FAIR | Canadian Foundation *for* Advancement *of* Investor Rights
Fondation canadienne *pour* l'avancement *des* droits *des* investisseurs

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Darshna Amin
Senior Policy Counsel, Member Regulation Policy
Investment Industry Regulatory Organization of Canada
Suite 2000, 121 King Street West
Toronto, ON M5H 3T9

And

Market Regulation
Ontario Securities Commission
Suite 1903, Box 55
20 Queen Street West
Toronto, Ontario M5H 3S8

Sent via e-mail to: damin@iiroc.ca and marketregulation@osc.gov.on.ca

RE: Republication of Proposed IIROC Dealer Member Plain Language Rule Book – IIROC Notice 18-0014

FAIR Canada is pleased to offer comments in response to IIROC's consultation on those sections of the Plain Language Rule ("PLR") Book with material changes since the last publication of proposed amendments to the PLR in March 2017, as set out in IIROC Notice 18-0014 dated January 18, 2018 (together with its Appendices, referred to herein as the "IIROC Notice").

FAIR Canada is a national, charitable organization dedicated to putting investors first. As a national voice for Canadian investors, FAIR Canada is committed to advocating for stronger investor protections in securities regulation. Visit www.faircanada.ca for more information.

1. General Comments

1.1. The PLR project's purpose was to rewrite, reformat, rationalize and reorganize IIROC's Dealer Member Rules ("DMR") in plain language. IIROC Notice 16-0052 cites five intended benefits of the PLR project namely:

(i) Improving the clarity and understanding of the DMR;

(ii) Streamlining the DMR by focusing on core requirements and moving non-essential details to guidance;

(iii) Eliminating obsolete, duplicative and unnecessary requirements;

(iv) Reorganizing the rule structure in a more logical fashion; and

(v) Clearly stating the objective of each rule.

1.2. IIROC Notice 16-0052 also states that certain rules were identified that also needed revision in order to "update and improve regulatory policy and, in some instances, to conform to requirements under National Instrument 31-103."

1.3. This project commenced around 2010 when the first tranche of proposed PLRs was issued for consultation. The full set of PLRs was then published for comment in March 2016 and again in March 2017 (with the Consolidated Enforcement, Examination and Approval Rules). The PLR project has taken a considerable period of time to accomplish its objectives.

1.4. At this late stage, one would think that material or substantive changes would be minimal, and if necessary, would be highlighted in the section "Nature of proposed amendments" so that stakeholders would be aware of the proposed amendments. Few stakeholders continue to provide comments on the PLR at this late stage, with the March, 2016 proposed amendments only receiving comments from six stakeholders, and not one of those six was from a retail investor perspective.[1] The IIROC Notice does not indicate how many stakeholders commented in response to IIROC Notice 17-0054, published in March, 2017.

1.5. FAIR Canada notes that the IIROC Notice contains, among other things, proposed amendments to be carried out as part of the PLR project as follows:

(i) Proposed amendments that change a discussion of account appropriateness found in 2012 Know Your Client and Suitability – Guidance into a PLR (earlier proposed in a March 2017 IIROC Notice 17-0054 but for which FAIR Canada was not aware) (Proposed PLR 3211);

(ii) Proposed amendments relevant to order execution only ("OEO") accounts which will:

(a) Require OEO firms to determine that an online account is appropriate for a person but not require that the OEO firm determine whether "the scope of products and account types" that the person has access to within the OEO account are appropriate for the person (proposed PLR 3211(2)); and

(b) Absolve OEO firms for being responsible for making a determination that the "products and account types offered by the Dealer Member in the order execution

[1] See IIROC, "Comments Received in Response to Rules Notice 16-0052 – Rules Notice – Request for Comments – Dealer Member Rules – RePublication of Proposed IIROC Dealer Member Plain Language Rule Book", online: <http://www.iiroc.ca/Documents/2017/2ab347d9-acf6-4ed7-b154-e33cf1fd9e81_en.pdf>.

only account are appropriate for the client". (PLR 3241(2)(i)(c)). The aforementioned proposed amendments to the order execution account only services rule is not highlighted in the IIROC Notice under "Nature of proposed amendments."

1.6. FAIR Canada also notes that PLR 3211's and 3241's wording, on its face, are confusing and unclear, and therefore, not written in conformance with the objectives of the PLR project.

1.7. At the same time, the IIROC Notice does not include any amendments to the PLR dealing with retail client complaints despite one of the stated objectives of the PLR being to update the rules to be in conformity with NI 31-103.

2. Comments Dealing with Proposed PLR Rules re Account Appropriateness and OEO Firms (also known as "Discount Brokerages")

2.1. **FAIR Canada recommends that any proposed changes regarding OEO firms, including the scope and content of an account appropriateness requirement, be deferred until such time potential changes in light of CSA Consultation 81-408, and the OSC's pending Seniors Strategy are launched.** After these consultations are completed, it would then be timely to issue for public comment any required or necessary changes to the PLR regarding OEO firms and any necessary changes to any IIROC OEO guidance. Therefore, IIROC's Proposed OEO Guidance issued for public comment in 2016, should not be finalized at this time and should be reissued for comment at a later date as with the proposed changes relevant to OEO firms contained in this IIROC Notice.

2.2. FAIR Canada reminds IIROC that the rationale for the payment of a trailing commission is that, in theory, the intermediary provides ongoing investment advice to the client. When investors purchase funds that include trailing commissions through an OEO platform we fail to see the justification for a trailing commission given that a recommendation or advice was not, and could not, be provided. Many investors who purchase such funds through OEO platforms are not aware of the existence of the trailing commission and are not aware that a trailing commission will negatively impact their rate of return. As such, these investors do not know to avoid funds that include embedded commissions, and are susceptible to purchasing them.

2.3. **FAIR Canada has called and continues to call for the immediate elimination of embedded commissions from investment products sold at discount brokerages given that IIROC Dealer Member Rules do not permit discount brokerages to provide recommendations**. FAIR Canada recommends that all firms offering a particular mutual fund be required to offer the "F" class version of the fund at discount brokerages. FAIR Canada is astounded that regulators have not done this to date.

2.4. FAIR Canada has called for both the CSA and IIROC to ban OEO platforms from selling products that include embedded trailing commissions immediately as there is no legitimate basis upon which to collect such commissions.

2.5. Even the Investment Funds Institute of Canada ("IFIC"), the mutual fund industry lobby group, in 2017, called on regulators to ensure that mutual funds carrying an embedded advisor fee are sold only in channels where advice is permitted. "Investors who buy funds directly, for example through a discount broker, should be confident that they are not inadvertently overpaying by

selecting a series that includes fees for services that are not available through that platform, says Paul C. Bourque, Q.C., IFIC's president and CEO."[2]

2.6. This is a problem that requires immediate action as $25 billion of the total $30 billion in mutual funds in the discount channel is estimated to be in the full trailing commission paying series[3].

2.7. **The current proposed amendments to the PLR may attempt to absolve OEO firms from any responsibility to protect investors from purchasing products, including purchasing or holding "A" class mutual funds** since it does not require that the OEO firm determine whether "the scope of products and account types" that the person has access to within the OEO account are appropriate for the person (proposed PLR 3211(2))**. FAIR Canada opposes the adoption of any such provision**.

2.8. **In addition, although it may not be intended, one of the consequences of the proposed amendments relevant to OEO firms may be to absolve OEO firms from any responsibility to detect unusual trading activity in a person's OEO account which may be the result of unlawful activity resulting from elder financial abuse, financial exploitation, undue influence or the result of diminished mental capacity.**

2.9. OEO firms, through the use of technology, currently have the ability to detect unusual activity in a person's OEO account and, as a result, through appropriate protocols, determine if this is due to suspected financial abuse, financial exploitation, undue influence or diminished mental capacity and to take steps to address it. While OEO firms do not have face to face contact with their clients, their affiliated firms may very well have such face to face contact and/or there are steps that may be taken to protect such persons in such circumstances.

2.10. For example, a conservative buy and hold investor who has a 40/60 or 30/70 portfolio, plain vanilla ETFs or mutual funds, may be flagged by the OEO firm if suddenly there is options trading, the trading of leveraged ETFs or highly speculative securities. It would not be in the interests of adequate investor protection to have no obligation to flag this and not make "…a determination that the products and account types offered by the OEO firm in the OEO account are appropriate for the client." Issues regarding self-determination of older adults to make poor decisions need to be balanced against the need to do what is possible and practicable to address and combat elder financial abuse, financial exploitation and undue influence as well as address diminished mental capacity.

2.11. **Therefore, FAIR Canada is opposed to the proposed amendments to the PLR regarding OEO obligations. The proposed changes to the PLRs re OEO firms should not proceed at this time.**

[2] The Investment Funds Institute of Canada, "Media Release - Limit Series A Sales to Channels that Permit Advice: IFIC", online: <https://www.ific.ca/en/news/limit-series-a-sales-to-channels-that-permit-advice-ific/>.

[3] CSA Consultation Paper 81-408: Consultation on the Option of Discontinuing Embedded Commissions, at page 41; online: <http://www.osc.gov.on.ca/documents/en/Securities-Category8/sn_20170110_81-408_consultation-discontinuing-embedded-commissions.pdf>.

3. Comments on PLR Dealing with Retail Investor Complaints

3.1. FAIR Canada and the Public Interest Advocacy Centre recently brought to the attention of the OBSI Joint Regulators Committee, by letter dated, October 11, 2017, the use of "internal ombudsman" by registered dealer firms, including that IIROC's present Rule 2500B (and proposed PLR 3726) is not in compliance with sections 13.6(3) and (4) of NI 31-103.

3.2. By Joint CSA Staff Notice 31-351, IIROC Notice 17-0229, MFDA Bulletin #-736-M, "Complying with requirements regarding the Ombudsman for Banking Services and Investments" (the "Staff Notice"), the CSA, IIROC and MFDA highlighted concerns with some registered firms' complaint handling systems and the use of internal ombudsmen including confusion arising from their use – for example, it is not an "alternative" to OBSI – and conflation with OBSI. **FAIR Canada recommends that the Proposed PLRs regarding complaints should be reviewed and amended in light of the Staff Notice and NI 31-103.**

3.3. **Moreover, in the interests of investor protection, including the fairness and effectiveness of responding to complaints, FAIR Canada recommends that IIROC (and the MFDA) review and consult publicly with respect to their rules dealing with client complaints.** Such a review should involve (although not be limited to) the following:

(i) Ensuring that policies and procedures of firms are in accordance with NI 31-103 so that their response to a complaint is "in a manner that a reasonable investor would consider fair and effective" rather than "a balanced approach to dealing with complaints that objectively considers the interests of the complainant, the Dealer Member, including the employees, Approved Persons or other relevant parties" (PLR 3723(2)(vi));

(ii) Whether it is in the interests of investor protection to prohibit firms from using the term "internal ombudsman" and whether all internal complaint processes, including the use of any "internal ombudsman" should be required to be completed within 90 days;

(iii) Whether the PLRs regarding complaints need rewording to ensure that investors are made aware of the two brochures (rather than one) that IIROC has issued, which is mis-described in the proposed PLRs as one brochure - "…a copy of the complaint handling process brochure approved by IIROC";

(iv) Whether it is in the interests of investor protection and clarity to split the IIROC Brochure into two brochures, one entitled "Making a Complaint A Guide for Investors Part 1 of 2" and "How Can I Get My Money Back? A Guide for Investors Part 2 of 2";

(v) The empirical testing of the IIROC Brochures to determine whether retail investors use the information contained in them, as anticipated, or whether improvements could be made and, of at least equal importance, consultation with those who have relevant knowledge of consumers' understandings, experiences and needs with respect to pursuing their complaints and concerns

(i.e. consumer advocates, OBSI, and the Osgoode Investor Protection Clinic founded by Osgoode Hall Law School and FAIR Canada). For example, possible changes may include:

a. combining the Part 2 of 2 brochure into the first, Part 1 of 2 brochure;

b. making pages 8 and 9 of the "Making a Complaint A Guide for Investors" brochure into pages 1 and 2 of that brochure;

c. making it clear at the outset of the brochure that if a person wants their money back, they must start with a written complaint to the firm, whereas if they want to notify the regulator so that the regulator can determine if any regulatory investigation or enforcement is merited, they can notify (or advise rather than bring their complaint to) IIROC about their complaint/concern; and

d. whether a flow chart or other type of diagrammatic would be helpful or not.

(vi) Whether the reporting of investor complaints, given the requirements set out in PLR 3703 (see appendices to the March, 2017 Notice), are sufficient to ensure the adequate protection of investors and transparency and accountability of the system overall, for example (but not limited to) requiring dealer members to report to IIROC when a client agrees to use its voluntary "internal ombudsman" process and how often the firm resolves the matter at this stage to the satisfaction of the client. Furthermore, whether it would foster confidence in our capital markets and improve investor protection to require the reporting of verbal complaints to IIROC in addition to requiring the handling of verbal complaints, and overall to ensure the system of tracking and reporting of complaints is robust, transparent and fosters accountability for all stakeholders.

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 Frank Allen at 647-256-6693/frank.allen@faircanada.ca or Marian Passmore at 647-256-6691/marian.passmore@faircanada.ca.

Sincerely,

Canadian Foundation for Advancement of Investor Rights