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## **RE: The Investor Advisory Panel Seeks Your Input**

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FAIR Canada is pleased to offer comments to the Ontario Securities Commission's (the "**OSC**") Investor Advisory Panel (the "**IAP**") regarding issues that are important to investors.

FAIR Canada is a national, non-profit organization dedicated to putting investors first. As a voice of Canadian investors, FAIR Canada is committed to advocating for stronger investor protections in securities regulation. Visit [www.faircanada.ca](http://www.faircanada.ca) for more information.

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### **1. FAIR Canada's Comments on the OSC's Draft Statement of Priorities**

- 1.1. FAIR Canada has addressed many of the issues identified in the IAP's request for written comments in our comment letter ("**Comment Letter**") addressed to the OSC in response to its Request for Comments Regarding Statement of Priorities for Financial Year to End March 31, 2013 (the "**OSC's Draft Statement**").
- 1.2. FAIR Canada is generally very supportive of the OSC's Draft Statement. Our Comment Letter supports the OSC's proposed priorities and makes additional recommendations for the OSC's consideration. We direct the IAP's attention to our Comment Letter, which is enclosed in full.
- 1.3. Below, we discuss in detail some issues of importance to investors that are not canvassed in full in the Comment Letter.

## 2. Investment Dealers/Advisors – Best Interest Standard

- 2.1. FAIR Canada strongly believes that dealers and advisors should be required to act in their client’s best interest. There is a misalignment of investor expectations and advisors’ actual duties under the current rules, as demonstrated by research commissioned by the IAP and other groups.<sup>1</sup> Furthermore, there is an extreme informational asymmetry between investors in Canada and their financial advisors, which needs to be addressed by imposing a higher onus on advisors.
- 2.2. Marketing materials that make promises such as “we will take care of you” or that promise that the firm will deliver a comfortable retirement lifestyle serve to increase reliance by investors on the advisory relationship and often encourage clients to passively accept and implement the advice proffered. Advisors’ use of inflated titles exacerbates these problems. Clients are generally unaware of what and how they pay for financial products and services. They may not understand that advisors often are paid (directly or indirectly) to encourage sales of a particular product. As a result, clients are not aware that the advice received may have been affected by the advisor's monetary interests.
- 2.3. FAIR Canada recognizes that a best interest requirement would pose a significant change to the framework of securities regulation in Ontario. However, we note that other leading jurisdictions, including the U.S., the U.K., and Australia, have made significant movements towards this type of standard and are continuing to refine their approach in this direction.
- 2.4. **FAIR Canada believes that introducing a standard that requires dealers and advisors to provide advice that is in the client’s best interest would provide greater protection for investors. Canada must ensure that the relationship between retail investors and their advisors appropriately protects the interests of the investing public.**
- 2.5. It is also important that regulators develop a system to ensure that advisors have attained the appropriate level of proficiency to provide the services that they offer. Investors need to have the means to evaluate the education, certification and training, as well as experience, of any registrant from whom they consider obtaining advice.

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<sup>1</sup> For example, “Focus Groups with Retail Investors on Investor Rights and Protection”, Prepared for The Investor Advisory Panel Of The Ontario Securities Commission (April 7, 2011), online: <[http://www.osc.gov.on.ca/documents/en/Securities-Category1-Comments/com\\_20110427\\_11-765\\_ananda.pdf](http://www.osc.gov.on.ca/documents/en/Securities-Category1-Comments/com_20110427_11-765_ananda.pdf)>.

### 3. Disclosure

#### *Annual Performance and Cost Reports*

- 3.1. It is vital that investors are provided with regular cost and performance reporting that is complete, accurate, and provided in language and a format that investors can easily understand. Providing complete cost disclosure and clear and meaningful account performance reporting is essential to promoting clients' financial awareness.
- 3.2. It is particularly important, in FAIR Canada's view, that costs are clearly and completely disclosed, in dollar terms. It is essential that the total compensation paid (directly or indirectly) to the client's financial advisor is clearly and completely provided to allow the investor to evaluate whether they are paying a fair price for the service and advice received. Many investors are not provided with this information, even though they have a right to know what they are paying for the advice they receive.

#### *Benchmarks*

- 3.3. It is important that annual performance disclosure allow investors to compare their investment's performance to benchmarks. FAIR Canada recognizes that benchmarks can be complicated, and suggests that the Canadian Securities Administrators ("**CSA**") determine how best to calculate, present and use benchmarks to retail investors in order to provide context to an individual's investment returns.
- 3.4. As was noted in a report commissioned by the CSA, "a simple understandable but imperfect benchmark will help investors more than a complex perfect benchmark that they don't understand."<sup>2</sup> Simply mandating the use of a five year GIC or average savings deposit rate and the S&P/TSX Composite Index would be better than no benchmark information at all. Clear disclosure regarding the benchmark provided is essential to make the comparison fair and meaningful for investors.

#### *Fund Facts*

- 3.5. FAIR Canada is generally supportive of the Fund Facts concept. However, FAIR Canada takes issue with the length of time the point of sale initiative has taken, how it is being implemented and has concerns with several aspects of the document itself:

#### Prospectus Delivery Requirements

- 3.5.1. The CSA has permitted the delivery of the Fund Facts to satisfy the prospectus delivery requirements prior to a full public consultation. Not only are we concerned that the Fund Facts document is flawed, but we also view the prospectus to provide important information that is not available in Fund Facts.

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<sup>2</sup> Dr. Edwin L. Weinstein, *Report: Performance Reporting And Cost Disclosure*, Prepared for: Canadian Securities Administrators (Sept. 2010), online: <[http://www.osc.gov.on.ca/documents/en/Securities-Category3/rpt\\_20110622\\_31-103\\_performace-rpt-cost-disclosure.pdf](http://www.osc.gov.on.ca/documents/en/Securities-Category3/rpt_20110622_31-103_performace-rpt-cost-disclosure.pdf)>.

Fund Facts is not intended to be a comprehensive disclosure document; instead, it is meant to highlight key information that is important to investors, including objectives of the fund, past performance, risks and the costs of investing in a mutual fund.

#### At or Before the Point of Sale

3.5.2. The Fund Facts document was intended to be a key element of the Point of Sale initiative. However, in addition to permitting delivery of the Fund Facts to satisfy prospectus delivery requirements, the Fund Facts is not yet required to be delivered at or before the point of sale.

#### Fund Facts Deficiencies

3.5.3. FAIR Canada views the current version of the Fund Facts document to be deficient in several respects. We understand that the CSA is reviewing a number of the concerns that FAIR Canada and other investor advocates (including the IAP) have highlighted in the current iteration of the Fund Facts document. In particular, we are concerned with the following Fund Facts information:

- 3.5.3.1. Deficient risk disclosure;
- 3.5.3.2. Lack of benchmark information;
- 3.5.3.3. Inadequate conflicts of interest provision; and
- 3.5.3.4. Lack of currency and hedging policies.

3.5.4. One of the primary objectives of the fund facts document was to allow consumers to compare different products; these problems impede comparability, particularly the deficient risk disclosure.

#### *Point of Sale Requirements Extended to Other Investments and Financial Products*

3.6. FAIR Canada agrees that the Point of Sale requirements should be extended to other investments and financial products. Delivery at or before the point of sale should not be delayed while requirements for like documents are developed for other investment products, such as ETFs.

#### *Best Interest Obligation*

3.7. It is important to note that disclosure alone is insufficient to provide an acceptable level of investor protection; the client's best interest obligation, as discussed above in section 2, is also necessary to provide adequate investor protection.

#### 4. Disclosure and Investor Protection

- 4.1. FAIR Canada does not believe that the emphasis by regulators on “full and fair disclosure” is enough to protect investors. The recent financial crisis has confirmed this view. Given the constant evolution of securities products and the length and legalistic language of most disclosure documentation (not to mention the evidence pointing to the fact that the majority of investors do not read these documents)<sup>3</sup>, a framework based solely on formal disclosure documents is insufficient to adequately protect investors.
- 4.2. It is essential that some elements of a merit- or substantive-based regulatory approach are incorporated into the Canadian securities regulatory framework. “Both principles-based and proportionate-based approaches to regulation are to some extent already reflected in existing securities regulation in Canada.”<sup>4</sup> For example, securities regulators have a discretionary power to not receipt a prospectus if they believe that the offering is unconscionable. Although merit-based regulation of actual investment products does not currently form the basis of Canadian securities regulators' reviews of offerings, we suggest it may be time for regulators to consider merit-based review of the products themselves. **There is a need for more substantive regulation, particularly given the informational asymmetry between well-resourced, sophisticated investment firms and unsophisticated retail investors.**
- 4.3. In FAIR Canada’s view, group scholarship plans are one example of securities that require substantive or merit-based regulation. As outlined in its Comment Letter, FAIR Canada believes that, given many features common to group scholarship plans, improved disclosure is inadequate to provide an acceptable level of protection for the vulnerable consumers such plans frequently target. **We believe that disclosure alone will only create the illusion of consumer protection and cannot be an end in itself given the problems with the design of group scholarship plans, the aggressive manner in which they are marketed and advertised, and the misalignment of incentives between the salespersons and the mainly modest or low-income consumers who are sold this product.** FAIR Canada recommends that securities regulators introduce substantive regulation, such as limiting the fees that can be charged on such products (for example, to a maximum of ten percent of contributions for a given year).
- 4.4. Another example of products that warrant substantive regulation are double- and triple-levered ETFs. These highly levered products magnify returns and losses by 2.5 to 3.5 times that of the underlying security. FAIR Canada believes that regulators should question whether such risky and complex products should be permitted to be made available to retail investors, and if so, what additional safeguards should be implemented.

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<sup>3</sup> *Supra*, note 2.

<sup>4</sup> Expert Panel on Securities Regulation, “Final Report and Recommendations” (January 2009), online: <[http://www.expertpanel.ca/eng/documents/Expert\\_Panel\\_Final\\_Report\\_And\\_Recommendations.pdf](http://www.expertpanel.ca/eng/documents/Expert_Panel_Final_Report_And_Recommendations.pdf)>, at page 17.

## **5. Corporate Governance**

- 5.1. In October 2011, FAIR Canada provided comments to the Toronto Stock Exchange relating to corporate governance practices<sup>5</sup>. FAIR Canada supported the proposed amendments to eliminate slate voting in favour of electing directors individually and to prevent staggered boards and require annual elections for all directors.
- 5.2. FAIR Canada urged the TSX to mandate majority voting rather than implementing an “adopt or explain why they have not” approach to voting. Majority voting policies would support good governance by providing a meaningful way for security holders to hold directors accountable and remove underperforming or unqualified directors. Majority voting policies would also align the TSX Company Manual with international best practices.
- 5.3. FAIR Canada recommended that the TSX require disclosure to the public of the voting results for each item on the proxy, including voting results for individual directors, in order to improve communications between shareholders and issuers and in order to improve accountability to shareholders.
- 5.4. FAIR Canada further suggested that securities regulators undertake a public consultation to examine reforms that would allow shareholders to put forward nominees for election to the board of directors and have their nominees listed in the management proxy circular without the onerous and expensive current legal requirements. FAIR Canada recommended that securities regulators undertake a public consultation to examine ways to allow shareholders to communicate or solicit other shareholders without the need to file a dissident proxy circular.
- 5.5. FAIR Canada believes that the recommendations above would go a long way to improving corporate governance for Canadian shareholders.

## **6. OSC’s Strategic Plan**

- 6.1. FAIR Canada strongly supports the OSC’s focus on investors in its 2012-2015 Strategic Plan. As noted in the attached Comment Letter, FAIR Canada supports the OSC’s initiative to create an Office of the Investor (“**OI**”) to establish a stronger investor focus and understanding at the highest levels of the organization. FAIR Canada is pleased that the Strategic Plan refers to the OI participating in the new Policy Coordination Committee to “bring a clear investor perspective to the policy agenda of the OSC”. We believe that the OSC will greatly benefit from the creation of such an office. FAIR Canada recommends

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<sup>5</sup> FAIR Canada comments Re: Proposed Amendments to Part IV of the Toronto Stock Exchange Company Manual outlined in the Amendments to Part IV of the TSX Company Manual – Request for Comments dated September 9, 2011 (October 11, 2011), online: <<http://faircanada.ca/wp-content/uploads/2011/01/111011-FAIR-Canada-submission-to-TSX-re-Part-IV-of-the-Manual.pdf>>.

that the OI mandate focus primarily on retail investors, as they are the most vulnerable investor group and in the greatest need of protection in Canada's capital markets.

- 6.2. Under the 'OSC Organizational Goals', FAIR Canada is pleased to see that goal 3 is 'Deliver Strong Investor Protection' and that the OSC has committed to "champion investor protection, especially for retail investors." We believe that the Commission's vision is aligned with its mandate to protect investors.

We thank you for the opportunity to provide our comments and views in this submission. We welcome its public posting and would be pleased to discuss this letter with you at your convenience. Feel free to contact Ermanno Pascutto at 416-214-3443 (ermannopascutto@faircanada.ca) or Ilana Singer at 416-214-3491 (ilana.singer@faircanada.ca).

Sincerely,



Canadian Foundation for Advancement of Investor Rights

Encls.