

June 3, 2013

COMMENT LETTER/SUBMISSION STATEMENT OF PRIORITIES

**ONTARIO SECURITIES COMMISSION
NOTICE 11-768 – REQUEST FOR COMMENT
STATEMENT OF PRIORITIES
April 4, 2013**

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The Investor Advisory Panel is pleased to submit this comment letter regarding Ontario Securities Commission Notice 11-768 – Statement of Priorities.

Executive Summary

The Investor Advisory Panel (IAP) was established to provide the Ontario Securities Commission with its advice on retail investor protection. Our response to the *OSC Statement of Priorities for Financial Year to End March 2014* will therefore focus on those priorities which address retail investor protection issues.

The Panel is satisfied that the OSC has identified key retail investor priorities that require its immediate attention, with some exceptions. We support the Commission's efforts to expand outreach and engagement. We also support the Commission's goals to improve accountability by increasing transparency of its regulatory performance, but note that ultimately success will be determined based on results rather than on processes. The Commission needs to set more specific deliverables within specific time frames. We recognize that this is not always easily done but we encourage efforts to move more in this direction.

The Statement of Priorities identifies the most important areas where the OSC intends to focus its resources. These five areas are: expanding outreach to investors and community leaders; cost effective access to capital; enhanced compliance oversight, especially suitability obligations for registrants; intensifying its enforcement program; and market structure issues. Three of

these areas of focus directly impact the Commission's capacity to deliver strong investor protection, which we are particularly interested in given our mandate.

Since its establishment, the Investor Advisory Panel has called on regulators to act promptly to ensure more effective investor protection. Our priorities have focused on the provision of fair and informed advice to retail investors. Our recommendations have included ensuring that the adviser is the true agent of the client, putting the clients' interests first; eliminating compensation practices which can bias advisers' advice and product recommendations; requiring advisers to have appropriate qualifications and to use informative, accurate business titles; and ensuring fair, timely and independent complaint handling, enforcement and compensation.

It is in light of this agenda for retail investor protection that the IAP offers its comments on the current priorities of the Ontario Securities Commission.

Delivering strong investor protection; the Registrant/Client relationship

The provision of fair and informed advice by qualified registrants is the foundation of the registrant/client relationship. At issue is whether or not the standard of suitability currently applicable to advisers and dealers offers sufficient investor protection.

Best Interest Standard

In our response to the CSA consultation paper on the merits of replacing the current suitability standard with a statutory best interest duty (Submission re CSA Consultation Paper 33-403, March 1, 2013), we noted that "in today's rapidly evolving and complex marketplace, with a plethora of opaque and complicated product offerings that even professionals are sometimes challenged to understand, investors must be protected through higher standards than today's inadequate suitability regime". The Statement of Priorities acknowledges that the increased complexity of available investment products has blurred the lines between securities, insurance and investment products, and has created challenges for retail investors to determine product suitability. The Statement of Priorities also acknowledges concerns that "the current (suitability) standard of conduct may not adequately address the information and literacy imbalances that exist between advisers and dealers and their retail clients". We share these concerns and in our response to the CSA discussion paper called on Canadian regulators to emulate their counterparts in the UK and Australia, who are now implementing a best interest duty, and raise the bar on investor protection in Canada. In particular, we urge the OSC to work with FSCO to ensure segregated funds are dealt with in the same way as mutual funds.

We have also called for less regulatory reliance on disclosure, a demonstrably inadequate investor protection measure in today's marketplace, supporting instead a best interest standard regime which would require avoidance, rather than mere disclosure, of adviser conflicts of interest (for example, prohibiting embedded compensation/trailer commissions for mutual funds).

The Statement of Priorities notes that introduction of a statutory best interest standard is a complex issue that requires careful consideration in order to protect investors while recognizing challenges to the current business models of market participants.

The Panel has full confidence in the Canadian investment industry's innovation and creativity, which they have so richly demonstrated in responding to business opportunities in a constantly evolving marketplace, to respond to regulatory change that may require them to modify their current business models. A fair advice regime which delivers robust investor protection will benefit Canada's investment industry, whose business models ultimately derive their success from earning the trust and confidence of their clients.

Implementation of Best Interest Standard

We believe that impact studies are appropriate and useful. These studies have proven useful in other jurisdictions and we would encourage the Commission at the same time to carefully consider impact studies already undertaken by UK and Australian regulators as they moved to implement a best interest duty. We strongly urge the Commission to undertake a simultaneous study on the impact of imposing a best interest duty on all parties, – dealers, advisers and investors – not just on advisers and dealers, as currently proposed. Examining the impact on all parties will foster informed, constructive and balanced examination and advancement of this key investor protection initiative.

While we are supportive of thoughtful, careful analysis and a measured regulatory response, we note again that Canadian regulators are lagging behind regulators in other jurisdictions where implementation, not study, of many of these new initiatives is now underway. Canadian investors need and deserve high standards of investor protection. We urge the OSC to move expeditiously to decide on the merits of a statutory best interest duty. It has taken close to 13 years to introduce the Client Relationship Model, and it is still an estimated three years away from full implementation. Canadian investors cannot afford this slow pace of reform. Justice delayed is justice denied.

Professional Titles and Specific Proficiency

In our comment letter on the merits of introducing a statutory best interest duty (Submission re CSA Consultation Paper 33-403, March 1, 2013), we strongly recommended that this be accompanied by a reform of regulation regarding titles and the specific proficiency requirements to support the use and maintenance of such titles.

Business titles and designations need to be meaningful and representative of an individual's proficiency but, unfortunately, today's regulatory regime does not ensure that this is the case. Until regulators set out clear rules, investors will continue to be, at best, confused, and at worst, badly misled. This is also unfair to those many industry participants who deserve clarity about and support for their high professional standards.

While we fully support the Commission's goal to "better educate investors about the dangers they may face from unregistered entities and advisers", we would encourage them to also

educate investors about the dangers they may face from registered entities and advisers using misleading and inaccurate titles. As part of their investor protection efforts, regulators have recently been encouraging Canadian investors to check their adviser's registration status. Unfortunately, investors are unable to properly verify the registration status of their adviser if the adviser is carrying out his/her business activities using self-selected titles (such as Seniors Specialist or Senior Wealth Advisor) which will not appear in regulators' official registration records. The Commission should make title reform a priority for its registrants and also begin discussion with the self-regulatory organizations to encourage them to move beyond guidance to action.

We are pleased to see the Commission's intent to "work with standard setters to advance registrant proficiency through changes to professional standards and industry examinations." We assume that this would include working with the self-regulatory organizations, such as MFDA and IIROC, to encourage them to also undertake a long overdue comprehensive review of the educational and professional requirements for their registrants.

Complaint Handling

We note with concern the absence of references to fair and timely complaint handling and compensation. In our response to the CSA consultation paper on OBSI (Submission re CSA Consultation Paper 31-103, January 31, 2013), we urged regulators to move immediately to address OBSI's inability to enforce its compensation recommendations and to make other improvements to the existing complaint handling regime for CSA registrants. We reiterate our recommendation that CSA registrants be subject to the same complaint handling standards introduced for firms and advisers regulated by IIROC and the MFDA several years ago. All investors deserve fair, timely and independent complaint handling and compensation. We are somewhat puzzled that this is not identified as a current priority for the OSC. We recommend that the OSC include it as a priority, given that the Commission and its CSA colleagues are still assessing responses to their Consultation paper and have not yet communicated their intentions.

We also recommend a stronger and clearer focus on seniors' issues. This should be a priority for the Commission in its policy development, compliance and enforcement activities. Many Canadian and American regulators have recognized the particular vulnerability of seniors and have made the protection of seniors a regulatory priority. We strongly believe that the OSC should also adopt this focus as a top priority.

Delivering strong investor protection: better application/or enhancing current rules

The Panel and the OSC have clearly identified new directions that would deliver more robust investor protection. Until such time as these reforms are in place, we agree that the Commission must make better application of, compliance with, and/or enforcement of existing rules a priority.

Disclosure

We support efforts to provide investors with ***more effective and meaningful disclosure***. We have already provided our views on necessary improvements to Fund Facts and hope they will be quickly introduced and implemented. We agree that increasingly complex products such as leveraged, exchange traded funds are another area where clearer information should be provided. We would encourage the Commission to link its success measures (for all its priorities) to clear deliverables at a specific time rather than to provide abstract and time-free goals like “advancing improvements”. We would hope, for example, that it would be possible to set a goal of not just developing but introducing a summary document for ETFs within the next calendar year. We appreciate the time constraints imposed by lengthy consultation processes but we ought to be able to make timely improvements, especially when dealing with the application of existing rules.

Suitability

We strongly support the many initiatives that focus on ***better and more effective compliance***, and where necessary enforcement actions, to ensure that the advice provided to investors is suitable and unbiased. Both IIROC and the MFDA have reported that ***suitability*** is by far their most frequent 2012 complaint issue (Source: IIROC and MFDA 2012 Annual Enforcement Reports).

We commend the Commission for undertaking a mystery shop research sweep of advisers to assess the suitability of advice currently being provided. We assume that the results of this research will be published. We also look forward to the published results of the 2012-13 compliance suitability sweep. Compliance reviews and sweeps of suitability need to acknowledge at the outset that the very foundation of any suitability recommendation – the KYC documentation – is deeply flawed and actually facilitates the provision of unsuitable recommendations. We would suggest including an additional success measure for these enhanced suitability compliance efforts. The anticipated “efficient and timely referrals of serious cases of unsuitable advice to Enforcement” should also be a key public indicator of success.

Mutual Fund Fees

The IAP supports regulatory reforms to address investor protection and fairness issues regarding the ***current structure of mutual fund fees***.

The Commission intends to “consider comments on the discussion paper”, “host a stakeholder roundtable” and “develop recommendations for next steps”, “identify options to move forward” and “publish a progress update”. It will measure success through positive feedback from stakeholders on engagement in the consultation process and on the quality of OSC policy and impact analysis. Success will also be measured through completing the analysis and identifying options for next steps.

We believe the Commission needs to go farther than this. The consultation paper eloquently and effectively analyzed the current fee structures for mutual funds and has already identified a number of options to move forward.

We need to move beyond talking, beyond advancing the discussion. Identifying additional options to address the mutual fund fee structure is not necessary and simply delays the process. It is time to decide. It is time to choose an option and to turn our collective efforts to effective and fair implementation.

Fixed Income Market

We strongly support the proposed ***review of the fixed income market*** and development of an action plan to address specific key gaps or risks to investors. Retail investor participation in the fixed income market is significant. Recent statistics show that approximately one quarter of retail client assets entrusted with Canadian investment dealers is invested in fixed income securities. (source: The Investment Industry Association of Canada). As the Statement of Priorities notes, issues such as transparency (the absence of pre and post trade transparency) and investors' search for yield in the current low interest environment are a potential source of risk. Canada's fixed income market differs significantly in structure and operations from markets for listed securities and strongly disadvantages retail investors who do not have access to reliable and independent pricing and yield information.

As the Statement of Priorities notes: "more investors have broadened their investments beyond equities and saving and now include fixed income, real estate, private equity and other strategies as they search for better returns. This demand for yield may increase the potential for mis-selling.... The flow of assets into fixed income securities, either directly or into mutual funds, also raises questions about whether investors understand the impact of interest rate changes on their investments." Seniors and Canadians approaching retirement are at particular risk as they turn to fixed income investments to preserve their savings. We encourage the Commission to also work closely with IIROC which recently issued a proposal for timely surveillance and enhanced oversight of this important market.

Delivering strong investor protection: Timely and Effective Enforcement

The Panel endorses the Commission's efforts to improve the efficiency and effectiveness of its enforcement processes, including seeking criminal or quasi criminal sanctions where appropriate. We support the current focus on deterrence through targeted investigations of scholarship plan dealers, insider/manipulative trading, and the role of gatekeepers. It may also be appropriate to consider the use of investigative tools available to regulators in other jurisdictions. For example, wiretapping has been integral to recent US successes in investigating and prosecuting insider trading cases. We would like to see a focus on senior investors in the Commission's complaint handling, investigations and prosecutions. We encourage the Commission to demonstrate success through expanded reporting of results, particularly with regard to suitability and seniors. Finally, we encourage the Commission to continue to seek out innovative enforcement tools and partnerships with other policing agencies and new approaches to the collection of fines.

Capital Markets Accessibility- shareholder democracy and capital raising

The Panel has supported the OSC's policy initiative to improve shareholder democracy through the introduction of final rules for a new, clear regime for the use of shareholder rights plans. In addition, the IAP encourages the OSC to continue the review and regulatory development of the shareholder democracy issues begun in OSC Staff Notice 54-701, Jan. 2011:

- Slate voting and majority voting for uncontested director elections;
- Shareholder votes on compensation; and
- The effectiveness of the proxy voting system.

As the IAP has previously pointed out in its submission to the OSC (Submission re OSC Staff Notice 54-701, April 10, 2011), shareholder democracy is important to all investors, both institutional and retail. We believe that the interests of retail and institutional investors are largely aligned on issues relating to shareholder democracy and corporate governance. We also wish to emphasize that a central principle of the IAP is that investors, both retail and institutional, should be as well protected in Ontario as they are in other developed market systems. The advances in shareholder democracy and corporate governance rules in other advanced markets highlight the need to examine the rights of investors in Canadian public corporations.

The Panel understands the need to explore opportunities to improve access to capital for issuers and agrees that this legitimate objective must be achieved while maintaining an appropriate level of investor protection. We have not commented formally on proposals regarding crowd funding but do have concerns with regard to investor protection. Failure to ensure robust investor protection from abuses would undermine investor confidence in the regulatory regime.

Delivering strong investor protection: investor outreach and focus

We will conclude this Comment Letter with our views on the Commission's laudable focus on investor outreach and engagement. We believe that outreach and engagement are essential in sound policy development. However, we do not agree with the proposed focus on "understanding investors' key concerns." With respect, we believe that investors' primary concerns have been clearly identified and should by now be widely understood. They have been strongly advocated by many individual investors as well as organizations like the Canadian Foundation for the Advancement of Investor Rights (FAIR), the Small Investor Protection Association, and this Panel. We acknowledge the financial support of the Commission for both FAIR and this Panel and encourage other securities commissions to similarly support participation by informed and independent retail investor voices to ensure investor concerns are clearly understood.

The Commission needs to shift the focus of its outreach and research to solutions identification and determining the appropriate regulatory responses it needs to take to address these

identified concerns. Ultimately, success will be measured by evidence of decisions taken supported by action plans with specific timelines.

Conclusion

In this Comment letter, we have provided our views on the Commission's priorities and identified where they are aligned with and supportive of our key concerns. We have consistently urged the Commission to move beyond issue identification and discussion and into the realm of response and action. Research like mystery shopping, impact studies of implementation of specific options, and compliance sweeps can advance an evidence-based decision making process. The Commission should also devote research resources to analysis of the many research projects and studies undertaken by regulators as they moved to implement major regulatory reforms in the UK and Australia to determine the best options for the Canadian situation. We think that this is a role which could be carried out in part by the Office of the Investor. We look forward to continuing a detailed dialogue on the work of this newly formed and important Office as it makes its contributions in such key Commission initiatives as reform of mutual fund fee structures and the introduction of a statutory best interest duty.

The Investor Advisory Panel looks forward to providing our input and support to the Commission as it undertakes engagement with retail investors in Ontario and works to provide strong investor protection.

We hope that this Comment Letter is helpful to the Commission and are pleased to respond to any questions regarding this submission.

The Investor Advisory Panel.

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