

September 29, 2016

Alberta Securities Commission
Autorite des marches 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

Attn: Josee Turcotte, Secretary
Ontario Securities Commission
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RE: CSA Consultation Paper 33-404 (“the Consultation Paper”) – *Proposals to Enhance the Obligations of Advisers, Dealers, and Representatives Toward Their Clients*

Thank you for the opportunity to participate in the consultative process. I am pleased to provide my comments on the proposals contained in the Consultation Paper.

As a consultant, I help registrants implement regulations and manage their compliance risk by incorporating their compliance obligations into their business operations and processes.

The comments below reflect my personal views and draw on over 25 years of relevant industry experience. This experience includes roles in audit and operations within the financial services industry. A 12 month role as a Senior Accountant with the Compliance and Registrant Regulation Branch of the Ontario Securities Commission “OSC” rounds out this experience.

With respect to the Consultation Paper, I have had the opportunity to hear directly from stakeholders in a variety of forums. These include industry seminars and roundtable discussions and also the 2013 CSA panel discussion. From these discussions, it's clear that to achieve the compliance outcomes you desire, regulations need to be relevant, clear, practical and easy to implement. In addition, attention should also be given to implementation matters. The CSA has emphasized that "the status quo must change"; this implies that you would like to move quickly with rule drafting following the consultative process. The proposed targeted reforms and Best Interest Standard introduce new concepts and will require registrants to elevate their proficiency levels and standard of conduct, if implemented. They need to be ready. It is equally important for CSA staff to be fully prepared when the new rules come into effect. As such, I would encourage the CSA to consider the implementation issues as you move forward with drafting the new rules and to also consider adopting a reasonable transition timeline, particularly as there may be wide gaps between what is current state versus what you hope to become the target state.

General Comments

I would like to preface my answers to the specific questions with some general comments.

1. *Tailoring explicit rules.* The proposed targeted reforms contained in Part 7 of the Consultation Paper makes explicit the proposed *minimum standards* that registrants will be required to follow. I will state my preference for principles-based regulations (supplemented with detailed guidance) that allows registrants to tailor their approach to the size of their organizations and business model. The proposals adopt a more prescriptive approach and thus, you have recognized that specific rules are needed to account for the diversity of business models within registrant categories. You have asked registrants to provide input in areas where explicit rules need to be tailored to a particular business model. I would encourage the CSA to consider holding in-depth roundtable discussions by industry segment to develop workable solutions as you move forward with your consultative process.
2. *Simplicity.* All Registrants would benefit from a consistent and harmonized set of regulations across all jurisdictions. As such, harmonization is encouraged as you move forward with rule drafting.
3. *Clarity and certainty.* The proposed targeted reforms incorporate some common practices that are described in Staff Notices. For these proposals, the rules and guidance are clear. However, the Consultation Paper also introduces new concepts. Greater clarity around new concepts is requested to help registrants prepare to meet their additional compliance obligations. In addition, further discussion and guidance is needed in these areas for implementation. More specifically, there is uncertainty as to where CSA staff will establish the "goal posts". For example, new concepts appear in the following sections:
 - *Know your client "KYC" – "Basic tax position".* See Part 7 of the Consultation Paper amending s 13.2 of NI 31-103 dealing with KYC, and Appendix B. There is little guidance as to what constitutes "basic tax position". Additional clarity is needed as a registrant's KYC obligations will potentially form a new baseline for proficiency. Also see response to Question 28 under *Proficiency* below.

- *Know your product* – See Part 7 of the Consultation Paper; amendments to Part 13 of NI 31-103, and Appendix D. What constitutes a sufficiently “broad range of products” when designing a firm’s product list? And what would the CSA consider to be a range of products that is “appropriately representative of the products most likely to meet the needs and objectives of its clients? During a field review, how will CSA staff form a view as to whether the product list is sufficiently broad?
- *Product selection suitability* – See Part 7 of the Consultation Paper; amendments to s 13.3 of NI 31-103 on suitability, and Appendix E. During a field review, how will CSA staff form a view as to whether a representative’s recommendation or the transaction is one that is “**most likely**” to achieve the client’s investment needs and objectives, given the client’s financial circumstances and risk profile....on the firm’s product list”?

Registrants will require more clarity on these concepts if they are to meet the minimum requirements that are explicitly described in Part 7 of the Consultation Paper.

4. *Practical*. Some of the proposals in its current form may not be practical to implement given the current environment. For example, certain of the proposed targeted reforms dealing with *Know Your Product* and *Proficiency* assume that the information or training that is necessary to move forward with the proposals exist or can be obtained at a reasonable cost. Certain registrant groups will advise that is not the case.
5. *Implementation*. The CSA has emphasized that “the status quo must change”. I understand the reasons for your proposals and your desire to move quickly to address the gaps identified and summarized in the Consultation Paper. Putting aside the merits for or against the proposals, there are other factors that are worthy of consideration from the perspective of setting implementation timelines:
 - *Registrants’ capacity for change*. I will convey that many registrants (large and small) feel overwhelmed by new requirements from many regulatory bodies i.e., securities regulators, FINTRAC, CRA etc. Smaller registrants in particular don’t always have the bandwidth to actively engage in the consultation process. As such, their voices and challenges won’t always be heard. If implemented, some of these proposals will require significant systems development efforts as well as re-training of registered reps given heightened proficiency requirements, new concepts and business processes. Clients will also need to be informed and re-educated on new concepts and terminology. The effort is expected to be significant. Accordingly, when setting implementation timelines, I would encourage the CSA to also take into account the registrants’ capacity for change given other ongoing compliance initiatives. Let’s set everyone up for success. Registrants, regulators and in the end investors would all benefit from a reasonable implementation timeline.
 - *Clarity and consistency in CSA policy oversight/enforcement*. A question to be addressed is: where will the CSA set the “goal posts” for certain new concepts? More clarity is needed to understand how CSA Staff will apply new concepts so that registrants can better prepare for implementation and meet their obligations *when the rules take effect*. Respectfully, I would suggest that CSA staff might also benefit from this exercise and move forward with confidence that registrants have a common understanding and that new concepts will be consistently applied across self-regulatory organizations, CSA

teams and jurisdictions. It is important for all parties to be aligned and fully prepared once the new regulations come into effect.

For these reasons I would encourage you to seek industry input on a reasonable implementation and transition timeline. The timeline would take into account the significant efforts that may be required, for example,

- Availability of market information on competing products for product due diligence
- Systems development and business process changes
- Heightening registrant proficiency requirements and the development of course curriculum and exams
- Registrant and CSA Staff training
- Client and investor communications around title changes, conflicts of interest, new concepts e.g. risk profile etc.

I would also add that some initiatives require a longer lead time since it isn't feasible to start implementation until the rules are finalized.

6. *Financial Literacy*. I make the observation that Part 5 of the Consultation Paper lists five key investor protection concerns that are driving these proposals. The issue of information asymmetry, more specifically investor financial literacy, needs to be highlighted for further discussion. I have concerns that the proposed targeted reforms and the new Best Interest Standard won't fully address your concerns and achieve the outcomes you hope to attain until we collectively make improving financial literacy a priority in Canada. I will leave it to the CSA jurisdictions, legal profession and others to debate the merits of elevating the standard of conduct to a Best Interest Standard and whether it will improve the investor outcomes stated in the Consultation Paper. What I will say is I believe that basic financial literacy is a life skill and as such, it should be incorporated into the core curriculum in the education system. Indeed, even some of the CSA's proposals require registrants to have reasonable assurance that their clients understand the disclosures being made to them. Financial advisers have a role to play in educating their clients. It's in their interest to have clients who are well-informed and engaged. However, shifting the burden of investor financial literacy onto the shoulders of registrants is, in my view, a costly way of addressing a matter of public interest. The cost of conducting business will ultimately be borne by all investors. There is also a risk that these reforms could result in a reduction of registrants, product choice and potentially channel certain investor segments towards business models that provide less advice. Individuals who may not have, or who may eventually lose, the capacity to understand financial matters require protection. This at risk group can be identified through a robust KYC process and registrants will need to take extra measures to meet their obligations to this investor group. As for the general population, we need to take steps to improve financial literacy and to close the gap in information asymmetry, not encourage it. It's in everyone's interest.

Answers to specific questions in the Consultation Paper

My response to specific questions in the Consultation Paper are set out below. I have identified some of the areas requiring more clarity or where there may be practical or implementation issues for your consideration.

Know Your Client “KYC”

General Comment

I believe it is important to have a robust KYC process. In my view, a registrant must collect the information that is required to meet their regulatory obligations and that which is needed to fulfill their mandate, or deliver service or sell a product or a solution. Registrants will tell you they may seek additional client information in order to identify areas where they believe they can add value or where there is an opportunity to eventually expand their mandate. This process can occur over time. One of the challenges lies in how to document this process. Advising and dealing representatives in different registrant categories have different roles. If you move forward with establishing a minimum standard for KYC information, then it will need to be relevant to a range of roles and business models and also recognize that client relationships develop over time.

Questions 4

Requiring registrants to collect information to establish a client’s “basic tax position” implies that you envision registrants to have some understanding of their client’s tax affairs and tax needs and to apply these concepts in assessing suitability. Registrants who are in tune with their client’s needs but who don’t have tax expertise may refer clients to others who can provide that advice. Under the current proposals, if a registrant does not have this proficiency, does this mean they must now work with professional tax advisors?

I would ask the CSA to provide guidance on what information you require a registrant to obtain in order to establish a client’s “basic tax position”. I would also add that it may prove challenging to require registrants to collect this information. Registrants will tell you that new clients may not be forthcoming with this information when an account is opened, or they may assert their right to privacy. In addition, clients may have to refer the registrant to their accountant who provides them with tax advice. That said, a registrant should obtain sufficient information to assess the suitability of the product, solution or service.

Question 54

The proposed targeted reforms require both the client and representative to sign the KYC form and a new client risk profile. Having both parties sign the KYC form makes sense, recognizing that the information on the form is part of a larger process.

The guidance contained in Appendix B appears to suggest that the client risk profile is an “output” that is created by the firm and the representative using information provided by the client during the KYC process (“based on concepts including risk attitude, risk capacity and loss aversion”). Do the new requirements allow an advising representative the ability to exercise professional judgment? Given the foregoing, what comfort will you as a regulator take from a client’s signature on the risk profile as you propose in Part 7? Does the client’s signature mean that he/she understands and concurs with the risk profile prepared by the firm and representative, which implies that the client understands the process behind the results? Or is it simply an acknowledgement that the resulting risk profile was discussed with the client? Finally, with regards to “risk profile”, is it your expectation that there will be some consistency in how the risk profile results will be applied across the industry, for example, in determining what types of products to recommend or strategies to follow?

Question 5

As mentioned in my opening comments, compliance obligations are often incorporated into business operations and processes. As such, firms may design KYC forms or new account documents in a manner

that fits how they conduct business and how they engage with the client. In addition, the information collected on new account forms is not used solely to meet a registrant's obligations under securities law. Registrants also need to incorporate the requirements for CRA reporting as well as those required under the Anti-Money Laundering and Terrorist Financing requirements. Any mandated KYC form will need to account for these matters as well as the range of services that a registrant firm provides. Finally, a robust KYC process does not end with an account opening form.

Know Your Product

Question 7

There may be practical difficulties with proposals 1) and 2) on their own and also when taken in conjunction with the expanded suitability requirement to recommend a product that is suitable and one that will **most likely** achieve the client's financial objectives. Registrants will tell you that where the firm offers a very broad selection of securities, there will be time constraints to educate reps of all products that are on the list. One result is potentially a much reduced product list. In addition, certain reps may only have the expertise to sell a limited type of product that are on their firm's product list.

Question 8

More guidance is needed from the CSA as to what constitutes a "broad range of products" for mixed/non-proprietary firms.

Question 11

You are making an assumption that market information is available at a reasonable cost that would allow registrants to do a market investigation of products that they are licensed and qualified to sell or advise on. Certain groups of registrants will tell you that the universe of competing products may not be known or may be cost prohibitive to obtain or, that this information is not always available.

Suitability

Question 16

Regarding the requirement to consider "other basic financial strategies", please clarify where CSA staff will set the "goal post". It would appear that you assume clients expect their registrants to play some role in financial planning and that clients are willing to provide registrants with information around all their financial affairs when they enter the relationship or open an account (see also proposed targeted reforms under KYC). I believe it's important to consider both the client's and the registrant's perspectives in the relationship.

Clients may have relationships with more than one registrant and/or they may have established relationships with other professional advisers. These relationships take time to develop. It's the client's decision to choose whether they want financial planning advice from their registrant, which registrant will provide that advice (in the case where there are multiple registrants) or to seek advice elsewhere. However, by making this requirement explicit and thus requiring all registrants to expand the scope of the suitability test without regard for what the client is looking for in the relationship will add cost with little perceived benefit to the client, particularly at the onset of a relationship.

By contrast, as the relationship progresses, a registrant may want to gather more information to determine where they can provide value or in order to expand the services for the client. A registrant is

in the best position to gauge how to add value to the relationship and more importantly, when and whether to pursue a larger mandate with a client.

In this context, prescriptive rules (i.e., minimum standards) requiring the expanded collection of KYC information at account opening and an expanded suitability assessment that may not impact the type of service provided or product recommendation is not optimal, in my view.

Relationship Disclosure

Question 27

Appendix F requires firms with a mixed/non-proprietary list to disclose the proportion of proprietary products they offer. Please clarify whether this information is a percentage and at what point in time it must be provided.

Proficiency

Question 28

I'm in favor of the CSA working collaboratively with registrants and other stakeholders to establish the core proficiency requirements and to specify the standards and the core knowledge a registrant needs in order to be proficient in their role and to fulfill their regulatory obligations to their clients. I would concur that proficiency standards need to be set in relation to the knowledge elements that are required to fulfill their regulatory obligations. I would encourage the CSA to have an active and continuous involvement in this process and to consider the following implementation matters:

- Who will set the core curriculum and exams needed to achieve the desired outcome?
- Who should be involved in the development, review and update of the course materials to ensure that it covers the core knowledge needed to meet the required proficiency standards and that the curriculum remains relevant to the changing marketplace?
- Which organizations are qualified to deliver the course materials and exams?
- What is a reasonable transition timeline to enable registrants to migrate to the new requirements?
- Do you expect registrants to have a minimum number of continuing education hours a year; and what courses or seminars would qualify for continuing education accreditation?
- Who will have continuing oversight responsibility to ensure that all objectives and conditions of the education program(s) are met?

In addition, I make the observation that tax proficiency is not explicitly listed in the Consultation Paper. Under the proposed KYC provisions, you require registrants to have an understanding of their client's basic tax position, however you make no specific mention of tax proficiency in Part 7 of the Consultation Paper. It's not clear whether this omission was deliberate or an oversight on the part of the CSA. If you move forward with the proposed targeted reforms to require the collection of information to establish a client's basic tax position, then I would recommend that tax proficiency be added to the core curriculum and that you work with industry participants to

- Define what tax concepts you expect registrants to have and to apply in order to meet the proficiency requirements
- Add it to the core proficiency requirements for registrants
- Identify which parties or organizations are capable of delivering this part of the course curriculum

Titles

Question 30

Registrants will advise that this topic is highly sensitive. This change will require tactful handling given the client-facing impact. I would like to add that restricting titles in and of itself is insufficient, in my view. Investor education on the distinctions between registration categories and what services or products a registrant is licensed to provide or sell is also needed in order to address the issue of confusion that was identified in Part 4 of the Consultation Paper.

Thank you again for the opportunity to participate in the consultative process. I look forward to attending the upcoming roundtable discussion in December. I would be pleased to answer your questions relating to the contents of this letter.

Yours truly,

[Signed: Merici Young]

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