Gluskin Sheff

September 30, 2016

Alberta Securities Commission
Autorité des marché 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
comments@osc.gov.on.ca and consultation-en-cours@lautorite.qc.ca

Re: Canadian Securities Administrators Consultation Paper 33-404 – Proposals to Enhance the Obligations of Advisers, Dealers, and Representatives Toward Their Clients

Gluskin Sheff + Associates Inc. ("Gluskin Sheff") is an independent wealth management firm that manages investment portfolios for high net worth private clients as well as select institutional investors, including family offices, foundations, endowments and both public and private pension plans. Gluskin Sheff is also a publicly-traded corporation listed on the Toronto Stock Exchange. We are pleased to have the opportunity to comment on the Canadian Securities Administrators' ("CSA") Consultation Paper 33-404 – Proposals to Enhance the Obligations of Advisers, Dealers, and Representatives Towards Their Clients (the "Proposals").

Our response is primarily focused on the practical implications of the Proposals on Gluskin Sheff and other firms that offer discretionary investment advice under the Portfolio Manager category of registration, although some of our comments may be applicable to other business models or registration categories. In addition, we have commented briefly on the proposal for a regulatory best interest standard.

We are generally supportive of the CSA's work towards "improving the relationship between clients and their advisers, dealers and representatives", and recognize that our industry should continue to push for best practices to be established and implemented across registration categories.

Conflicts of Interest – General Obligation

We recognize that there are many conflicts of interest that arise in the course of providing our discretionary services to our clients. The CSA has, in our opinion, correctly prioritized this as an area to highlight and any attempt to establish best practices in this area are a benefit to the industry.

Question 1 – Is this general approach to regulating how registrants should respond to conflicts optimal?

We feel that the general approach proposed, subject to our specific comments throughout the remainder of this comment submission, is a reasonable approach to dealing with conflicts of interest. We are supportive of the requirement that firms and representatives respond to each material conflict of interest in a manner that prioritizes the interests of the client ahead of the interests of the firm and/or representative. In addition, clear and well-written disclosure can be

a useful tool to assist clients in understanding the inherent conflicts of interest in this industry and the specific conflicts that arise at each firm.

Question 2 – Is the requirement to respond to conflicts "in a manner that prioritizes the interest of the client ahead of the interests of the firm and/or representative clear enough to provide a meaningful code of conduct?
We currently use similar language in our Code of Business Conduct and Ethics at the firm, and feel that it provides a solid general principle for guiding our decisions.

We would like further guidance on the requirement that "firms and representatives should have a reasonable basis for believing that clients fully understand the implications and consequences of the conflict between the firm or representative and the client". Any assessment of the client's ability to understand is, by its nature, a subjective evaluation. We feel that this would be difficult to monitor and test for at the firm level and likely difficult to regulate. Once the conflict and the potential implications have been explained in clear language, we believe that a registrant's duty has been discharged unless there is reason to believe that a particular client does not understand.

Question 3 – Will this requirement present any particular challenges for specific registration categories or business models?
One area that could present a challenge, and is not be appropriate for a discretionary manager, is the requirement to obtain consent before a transaction is entered into. This would be inconsistent and unworkable with the discretionary authority that our clients have granted us. Our clients have delegated the everyday management of the assets they have put under our management, and we are obligated to take actions in our clients' best interests already, as outlined in the following paragraph. Disclosure of this obligation and identified conflicts of interest and how we respond to them should be sufficient to inform clients in their decision to grant us discretionary authority, without impeding our ability to manage each client's portfolio on a daily basis. We do note that NI 31-103 already specifies certain conflicts that require client consent.

As a firm, we are already operating under a requirement in our Code of Business Conduct and Ethics to put our client's interests ahead of our own. In addition, we are held to a statutory standard of care, to contractual standards of care in our client agreements and fund documents (which can be higher than our statutory standard), and may be held to a fiduciary standard at common law.

Questions 46 and 47 – Is the definition of "institutional client" appropriate for its proposed use in the Companion Policy? and *Could institutional clients be defined as, or be replaced by, the concept of non-individual permitted clients?*
We would not like to see the introduction of another definition of a type of sophisticated investor. There are already several definitions in use by various regulations, and another one would not benefit investors or registrants. We agree that the current definition of "permitted client" could be used in this instance. Furthermore, we do not see a need to restrict the definition to only non-individuals. There are individuals who clearly do not require a suitability assessment, including those individuals who make the decisions for institutional clients and other permitted clients, such as registered representatives of adviser firms and of investment dealer firms that are exempt from adviser registration.

Other Comments
We feel that the requirement to disclose "all outside business activities of the firm and applicable representatives" would not be useful to individual investors and is likely to cause confusion. Currently, the CSA collect a very broad array of outside business activity information from registrants. Many of these activities are unrelated to the registrant's client activity, and if likely to cause a conflict, would not be permitted by the firm or the CSA, or would require certain protocols to be put in place to manage the conflict. We suggest that removing this requirement, or disclosing only those activities that, in the judgement of the CCO, as likely to create a material conflict, would provide more meaningful disclosure to investors and potential investors.

Know Your Client
We support the documentation of the best practices around KYC as noted in the Proposals. In many cases, this is the codification of previous guidance and recommendations provided by the CSA. As noted below, we do have some concerns about the possibility of creating an expectations gap between ourselves and our clients through some of the changes that are suggested in the Proposals. Specifically, we think this could arise through the requirement to collect tax information and information about indebtedness. We would like to see explicit guidance that acknowledges clients who refuse to provide complete KYC information (such as net worth, tax and indebtedness information), and permits their acceptance of continued advisory services based on the information provided.

Question 4 – Do all registrants currently have the proficiency to understand their client's basic tax position? Would requiring collection of this information raise any issues or challenges for registrants or clients?
While we believe that most registrants at our firm currently have the proficiency to understand their clients' basic tax positions, there would be challenges in requiring the collection of tax information by registrants, not the least of which is clients' desire not to share this information. Also, as an investment adviser, we recommend that our clients obtain tax advice tailored specifically to their situation, just as our investment advice is tailored. Requiring the collection of tax information may increase clients' and the courts' expectation that we are also providing tax advice, or have optimized a client's personal tax situation. In our opinion, without an in-depth understanding of each client's tax position, the necessary ongoing education, and a specific client mandate to provide tax advice, this would be unreasonable to expect. This is particularly true of many of our high-net worth clients, who have a team of advisers, including tax, accounting and legal advisers, providing specific advice relevant to their area of expertise.

Question 6 – Should the KYC form also be signed by the representative's supervisor?
We do not believe that this is necessary for portfolio managers, nor are we clear on what the signature of the supervisor is supposed to represent. If the intent is to ensure that the form is correctly completed and that all appropriate information has been documented, the supervisor may be unwilling to do this verification not having been at the client meeting where the information was collected. We believe that supervisory policies and procedures should be specific to each registrant.

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Question 55 – To what extent should a representative be allowed to open a new client account or move forward with a securities transaction if he or she is missing some of all of the client's KYC information? Also, question 57.
We find, that many of our clients, who are generally high net worth, are reluctant or unwilling to provide information that they feel is private, such as personal indebtedness. In addition, many of our clients have approached us as a firm, because we have a particular area of expertise or approach to investing, and are not interested in a more broad financial planning discussion (which we believe is common in the portfolio manager space). These clients are often sophisticated, or have other financial advisers that provide this type of advice. In these cases, an attempt to suggest the client take other financial approaches, such as paying down debt, could come across as condescending, unwanted and inappropriate.

In this context, we feel that the KYC information requirements should only be carefully expanded to include information required to make investing decisions. If they are expanded as suggested in the Proposals, we would suggest that guidance be provided to registrants and firms as to how to document a client's refusal to provide certain information, and under what circumstances a registrant could continue to open an account, absent certain information. This would have to be principles-based guidance, as the nature of the information not provided and the nature and extent of the proposed investment/transaction will be very much fact-based and a decision as to whether there is sufficient information to assess suitability will be subjective.

Know Your Product – Representatives and Firms
We generally support the idea in the Proposals that representatives "have sufficient knowledge of a product, together with the KYC information about the client, to support a suitability analysis". That being said, our general comment on the KYP sections of the Proposals is that they are not feasible for our firm's business model, nor likely for portfolio managers in general. The fundamental issue with the Proposals as written is the focus on "products" and "product shelves". As a firm, we do not sell products, nor do we have a product shelf. We are selling our investment management services. While we do have proprietary pooled funds as part of our clients' holdings, these funds are used to implement specific investment strategies, which can also be provided through separately managed accounts. Pooled funds provide for investors of varying sizes to have access to investments and investment strategies to which they might not otherwise, but they are not themselves "products" that we are selling. We feel that this is a fundamental difference between discretionary portfolio managers such as Gluskin Sheff and other registrants.

We found it difficult to understand the distinction that is being made between proprietary and mixed/non-proprietary firms in the context of portfolio managers, and are concerned that the requirements that follow from this distinction could have significant negative impacts on portfolio managers, both in terms of additional costs and investor confusion.

Furthermore, we were unclear as to whether a distinction is being drawn between "products" and "securities". The Proposals seem to use the terms interchangeably.

We have attempted to highlight some specific examples of the challenges we see with the Proposals relating to KYP as they currently stand in our responses below.

Question 8 – The intended outcome of the requirement for mixed/non-proprietary firms to engage in a market investigation and product comparison is to ensure the range of products offered by firms that present themselves as offering more than proprietary products is representative of a broad range of products suitable for their client base. Do you agree or disagree with this intended outcome?
We agree with the intended outcome as it relates to firms that are providing a suite of "products". The outcome as described, since it focuses on products that are offered by firms primarily engaged in distribution, as opposed to the investment management services that we provide is, by its nature, not applicable to portfolio managers in the way it is to other registrants. However we agree that for firms that generate income both from portfolio management services and from fund and other product sales activities, the inherent conflicts of interest that the CSA have identified need to be addressed.

Question 9 – Do you think that requiring mixed/non-proprietary firms to select the products they offer in the manner described will contribute to this outcome?
We would assume, from a KYP point of view, that a firm such as Gluskin Sheff should put its focus on investigating and analyzing the securities and other investments that are held in its portfolios, and that individual representatives should understand the firm's investment strategies, the holdings in each model, the structure, features, costs and risks of each portfolio, whether held directly or through a pooled fund. These features and our firm's investment style should also be explained to the client at the inception of the client relationship. The Proposals, as written, require a process of "market investigation of a reasonable universe of products" for mixed/non-proprietary firms, and, given the methods we use to provide investment management services to our clients – a combination of pooled funds and separately managed accounts – it seems likely that a firm such as Gluskin Sheff would fall under this requirement as a mixed/non-proprietary firm. A prescriptive reading of the Proposals would seem to imply that our investable universe is every security globally. This would seem to make a market canvass of the type envisioned to be impractical, if not impossible, and it would be a large consumer of firm and industry resources. We would also question whether such a study would have any practical benefit.
Furthermore, this type of requirement is unlikely to benefit our clients, who are interested more in what we do for them, the fees we charge and the specific expertise we bring. As we don't have a list of products we are selling, the sort of canvass and disclosure contemplated would not be of benefit to portfolio management clients.

At minimum, we think the Proposals should clarify that offering discretionary managed accounts does not constitute non-proprietary activity, including when such account owns products like ETFs in incidental quantities alongside other portfolio investments.

Question 10 – Are there other policy approaches that might better achieve this outcome?
We feel that, for portfolio managers, an approach that focuses on the alignment of compensation models and fee structures to client interests could better represent the intent of the CSA without creating unnecessary and burdensome compliance obligations. For example, requiring an explanation by firms that have referral arrangements or who pay commissions to employees or others for the sale of pooled fund units as to how they deal with this conflict in the best interests of clients.

Question 11 – Will this requirement raise challenges for firms in general or for specific registration categories or business models?
As described above, we feel that the Proposals, as written, would pose significant challenges and costly compliance burdens without an offsetting improvement in client outcomes unless they are tailored to specific registration categories or business models. Again, a distinction needs to be made between firms whose principal business is portfolio management and firms that, although registered as portfolio managers, are also registered as dealers and that also sell third party funds (and are compensated for doing so). A firm whose principal business is portfolio management but that also accepts direct investment in a proprietary fund through its EMD registration (but does not sell third party funds) should not be subject to the proposed KYP obligations. For example, certain firms have a specific expertise that can be made available to non-managed account clients who seek only that expertise. Such a firm should not be obligated to assess other "comparable" funds before selling their own fund to interested investors. They would of course still be subject to KYC and suitability obligations.

Question 12 and 13 – Will this requirement cause any unintended consequences? For example, could this requirement result in firms offering fewer products? Could it result in firms offering more products? and *Could these requirements create incentives for firms to stop offering non-proprietary products so that they can fit the definition of proprietary firm?*
We think that this requirement could result in firms changing their offering in order to fit more clearly into the proprietary model to avoid the burdensome market investigation requirement, or to avoid the risk of selecting the "wrong" products as a result of the market investigation. If the requirement is extended proprietary firms, it could result in firms deciding to either manufacture investment solutions or distribute, but not both.

We think that other unintended consequences are also a possibility, for example, firms may push research companies to provide information about the available universe of products in a certain manner, in order to facilitate the outcome of the market investigation.

Question 15 – Do you think that categorizing product lists as either proprietary and mixed/non-proprietary is an optimal distinction amongst firm types? Should there be other characteristics that differentiate firms that should be identified or taken into account in the requirements relating to product list development?
As discussed above, we do not feel that this categorization is optimal. It doesn't take into account the myriad business models used by firms in the industry, nor does it address the needs of portfolio managers, who, by their nature, do not sell products, or necessarily have a product list. Our current business model at Gluskin Sheff relies on our investment team conducting rigorous research and analysis on investment opportunities throughout the world, the results of which are delivered either through pooled funds or separately managed accounts. Our client wealth management team assesses each client's needs and determines an appropriate asset mix, taking into account each client's unique circumstances, and based on their in-depth knowledge of the models and pools managed by our investment team. We are not selling a product, and a categorization of our firm as having one or another type of product shelf does not make sense in the portfolio manager context.

<u>Suitability</u>
As with most of the Proposals, we generally support the underlying motivation to ensure that a suitability analysis is fundamental to the management of clients' portfolios. However, with

some of the KYC limitations we have described above, and by virtue of the discretionary nature of the portfolio manager/client relationship, and the applicable standards of care that portfolio managers are subject to, we feel that several aspects of the specific guidance would not be appropriately applied to portfolio managers, as discussed below.

Question 16 – Do you agree with the requirement to consider other basic financial strategies?
The consideration of other basic financial strategies may be appropriate in certain circumstances, however, we do not feel this would be practical or welcome by clients in all cases. As noted above, many clients are unwilling to provide the "private" information that would be required by a portfolio manager in order to make such a recommendation. Furthermore, many clients are not interested in receiving such debt management or tax planning advice, for example, from a portfolio manager, nor would the requirement to do so be welcome.

Question 17 – Will there be challenges in complying with the requirement to ensure that a purchase, sale, hold or exchange of a product is the "most likely" to achieve the client's investment needs and objectives?
We believe that this is another example where the regulatory requirement may create an expectation gap with certain clients. We feel that the "most likely" requirement at both the asset allocation level and the security level is an unrealistic standard to meet. We also note that there is a statutory prohibition against giving, in connection with a trade, an undertaking relating to the future value of a security or derivative, and the typical client may not understand the distinction between these two concepts. The definition of all of the potential alternatives or proposed strategies, and the establishment of a system to assess the probability of each alternative meeting the client's investment needs and objectives would be daunting on its own. At the asset mix level this would require the consideration of an incredibly large number of alternatives, many of which could be likely to achieve the client's goals. At the security level, given the universe of alternatives, this would be a near impossible standard to meet.
Also, it should be noted that as discretionary managers, we are not generally receiving orders to purchase, sell or hold from our clients. We are making these determinations on a daily basis, in the client's best interests, subject to our fiduciary duty.

<u>Relationship Disclosure</u>
Aside from the non-applicability of the proprietary vs. mixed/non-proprietary classifications of different firms and the disclosure of product lists, we generally support clear, useful disclosure of the sort advocated in the Proposals. As noted above, we do have a concern relating to the requirement that registrants have a "reasonable basis for concluding that a client fully understands the implications and consequences for the client of the content being disclosed." We feel that this type of requirement may be unworkable, in that it appears to go beyond regulating registrants' activities and ventures into the territory of regulating client understanding. Very explicit guidance would be required for this type of requirement to be more than a documentation exercise. Portfolio managers, in addition, are already subject to a relatively higher standard of care, and are obligated to act in their clients' best interests, regardless of the disclosure provided to each client.

<u>Proficiency</u>
Question 28 – To what extent should the CSA explicitly heighten the proficiency requirements set out under Canadian securities legislation?

We are generally supportive of the idea of raising proficiency standards, particularly as it relates to the knowledge elements required for compliance with the Proposals. As portfolio managers, our individual registrants are generally held to a high standard of proficiency, having attained a CIM or CFA designation in most cases, and as such, the idea of ongoing education requirements may be a more appropriate method of enhancing proficiency for this category of registrant.

As a practical matter, the availability of relevant, cost-effective training programs targeted at portfolio managers and the subject matter advocated in the proposals is a concern at this time.

Question 29 – Should any heightening of the proficiency requirements for representatives be accompanied by a heightening of the proficiency requirements for CCOs and UDPs?
We support continuing education requirements for CCOs and UDPs, but question the need for heightened initial proficiency requirements in these individuals for portfolio managers. UDPs in particular, who are CEOs of their firms, are from a diverse set of backgrounds, and are generally not hired for their particular proficiency as a UDP. Establishing a single proficiency standard for this role would be difficult. However, recognizing the importance of the UDP aspect of a CEO's role, continuing education requirements would be appropriate. CCOs on the other hand, are hired specifically for their background and education relating to compliance, and it is reasonable to establish initial proficiency and ongoing continuing education requirements for this registration category. Again, however, the availability of relevant, cost-effective training programs targeted as such individuals is a concern at this time.

<u>Titles</u>
We agree in principle that a multiplicity of titles may cause confusion among clients, and the CSA has clearly set out in the Proposals that the status quo is not acceptable. Based on this, we believe that it is inappropriate to mandate a prescribed number of titles based on the product shelf of the registrant firm.

Question 30 – Will more strictly regulating titles raise any issues or challenges for registrants or clients?
When this was raised within the firm, many questions arose as to how titles should be used when not facing a client. Would each registrant potentially have two titles, and two sets of business cards/e-mail addresses based on their client-facing and non-client facing titles? In addition, for certain well defined titles, such as CEO, would the registrant still be required to use the prescribed title? For example, if our CEO was an Advising Representative, would he provide a client with a card that simply said "Advsior", or could he provide one that said CEO as well? If the "Advisor" card was the only one allowed, would he then keep a separate set of cards that said "CEO" for use with anyone who was not a client? Guidance on this aspect of the Proposals would be appreciated.

Question 31 – Do you prefer any of the proposed alternatives or do you have another suggestion, other than the status quo, to address the concern with client confusion around representatives' roles and responsibilities?
Of the alternatives presented, we would prefer that the category of registration be adopted. However, we also think that the use of "portfolio manager" for Advising Representatives in that category would also be appropriate. Furthermore, we feel that the first alternative presented, and any alternative based on a firm's categorization as proprietary or mixed/non-proprietary, is confusing and inappropriate.

Designations
We believe that the Proposals in the area of designations are appropriate and serve to avoid the use of misleading or deceiving designations.

Role of UDP and CCO
We believe that the Proposals in the area of the role of the CCO and UDP are generally appropriate to clarify these roles.

Statutory Fiduciary Duty when Client Grants Discretionary Authority
We agree that the harmonization of the statutory standard of care across Canada for discretionary portfolio managers, whether labelled as a "fiduciary standard" or otherwise, would be of benefit to portfolio managers and investors alike as it would create more certainty.

Comments on a regulatory best interest standard for discretionary portfolio managers
Portfolio managers with discretionary authority are already subject to a higher duty of care, whether at common law or imposed contractually. We believe that the introduction of a regulatory best interest standard for all registrants would be confusing to both investors and registrants and may be inappropriate in many instances, as the duty of care needs to be reflective of the nature of the relationship. Furthermore, unless the standard could be implemented across all Canadian jurisdictions, the introduction of this standard in some jurisdictions could result in an uneven playing field where some investors are afforded protections that other Canadians are not. This would only increase the expectation gap that the CSA is seeking to address, and could result in regulatory arbitrage.

We would like to thank the CSA for the amount of effort that has clearly gone into the creation of these Proposals, and for the opportunity to comment on them. If you have any questions about our comment letter, please feel free to contact the undersigned.

Sincerely,
Gluskin Sheff + Associates Inc.

Amy Aubin, CCO
Tom MacMillan, President & CEO