OSC Investor Advisory Panel
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Re: Response to IIROC White Paper: The Public Policy Implications of Changes to Rules Regarding Proficiency Upgrade Requirements and Directed Commissions on the IIROC Platform

The Investor Advisory Panel ("IAP" or "Panel") is an independent body formed by the Ontario Securities Commission in August 2010. It is charged with providing input on the Commission's policy initiatives, including proposed rules and policies, the annual Statement of Priorities, concept papers and specific issues. Its mandate is to represent the views of investors and make recommendations to the Commission on matters affecting investors.

We are pleased to provide our perspective in response to IIROC's white paper, the purpose of which is to seek comment on an illustrative proposal that would allow firms and individuals to conduct, under IIROC's regulatory oversight, a business that is limited to mutual funds and exchange-traded funds. Under this approach, IIROC would:

1. Eliminate its current requirement for firms and individuals to be qualified to offer a full range of investment products, and instead allow firms and individuals to offer only mutual funds and exchange-traded funds (with appropriate adjustments for the relative risk of such firms and individuals to IIROC's proficiency, supervisory and oversight requirements); and

2. Allow all firms and individuals under IIROC's regulatory oversight to take advantage of what is referred to as "directed commissions".

IIROC is seeking comment on the white paper and has asked respondents to give their views on whether or not this illustrative proposal is in the public interest and how it could impact investors, as well as firms, registrants, and the overall Canadian regulatory and financial industry structure.

Panel's Response

To answer IIROC's question in as direct a manner as possible: we do not support the approach outlined in the white paper as being in the public interest.

In an earlier submission responding to IIROC Request for Comments on Strategic Issues, we expressly stated that IIROC must raise its standards in order to foster a culture of investment professionalism that puts the needs of investors ahead of those of the industry. This has not yet happened – and until IIROC takes concrete and meaningful steps in this direction, we see no reason to expand its mandate. We reiterate our comments submitted to IIROC at the end of this submission.

In response to the specific illustrative proposals outlined in the white paper, we have concerns in a few key areas:

Wrong time, wrong way – The Panel believes that the timing of IIROC's illustrative proposal is poor. Regulators are working at capacity towards the development and implementation of a common market regulator. This could divert the energy and resources of both SROs and potentially distract from regulatory business. The work required to make the changes suggested in this white paper would come at a time when there are already significant regulatory changes afoot, including the creation of a single national regulator.

At the same time, the Panel would question whether or not IIROC and the MFDA have adequate capacity to undertake such an initiative without increased chances of mistakes, errors, and missed deadlines in the delivery of its core mandate. The Panel finds it difficult to see how the environment outlined in the white paper addresses any serious concerns from the standpoint of either the industry or investors. Hence, the time and costs involved in moving this forward would be significant and, in our view, not in the public interest.

At the same time, this initiative sets up the very real possibility of a turf war between IIROC and the MFDA – a very unwelcome distraction from the business of investor protection.

Perhaps more importantly, this illustrative proposal from IIROC is not the way to create significant changes to the regulatory structure. Rather, as the Expert Panel on Securities Regulation recommends, changes in the regulatory landscape require a broader and comprehensive approach that considers all levels. IIROC and the MFDA are one part of the bigger picture.

Investor protection challenges – IIROC outlines a number of positive and negative implications for investor protection stemming from its white paper: *reduced industry competition; potential confusion as to which products and services can be offered by a mutual fund restricted dealing representative; risk of mutual fund restricted dealing representatives selling products for which they are not registered; transition issues; potential for increased costs; loss of aggregated CIPF and MFDA IPC coverage if mutual fund restricted dealing representative moves to the IIROC platform (i.e. if a client has an account with an MFDA firm and a separate account with an IIROC firm, the client has the benefit of both CIPF and MFDA IPC coverage).*

Worryingly, IIROC does not go as far as to describe how it would address emerging investor protection issues – a missing piece given IIROC's mandate to protect investors. These issues should be addressed.

Added costs for investors – In addition to the concerns noted above, the Panel is deeply concerned about the potential impact of dealers choosing to leave the MFDA. A smaller number of MFDA registrants could drive up costs for all MFDA dealers –those costs would likely be flowed down to mutual fund investors. This outcome is not in the interests of investors.

Directed sales commissions – The Panel is critical of sales commissions being directed to personal corporations, a practice IIROC currently prohibits. The entry of MFDA registrants could undermine this prohibition. Such a corporation could break the chain of accountability and give rise to creditor proofing, making it even harder to collect fines imposed on individuals.

Stock brokers as executors/trustees – In a separate consultation, IIROC proposes a situation where stock brokers are permitted to act as executors and trustees while the MFDA prohibits the practice. Would IIROC fund dealer salespersons be permitted to act as executors in the environment outlined by the paper? The Panel fails to see how this would benefit investors – and we have vigorously opposed this in the past.

Looking Ahead - Proposed Focus Areas for IIROC

The Panel believes IIROC's time and efforts would be far better focused in areas that would directly benefit investors and strengthen investor protection. To that end, the Panel would like to reiterate some of our recommendations for IIROC to step up its game during 2015:

> **Modernize and raise proficiency standards** - As the industry moves away from a transactional sales business model to focus on wealth management advice, its regulator must address badly outmoded professional standards. Titles must be properly regulated, reflecting advisors' training and scope of business practice. Educational and training standards must be raised. IIROC should launch a comprehensive review to update and modernize registrant retail proficiency requirements, which have been in place since the early 1970s.
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> **Regulate use of titles** - Investors need better protection than a standard that permits registrants to choose their own business titles based on meeting minimal standards of accuracy and misrepresentation. The Panel would like to point out that the recent "Mystery Shop" research undertaken by the Ontario Securities Commission, IIROC, and the Mutual Fund Dealers Association recorded no fewer than 48 different titles used by advisors. This is unacceptable.
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> **Ensure fair and timely complaint handling** - IIROC must make fair and timely complaint handling and restitution a priority for itself and for the firms it regulates. The CSA's 2014 audit of IIROC's own complaint handling identified serious concerns with investigation practices specifically with regard to suitability and supervision violations. IIROC should urgently undertake a review of its practices that will enable it to improve its performance. IIROC should also set performance targets that will

enable it to track and measure improvements in investigations and enforcement actions regarding suitability and firm supervision.

Spearhead the introduction of a best interest standard - We believe that IIROC should participate in and take a leadership role in the current regulatory and public discussions led by the CSA about improving advice standards for Canadians. This is what IIROC's U.S. regulatory counterpart FINRA has recently done. Until such time as a best interest standard is introduced, IIROC must address the serious business conduct compliance and enforcement failures documented in the CSA audit to ensure that its firms are in full compliance with the current suitability standard.

Unsuitable investments are the number one investor complaint that IIROC receives. As the exempt market expands and regulatory arbitrage becomes an even more frequent reality with the introduction of CRM2, IIROC's inability to identify and address issues of unsuitable product recommendations should be a grave concern to it.

Focus on conflicts of interest - IIROC should also make it a Compliance and Enforcement priority to review retail accounts dealing with conflicts of interest and the supervisory arrangements that firms have in place to address these issues. Conflicts of interest, especially with respect to compensation-driven conflicts of interest as well as with regard to outside business activities, should be a key compliance and enforcement focus.