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Mr. Robert Day  
Senior Specialist, Business Planning  
Ontario Securities Commission  
20 Queen Street West  
Suite 2200, Box 55  
Toronto, Ontario M5H 3S8

Dear Mr. Day:

**RE: Ontario Securities Commission Notice 11-771 – 2015-2016 Statement of Priorities**

We are writing to provide comments on behalf of the Members of The Investment Funds Institute of Canada (“IFIC” or “we”) with respect to the draft of the OSC’s Statement of Priorities (“the Statement”) for the financial year ending March 31, 2016.

**General Commentary**

As the Statement observes, today’s complex capital markets environment generates a host of challenges and issues that influence the regulatory agenda. These same factors are directing the agendas of our association and its Members, resulting in a convergence of many of the industry’s priorities with those of the OSC. Capital market structures and products continue to evolve at a rapid pace and, with the implementation of transformative reforms like CRM2 and the ongoing development of a cooperative Capital Markets Regulatory Authority (CMRA), the regulatory framework is evolving rapidly too. Shifting responsibilities for retirement savings mean that more and more Canadians will enter the capital markets for the first time. At the same time, increasing choice in investment products and distribution systems, coupled with structural demographic and economic shifts, mean that Ontarians will increasingly rely on financial advice to help secure their financial well-being.

We strongly concur with the Statement’s comment that “A well-functioning investor/advisor relationship is critical to the well-being of Ontarians and ultimately to achieving healthy capital markets”. For the millions of Ontarians who work with a trusted advisor in order to save and invest for the future, this relationship is already strong, and the investor experience will only improve in the months and years ahead as Canada’s world-leading disclosure reforms come into effect. Like the OSC, IFIC’s members are wholly committed to an environment where investor reliance on advice is well-placed, the advice being provided is suitable, and any conflicts are managed appropriately. We look forward to working with the OSC to realize these objectives in the year ahead.

We provide additional comments below on several of the Commission’s goals for the coming year.

## Goal 1 – Deliver Strong Investor Protection

As the Statement observes, existing regulatory requirements, including know your client (KYC), know your product (KYP) and suitability are among the most fundamental obligations owed to a client. These obligations are at the very foundation of a strong investor experience – one in which clients are confident that they are receiving high quality advice and can take comfort knowing that they are suitably invested for the future. Our Members are wholly committed to fulfilling these obligations and to safeguarding the trust that their clients place in them.

In the year ahead, the OSC has indicated it will bring its ongoing consideration of several proposals to conclusion, including whether a need exists for regulatory provisions to create a best interest duty and a review of mutual fund compensation arrangements. IFIC has previously provided the OSC with detailed, factual responses to both proposals. We are gratified that the OSC is considering both proposals carefully and has commissioned empirical research to inform its decision-making. Our views remain unchanged: the imposition of a statutory fiduciary duty on advisors would cause myriad legal complications and raise the cost of investing for ordinary Canadians, while a prohibition on embedded commissions would deprive investors of choice in how they pay their advisor and ultimately foreclose access to vital financial advice for those investors with smaller accounts.

Before considering such disruptions to the advisor/client relationship, the OSC should first assess the impacts of ongoing improvements to the investor experience and then identify any remaining areas in which this experience could be strengthened further. The Statement points to a number of possible areas of consideration. First, the OSC has identified improving retail investment product disclosure as a priority issue. This is an area where, as a result of recent reforms, Canada already leads the world. Over the past year, we have shared Fund Facts and the CRM2 cost and performance reports with industry colleagues and regulators from around the world. Consistently, we hear that these documents represent the gold standard in investor disclosure and far exceed what is available to investors abroad. Fund Facts is considered a global model for plain language investment product disclosure, and the pre-sale delivery of Fund Facts will allow all retail investors to easily access the key information about a fund before they make a purchase decision. With the implementation of CRM2, retail investors will soon have a full suite of easy to understand, plain language statements and reports to help them better understand their investments. The CRM2 reports will also bring clarity to the question of whether investors fully understand the costs of investing. In the public conversation around mutual fund compensation structures, embedded commissions are sometimes mischaracterized as “hidden” fees. This is inaccurate today, as these costs are fully and clearly disclosed within the Fund Facts and prospectuses, and they will become fully transparent to investors on a recurrent basis with the full implementation of CRM2 and the delivery of that information through their statements.

Our Members are dedicated to the success of CRM2 and view the implementation of CRM2 as an opportunity to demonstrate their value to clients.

Moreover, the development of Fund Facts and the implementation of CRM2, coupled with shifting investor preferences, have already engendered structural changes within the Canadian funds marketplace. In just the past few years, an array of different fund types, distribution channels and advice structures have emerged and achieved significant growth. These options, which include D- and F-series mutual funds, exchange traded funds (ETFs), and so-called ‘robo-advisors’, all point to an increasingly diverse and competitive marketplace in which investors can easily choose a preferred style of investment management and how (or whether) to pay for financial advice. We anticipate that these changes will only accelerate in the years ahead as CRM2 comes to full fruition. These developments should alleviate the OSC’s concern that the existing embedded commission model is poorly understood and limits consumer choice. Rather than taking disruptive regulatory action even as another transformative reform is implemented, the OSC should allow CRM2 to take full effect and its associated market developments to continue apace. This will allow the OSC to prudently assess whether CRM2

has addressed its concerns with the advisor/client relationship and mutual fund compensation structures and identify any remaining areas of concern.

Second, the Statement identifies the wide disparity of financial literacy and understanding among investor groups as a key source of risk for the OSC. We agree. Given the complexities of today's capital markets, investors with limited financial literacy and lacking guidance may be at risk of making poor financial decisions and susceptible to fraud. This reinforces the important role played by financial advisors, who not only help their clients select particular investment options or manage their portfolios, but also coach them in financial decision-making and how to save and invest to meet life goals. The investment funds industry is a valuable partner for policy makers seeking to improve financial literacy, as demonstrated through the resources it has dedicated to creating investor-friendly, plain language documents under CRM2. We would welcome the opportunity to collaborate on future initiatives and share best practices with the OSC on this subject.

Third, the Statement references the particular challenges posed by aging demographics and the growing number of senior investors. These challenges, especially when manifested through cognitive impairment and financial vulnerability, are inherently complex and sensitive. While there are no easy answers, working collaboratively with other stakeholders to identify and address these issues is a priority for our Members. That is why IFIC has established a multi-stakeholder committee, consisting of industry representatives, regulators and investor advocates, to consider these issues in detail, examine best practices in both Canada and abroad, and develop practical tools to help the industry serve and support vulnerable investors. We welcome the OSC's involvement in this important project.

Lastly, under the specific priority issue of fostering capital formation in Ontario while maintaining appropriate investor safeguards, the Statement commits to working with the SROs to mitigate the opportunities for regulatory arbitrage. The significant improvements to mutual fund disclosure generated by Fund Facts and CRM2, while positive in many respects, also give rise to a risk of regulatory arbitrage, given that other substitutable financial products may not be subject to the same level or type of disclosure. The additional interventions currently under consideration by the Commission would only amplify the risk of regulatory arbitrage: for instance, banning embedded commissions for only one type of financial product could lead investors to switch to similar products that still allow consumer choice in fees payment. If the OSC moved in this direction Canada would be the only jurisdiction in the world where such action was focused on a single product.

## **Goal 2 – Deliver Responsive Regulation**

With reference to the rapid changes taking place within Canada's securities regulatory landscape, the Statement observes that:

Within the context of today's capital markets, we continue to believe that a national securities regulator will enhance investor protection, foster efficient rulemaking and globally competitive markets in Canada, strengthen our capacity to identify and manage systemic risk and solidify Canada's international reputation for regulating its financial system. While working with the participating jurisdictions to transition smoothly to the CMRA it will be critical for the OSC to maintain high standards of regulation and to keep stakeholders informed and engaged throughout the transition period. The OSC will also need to work with the CSA to seek harmonized approaches to regulation as much as possible.

We concur and would emphasize the need for continued regulatory harmonization within Canada's capital markets. While we support the development of a cooperative regulatory system, we are concerned that the process by which the participating jurisdictions have advanced this proposal has led to a number of important regulatory changes outside of the normal rule-making consultative process. The continued non-participation of some provincial jurisdictions in the new cooperative system raises a number of questions about the future

functioning of Canada's generally harmonized securities regulatory framework. Accordingly, we would encourage the OSC to give priority to addressing how the proposed CMRA will interact with any non-participating jurisdictions, along with further detail on the decision-making protocol within the new system. Above all, and as the Statement correctly observes, it is imperative that the OSC and other participating jurisdictions keep stakeholders informed and engaged throughout the transition period.

The sequencing of regulatory change also matters. During a fiscal year in which so many major initiatives are coming to fruition, the OSC must pay close attention to the linkages between policy areas in order to avoid duplication and ensure that reforms are effective and efficient. As an example: the Statement commits to introducing both a mandated CSA risk classification methodology for mutual funds and a new summary disclosure document for ETFs in the year ahead. However, without sufficient collaboration between the two projects, the ETF disclosure documents (if modeled after Fund Facts) could be developed and implemented using existing fund risk methodologies, only to be shortly thereafter required switch to a different methodology. By proactively coordinating the sequencing of its various initiatives, the OSC can avoid the risk of duplicative effort, improve the efficacy of its regulatory agenda, and lower the administrative costs that are ultimately borne by retail investors.

### **Goal 3 – Deliver Effective Compliance, Supervision and Enforcement**

As Canada moves towards a more integrated securities regulatory system, IFIC urges the OSC, its counterparts within other provinces, and the SROs to deter misconduct by improving enforcement harmonization. Specifically, IFIC believes that if an advisor is banned for misconduct within one provincial jurisdiction, then this ban should apply nationwide. Although the vast majority of advisors abide by the rules and serve their clients well, a nation-wide registry of advisors who have committed misconduct would help to protect investors and increase their confidence in Canada's capital markets. We recognize that creating such a nationwide investor protection regime would require considerable coordination on the part of Canada's provincial securities regulators and SROs; however, we would be pleased to provide whatever assistance is required to bring such a system to fruition.

### **Goal 4 – Promote Financial Stability Through Effective Oversight**

Both in Canada and around the world, regulators are increasingly focused on how best to manage systemic risk within capital markets. While these risks warrant close attention and appropriate regulation, IFIC remains concerned that investment funds continue to be identified by some as potentially systemically risky entities, when in fact they act as risk dampeners and bulwarks of stability within our increasingly complex capital markets. The unique structure and strict regulation of investment funds means that attempts to impose systemic risk rules from other regulatory spheres, such as bank capital requirements, would cause irreparable harm to the investment funds industry and ultimately to retail investors.

We are encouraged to note that under the proposed CMRA, the regulation of systemic risk within capital markets would appropriately remain with the capital markets regulator. Given the OSC's leadership role in setting the international regulatory agenda, we urge the OSC to advocate for effective and measured tools to manage systemic risk within capital markets and to push back against the application to investment funds of inappropriate rules from other regulatory arenas.

### **Goal 5 – Be an Innovative, Accountable and Efficient Organization**

In today's globalized environment, securities regulators are increasingly looking beyond their borders for ideas, emerging trends and best practices. In doing so, however, regulators must take care to embed their international benchmarking and evidence-gathering within a strong understanding of the local regulatory and market context. Without this understanding, there is a risk that reforms which are appropriate for one market may be inappropriately applied without reference to the local context in others.

As the OSC engages with its international counterparts, we urge it to not only take this context-specific outlook, but also to promote a strong understanding of what makes Canada's world-class regulatory system so unique. From the creative application of behavioural economics in the development of Fund Facts, to the exceptional cost and performance disclosure forthcoming with CRM2, to the unique role played by our SROs, we believe that the Canadian regulatory system offers a number of success stories that should be shared as widely as possible.

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We thank you in advance for considering our comments on the 2015-2016 Statement of Priorities. Please do not hesitate to contact me directly, or contact Graham Smith, Senior Policy Advisor by email [gsmith@ific.ca](mailto:gsmith@ific.ca) or by phone at 416-309-2328 if you have any questions or would like to discuss our comments in more depth.

Yours sincerely,

THE INVESTMENT FUNDS INSTITUTE OF CANADA



By: Joanne De Laurentiis  
President & CEO