arrangement requirements. Referral arrangements more typically involve two firms, each of which offers securities, investments and other financial services products. The need for referral arrangements arises where one firm has a customer who wishes to purchase, or receives a recommendation to purchase, a product or service that the firm does not offer. This firm enters into a referral arrangement with another firm that does offer the product or service the customer wants or needs, and will often receive compensation in exchange for making the referral.

Leads Agreements are different from this. Parties who provide names and contact information to Scholarship Plan Dealers are not selling securities, investments or other financial products. In many cases, these parties are not selling anything; rather the party often serves as an aggregator for products, services and information that is provided for free and is of interest to certain targeted groups, such as new moms or young families. Members of the targeted group agree to provide their names and contact information in exchange for obtaining details on the products,

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services or information offered by the aggregator, who partners with the various actual providers of these items. For RESPs, the parties will enter into agreements with Scholarship Plan Dealer such as Knowledge First, to receive the names and contact information of interested and informed members of the targeted groups. This is a different from the typical referral arrangement and, in our view, should not be captured by the existing or proposed requirements of NI 31-103.