



**NATIONAL
BANK**

**CORRESPONDENT
NETWORK**

Via Email

September 30, 2016

Alberta Securities Commission
Autorité des marchés financiers
British Columbia Securities Commission
Financial and Consumer Services Commission (New Brunswick)
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Nova Scotia Securities Commission

Attention: Robert Blair, Secretary (Acting)
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, Ontario M5H 3S8
comments@osc.gov.on.ca

Dear Sir:

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

National Bank Correspondent Network (NBCN) appreciates the opportunity to provide comments on the Canadian Securities Administrators' ("CSA") Consultation Paper 33-404 – Proposals To Enhance the Obligations of Advisers, Dealers, and Representatives Toward Their Clients (the "Consultation Paper").

NBCN is a wholly-owned subsidiary of the National Bank of Canada and provides carrying broker and custodial services to some 70 IIROC members and over 350 Portfolio Managers. We act solely in the above-mentioned capacity with no responsibility for suitability or related obligations.

Specific concerns or suggestions that we have made related to the questions posed in the Consultation Paper are contained in the "National Bank of Canada Wealth Management's and National Bank Financials Position on the CSA's Consultation Paper 33-404 entitled Proposals to Enhance the Obligations of Advisers, Dealers and Representatives Towards Their Clients" and we have reviewed, provided input to and fully support the response being made by the Investment Industry Association of Canada ("IIAC").

This response addresses some issues that are specific to NBCN in its role as carrying broker and more generally to the impact we see to our clients, independent investment advisory firms registered either as Advisers (Portfolio Managers or Investment Fund Managers) or Investment Dealers and ultimately to their clients, the end investor.

In summary, NBCN agrees with the objective of enhancing the investor experience, improving clients' achievement of their intended outcomes and generally better aligning client and adviser goals. We appreciate the effort that the CSA has made in building the Consultation Paper and its commitment to the ongoing consultation process through town halls and other opportunities to what is a very complex challenge.

At NBCN we are committed to supporting the independent firm, our business model is focused exclusively on this space and we believe that both advice and independent thought are critical to achieving positive client outcomes in a complex environment. Further we believe that in order to provide this independent thought, independent firms need to be healthy, vibrant and focused on finding the best solutions for their clients. We are concerned that the Consultation Paper, while attempting to achieve such an outcome for the client, proposes oversight and procedures that will be unmanageable for many, if not most, independent firms; will require significant resources being devoted to process rather than investment advice; and ultimately may result in a client experience that is less ideal than the current state.

In our response we have tried to make suggestions that may assist in achieving the desired outcomes and welcome the opportunity to be involved in the continuing consultation process.

Proposed Regulatory Best Interest Standard

One of the challenges in implementing change on the scale contemplated by the Consultation Paper is that the proposals attempt to cover a wide range of registrants with a common solution. For the registrants that NBCN services, we see that IIROC members already have regulation that effectively provides for actions being in the best interest of the client and similarly Portfolio Managers already have a fiduciary duty. While we support extending this standard to all registrants (and we believe only registrants should be permitted to provide advice on either a discretionary or non-discretionary basis) we would recommend employing legislation that is already in effect and has been shown to be workable in the current environment. A solution using IIROC rules for non-discretionary and the fiduciary standard as set out in Alberta legislation for discretionary relationships might be an option.

We are also concerned that clients may not fully understand the differences between a Regulatory Best Interest Standard, a Statutory Fiduciary Duty and a legal fiduciary obligation and that multiple definitions or legislation may be applied to one relationship depending on jurisdiction. This may well result in client confusion and an unintended negative client experience.

There are circumstances where a non-discretionary account is allowed to operate on a discretionary basis for a period of time. We would recommend that existing IIROC rules be applied to these situations and not a fiduciary standard.

As it relates to NBCN, and perhaps by extension to other registrants who are exempt from client suitability, it will be important to recognize that such entities are driven more by what is administratively practicable on a particular platform rather than what may or may not be suitable for a particular client. As such we would expect that any registrant that does not have suitability obligations be exempted from the requirements of the Best Interest Standard.

Targeted Reforms

Conflicts of Interest

Under current IROC rules and when combined with CRM requirements, enhanced disclosure and steps to address conflicts of interest are significant and, we believe adequate.

For portfolio managers, as most potential conflicts seem to arise from the compensation model and portfolio managers have a compensation model that is driven from assets under management rather than from level of sales, we see the proposals, if they were to be applied to Portfolio Managers, as rather a solution in search of a problem.

We do agree that all registrants, IROC, MFDA, EMD or other should be held to the same standard and would therefore suggest relying on the IROC rules that are already in place combined with the CRM changes that have more recently been imposed.

For carrying brokers who are affiliated with full-service entities such as ourselves, there may be technical conflicts of interest created as a result of our affiliate entities that have no bearing on the client who is being advised by an independent investment professional (either IROC or portfolio manager). Disclosure of carrying broker conflicts created by its affiliates would create confusion on the part of the client and should be excluded from the requirement.

Know Your Client

Recognizing that the Consultation Paper acknowledges that KYC obligations should not apply to order-execution only service providers and assuming that this extends to carrying brokers then we see no direct implications to NBCN.

However, we are concerned that the likely costs that will result from the requirement to refresh the KYC for every client every 12 months will generate undesired outcomes. It has been our observation that when CRM 1 was implemented which required additional suitability reviews for accounts when either securities or funds were transferred in or out some of our client firms, due to the increased costs associated with these reviews, either started to enforce minimum size of assets for clients on their book or began to impose a small account maintenance fee. Both of these steps resulted in smaller investors, who have fewer options when seeking to obtain advice, either being forced into alternative solutions that they may not have considered suitable or paying more for essentially the same service. We are concerned that the same impact on a larger scale may be seen if such a proposal concerning KYC is enacted.

Another possible unintended consequence of the proposals is the degradation of service. Many clients seek out advisers for their expertise in a certain area. Asking advisers to consider tax impacts when a client may already have their own tax advice is counterproductive and creates a cost for registrants against which many clients will not see a corresponding value. This will force advisers to spend time in

areas that do not benefit the end client and, ceteris paribus, will, among other things, result in less time being spent researching potential investment opportunities for the client.

We do fully support that where advisers hold themselves out as providing tax-efficient investment solutions that they understand sufficiently the requirements needed and obtain the information required from clients to provide that service. We do not believe that all registrants should be forced to provide such a service as this will result in a homogenized offering that can never be tailored to the true needs of the client and will therefore almost certainly result in intended outcomes not being met.

There are other areas of the proposal as it relates to KYC that raise concerns but we believe that they are fully covered in the IIAC and NBCWM responses.

Know Your Product (“KYP”)

While there appears to be specific exclusion from KYC and Suitability responsibilities for order-execution service providers the same does not appear to be true for KYP. Whether this is an oversight or not we are not sure however, if, as a carrying broker we are required to have full KYP obligations this would be unworkable. Carrying brokers do not deal directly with end clients (unless in exceptional circumstances where liquidating transaction only are permitted) and accordingly there is no way for us to determine whether or not the products that we administer on behalf of introducing brokers or portfolio managers are suitable for the needs of the end client. We would recommend that carrying brokers be excluded from this requirement.

The NBCWM response addressed the concerns and potential adverse consequences with advisers being required to be familiar with a very broad range of products and how it could dilute their knowledge and value in their area of specialization. We concur with this position and would add that we see this as an even larger concern for portfolio managers. Portfolio managers very often specialize in certain areas (large cap Canadian equity, small cap US growth etc.) and their clients who tend to be wealthier, sophisticated investors with advisers outside of the portfolio manager seek out their expertise in these areas in building their own overall investment strategy. Requiring such a portfolio manager to become familiar with other investment options would negatively impact their expertise in their chosen area of differentiation. We believe that this would negatively impact both the investor and the adviser and would not achieve the intent of the Consultation Paper.

We fully support the position that any adviser should be fully conversant in any products or services that it purports to offer. Going beyond this adds cost without benefit.

Suitability

Similarly to the Know Your Client requirement set out in the Consultation Paper it appears that order execution only service providers would be exempt from suitability requirements. NBCN agrees with this proposal assuming that this exclusion extends to carrying brokers who operate under a suitability exemption with IIROC.

We also agree that advisers, whether they be IIROC registrants, portfolio managers or any other type of registrant need to ensure that the services they provide and the products they use to meet client objectives are suitable for that purpose. It would however be optimistic to suppose that an adviser could force a client or potential client to provide information against their will and also to assume that

an adviser, even if they had all the pertinent client information available, could have sufficient breadth of knowledge to make even a basic assessment as to the overall suitability of a position inside a client account related to that client's overall financial position. This challenge would be made even greater where the client is wealthy and has a complex situation and structure. The objective set out in the Consultation Paper while noble in intent is likely to prove unworkable in a real-world context.

There are also circumstances where a client may wish to make a purchase that is not recommended by an adviser. Today this is possible so long as it is appropriately documented. This may be more difficult to support under the proposed legislation which would result in investor expectations not being met.

We would recommend consultations with the industry to work through some real-life examples to set a reasonable target of suitability to be applied depending upon the services and products on offer by the adviser and their firm.

Relationship Disclosure

While IROC registrants already have significant and well-documented obligations for relationship disclosure this may not be true for all registrants and we fully support a level playing field where all investment solution providers are required to clearly set out the terms of the client-adviser relationship.

We are concerned with the proposed *General Disclosure Guidance* under Appendix F on this matter which states that registrants "should have a reasonable basis for concluding that a client fully understands the implications and consequences for the client of the content being disclosed." Advisors would have the onus to prove that the client understood the disclosure which will never be met if the client pleads that they did not understand the disclosure, whether it was the case or not. It has been suggested that even if the client signs a document that says they understand the disclosure this may not be sufficient which would essentially give the client a way to never be responsible for any investment decision. Registrants should not be expected to take on this level of responsibility.

Proficiency

As noted in earlier sections of the NBCN response certain of the provisions within the Consultation Paper suggest a one-size-fits-all approach to regulating the industry and the proficiency proposals are one of those areas. If there are to be different categories of registration that allow for different services and if investment advisory firms are to be able to provide services that are tailored to certain types of investor, then advocating one standard of proficiency across all registrants must create inefficiencies. In providing services to independent investment professionals we see very clearly the different offerings these firms provide, to apply this Proficiency standard would be to homogenize the offering which would not achieve better investor satisfaction.

With one standard, either the bar is set too low in certain areas, and the adviser does not have enough in-depth knowledge in areas that requires specialization such as derivatives, or the bar is set too high and no adviser can reasonably meet the expectations and as a result is constantly at risk.

It is our position that advisers should be sufficiently proficient to provide the services that they purport to offer and, much like the KYP scenario, should have the requisite knowledge to deliver those services. To attempt to set one standard which will meet all circumstances in a very complex business would be optimistic.

We would presume that as a suitability exempt carrying broker we would be exempt from proficiency requirements other than for those registered individuals that must be able to take liquidating orders from clients of firms who have ceased to be registered. Such individuals would need only a basic knowledge as set out by IIROC today. If this is not the intent of the Consultation Paper we would have concerns with being able to meet a heightened obligation.

Titles & Designations

Our position is well represented in the NBCWM response. We agree with the intent in principle although we do not agree with the proposed solutions.

For example, there are many portfolio managers who choose to provide a solution through private pooled funds. While these are proprietary products they are simply a vehicle for making the investing process more efficient and do not have associated compensation. Invariably the underlying securities are listed equities or widely traded debt and in some instances private securities or mortgages but to title the registrant as a Securities Salesperson instead of a Portfolio Manager would be misleading.

There are numerous other examples where there would be similar results but we do support the initiative and believe that a workable solution can be found through consultation with the industry.

Statutory Fiduciary Duty for Discretionary Accounts

We agree that there should be a common standard of care for all managed accounts whether they be managed by IIROC registrants who are qualified portfolio managers or by portfolio managers outside an IIROC registered entity. To introduce a Statutory Fiduciary Duty when portfolio managers are already fiduciaries will create confusion in the investing public. To the extent the public are even aware that there is a difference between Best Interests, Statutory Fiduciary Duty and acting as a fiduciary under common law it is unlikely that they will understand the differences and this will result in greater expectation gaps than may currently exist.

There are specific situations where accommodations will be required such as temporary discretionary accounts under IIROC however these are well-addressed in the NBCWM and IIAC submissions.

Conclusion

NBCN supports the ongoing improvements of client-advisor relationships within the investment industry and believes that the better the understanding of each parties responsibilities by the other the better the experience for the client and for the adviser.

Critical to the experience for the client is a healthy investment industry and a healthy investment industry needs healthy independent investment firms. The past decade has been a struggle for many independent investment firms and for independent IIROC members especially. Such firms are, we believe, critical to the process of capital formation in Canada as these are the companies that support the small ventures that initially become public companies and fuel growth and innovation. Without them and without independent thought and ideas clients and investors will suffer.

Ongoing regulatory reform is a necessity. The investment industry is ever-evolving and regulation has to change as well however this cannot occur in a vacuum and changes to regulation have ripple effects that require careful consideration, co-operation and consultation. We are reassured that the CSA is

committed to a careful consultation process as to implement such significant change without consideration of costs versus benefits and other impacts may ultimately be detrimental not only to the client but also to capital markets overall.

NBCN looks forward to being involved in the process going forward and we appreciate having the opportunity to submit our position on this paper.

Sincerely,



Patrick Primerano
President, NBCN Inc.



David Tasker
Chief Operating Officer, NBCN Inc.