



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

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RE: Ontario Securities Commission Notice 11-780 – Statement of Priorities

FAIR Canada is pleased to offer comments on Ontario Securities Commission's ("OSC") Notice 11-780 – Statement of Priorities – Request for Comments Regarding Statement of Priorities for Financial Year to End March 31, 2019 ("Statement of Priorities" or the "2019 Draft Priorities") published on March 29, 2018.

FAIR Canada is a national, charitable organization dedicated to putting investors first. As a 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. FAIR Canada is pleased to see that investor protection is emphasized throughout the 2019 Draft Priorities. Many of the initiatives the OSC offers to prioritize will have a positive impact on investors and help to improve investor protection in Ontario. For example, we welcome the OSC's priorities related to a best interest standard, implementing a Seniors Strategy and pursuing proactive compliance and achieving enforcement case results that have a significant deterrent impact.
- 1.2. FAIR Canada, like other investor-focused stakeholders however, believes that actions speak louder than words and that investor-focused initiatives simply take far too long to reach the finish line (regulatory outcomes). The key investor focused initiatives have been carried over from the previous Statement of Priorities, and in fact, have been "in the works" or subject to consultation(s) that have been ongoing for years.
- 1.3. The OSC (and other CSA members) need to ensure that outcomes derived from initiatives related to its key mandate to protect investors proceed at a much quicker pace. Not only is the

slow pace detrimental to investors that continue to be negatively impacted by these issues, but it also has negative consequences for investors that are affected by other emerging and existing issues, which cannot be addressed because work on previous investor protection initiatives has not been completed.

- 1.4. The following sections highlight some of the key investor related issues FAIR Canada believes are important for the OSC to keep at the forefront as priorities for the coming year.

2. Best Interest Standard and Conflicted Compensation Structures

Best Interest Standard

- 2.1. FAIR Canada is very pleased that the OSC will be publishing regulatory provisions to create a best interest standard along with embedding a new client/advisor standard in the core targeted regulatory reforms under National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*.
- 2.2. FAIR Canada hopes that the regulatory reforms contain the appropriate mix of broad and specific provisions, so that a meaningful standard, that is clear to investors and registrants, is achieved
- 2.3. FAIR Canada is disappointed that title and proficiency reforms are not well underway in light of their importance in ensuring investors obtain advice that is in their best interests.
- 2.4. FAIR Canada notes that the OSC in its Report on Statement of Priorities for fiscal 2013-2014 stated under “Best Interest Duty” that “Research was completed on proficiency standards in Canada, the US, the UK and Australia to inform our thinking on potential changes to our standards.” In addition, CSA Consultation 33-404 dated April 28, 2016 included consultation on reforms to proficiency and titles, and the OSC’s Seniors Strategy released in 2018 included references to needed work on misleading and confusing titles, designations and marketing practices.
- 2.5. In collaboration with efforts being made by the Ontario government with respect to regulating financial planning, we urge the OSC and other CSA members to proceed quickly with reforms in the area of proficiency and titles including providing regulatory reform proposals within the 2018-2019 fiscal year rather than “[i]nitiate work on remaining reforms such as titles and proficiency and provide recommendations to advance the initiatives to the Commission.”¹ FAIR Canada believes that this is an essential step (among others) to ensuring that a best interest standard is actually effective in practice. We urge action to prevent the use of a bewildering array of unregulated and frequently misleading titles that falsely convey high levels of proficiency, seniority, experience or authority and do not reflect the standard of advice being provided.

¹ Draft 2018-2019 Statement of Priorities at 6.

- 2.6. When revising proficiency standards, we urge the OSC to include mandatory education and competency-based training in the areas of elder abuse, undue influence, mental capacity issues, enduring powers of attorney and ageism. The consultations that FAIR Canada and the Canadian Centre for Elder Law undertook related to its project on vulnerable investors² indicated an absolute consensus amongst all stakeholders that mandatory education and training was desired and required for firms and representatives in the area of elder abuse, undue influence and mental capacity challenges.

Embedded Commissions

- 2.7. FAIR Canada believes it is now time for a regulatory decision rather than further consultation on policy recommendations, policy provisions and analysis of potential impacts, as contemplated by the 2019 Draft Priorities. The issues have been thoroughly canvassed and time is long overdue to implement changes so as to eliminate embedded commissions.
- 2.8. We agree with the OSC's Investor Advisory Panel's submission and the points it makes on embedded commissions.³ In particular we fully agree with its statement that "[w]e have reached the point where nothing new is being said or remains to be said on this subject. The time has come...for the OSC, along with other CSA members, to bring closure to this debate."
- 2.9. FAIR Canada believes that the financial services industry has had much time to consider how it will adapt to the elimination of embedded commissions and we urge the OSC and other CSA members to make public their decision.

Other Conflicted Compensation Structures

- 2.10. FAIR Canada continues to believe that other conflicted compensation structures require sufficient attention from the OSC. Poor recommendations and bad advice are not the result of a few bad apples in the system, but from compensation structures and firm-wide practices that place firms' and representatives' interests ahead of the interests of Canadians.
- 2.11. The CSA, IIROC and the MFDA all issued notices in 2016 and 2017 reviewing the many sales practices, compensation arrangements and incentives that significantly impede professional, objective advice being provided.⁴

² See the Joint Report by FAIR Canada and CCEL, Report on Vulnerable Investors: Elder Abuse, Financial Exploitation, Undue Influence and Diminished Mental Capacity (November 2017) at 55, online: <<http://faircanada.ca/wp-content/uploads/2017/11/171115-Vulnerable-Investor-Paper-FINAL-1.pdf>>. Joint press release available at <https://www.newswire.ca/news-releases/report-on-vulnerable-investors-elder-abuse-financial-exploitation-undue-influence-and-diminished-mental-capacity-657996063.html>. Funding of this project was derived from the Law Foundation of Ontario Access to Justice Fund.

³ AP Response to OSC Draft IStatement of Priorities for 2018-2019, online: <http://www.osc.gov.on.ca/documents/en/Securities-Category1-Comments/com_20180427_11-780_iap.pdf>.

⁴ CSA Staff Notice 33-318 Review of Practices Firms Use to Compensate and Provide Incentives to their Representatives (December 15, 2016), 39 OSCB 10115; IIROC Notice 17-0093 (April 27, 2017), "Managing Conflicts in the Best Interest of the Client – Compensation-related Conflicts Review; IIROC Notice 16-0297 (December 15, 2016), "Managing Conflicts in the Best Interest of the Client – Status Update; MFDA Review of Compensation, Incentives and Conflicts of Interest (December 2016).

- 2.12. The CSA Notice indicated that the work is ongoing and that they may issue “further guidance and/or proposed regulation related to compensation arrangements and incentive practices”.⁵ We urge the OSC to articulate in the Statement of Priorities how sales practices and compensation arrangements that are contrary to investors’ interests will be addressed.
- 2.13. We also would like the OSC to stipulate that conflicts that arise from selling proprietary products, which ultimately harm investors and market efficiency, will also be addressed in the upcoming year. Professor Douglas Cumming’s research found “...that both affiliated dealer flows and the payment of trailing commissions result in material conflicts of interest that are detrimental to mutual fund investors over the long term.”⁶ In the interests of retail investors, this should also be a priority.

3. Seniors Strategy

- 3.1. FAIR Canada is pleased that the OSC has published a Seniors Strategy and will be working on “[a] regulatory framework to address issues of financial exploitation and cognitive impairment developed together with regulatory colleagues.”
- 3.2. FAIR Canada and the Canadian Centre for Elder Law released a joint report in November 2017 entitled “Report on Vulnerable Investors: Elder Abuse, Financial Exploitation, Undue Influence and Diminished Mental Capacity” (through funding from the Law Foundation of Ontario Access to Justice Fund). The joint report examined the issue of how elder financial abuse, undue influence and mental capacity challenges are serious and growing social concerns and examined how the investment industry could play a key role in addressing these issues. The joint report received strong support from many stakeholders including the OSC’s Investor Advisory Panel and the Investment Funds Institute of Canada.
- 3.3. The joint report made six main recommendations:
1. Require investment firms to make reasonable efforts to obtain the name and contact information of a Trusted Contact Person for each client, who can be contacted in case of suspicion of abuse or diminished mental capacity, so long as they themselves are not suspected of financial abuse or exploitation of the client.
 2. Allow a Temporary Hold on Trades and Disbursements of funds or securities when there is a reasonable suspicion of financial abuse or where the client has lost the capacity to provide instructions.
 3. Provide a Legal Safe Harbour for investment firms and financial service providers who appropriately report suspicions of financial abuse or mental incapacity.
 4. Create a Conduct Protocol setting out the steps firms and financial services representatives

⁵ (2016), 39 OSCB 10115, CSA Staff Notice 33-318 Review of Practices Firms Use to Compensate and Provide Incentives to their Representatives, at 10115.

⁶ Professor Douglas Cumming, *Frequently Asked Questions about the Dissection of Mutual Fund Fees, Flows and Performance Report* (2016), at 7, online: <http://www.osc.gov.on.ca/documents/en/Securities-Category8/rp_20160209_81-407_faq-dissection-mutual-fund-fees.pdf>.

should take to identify and protect vulnerable clients including mandatory reporting of suspected financial abuse of vulnerable investors to the appropriate securities regulator.

5. Mandate Specific Education and Training in the areas of elder abuse, undue influence, mental capacity issues, enduring powers of attorney and ageism.
 6. Require that investment firms Become Familiar with Outside Resources and Responders and learn how and when to appropriately refer a case of suspected elder financial abuse, undue influence or diminished mental capacity to local responders.
- 3.4. As mentioned, the joint report received strong support from many stakeholders including the OSC's Investor Advisory Panel and the Investment Funds Institute of Canada. Therefore, the development of a regulatory framework and implementation should be able to proceed expeditiously.
 - 3.5. We would be pleased to contribute to efforts to create the regulatory framework and are supportive of an inclusive approach involving provincial and federal governments, self-regulatory organizations such as the Investment Industry Regulatory Organization of Canada ("IIROC") and the Mutual Fund Dealers Association of Canada ("MFDA"), the Office of the Privacy Commissioner of Canada and the Ontario Public Guardian and Trustee (and their provincial counterparts) working together, in a collaborative fashion, in order to better protect, empower and support older Canadians.
 - 3.6. FAIR Canada also recommends that the OSC discuss with stakeholders the industry's ability to provide financial products and services that are in the best interests of investors as they age, in particular during the de-accumulation phase.
- 4. Ombudsman for Banking Services and Investments (OBSI)**

Low-ball Offers and Binding Decision Making

- 4.1. FAIR Canada is encouraged that the OSC will give prominent focus to securing the ability of OBSI to make decisions that are binding on its members so that there exists effective investor redress as a necessary part of the capital markets framework and that it will, with its OBSI Joint Regulators Committee ("JRC") colleagues, address the other recommendations in the independent evaluator's report which was issued in May 2016.
- 4.2. We urge the JRC to indicate its expected timeline to actionize these recommendations.
- 4.3. We believe that all of the recommendations contained in the Battell Report are important. In particular, we agree with the Battell Report that the lack of binding decision-making authority on the part of OBSI tilts the playing field in favour of the firm. Firms are free to offer the consumer far less than what is fair in the circumstances since they do not have to factor in the risk that the ombudsman at OBSI has the ability to order an amount that is significantly greater (given its inability to render a binding decision).
- 4.4. We are of the view that action is long overdue to provide OBSI with power to issue binding

decisions as this is critical to the integrity of the Canadian financial services market and the protection of Canadian consumers. The prospect of OBSI imposing a result would: (a) allow the consumer to have confidence that they can reject a low-ball offer and still retain the ability to achieve a fair outcome; and (b) give firms a greater incentive to make fair settlement offers instead of low-ball ones.

- 4.5. Such a reform would also further the goal to have a dispute system in Canada that complies with our international obligations to be “accessible, affordable, independent, fair, accountable, timely and efficient.”
- 4.6. We urge the OSC to issue a specific proposal for OBSI to have binding decision-making within the fiscal 2018-2019 year. In addition, we urge the OSC to ensure that firms are adhering to CSA Staff Notice 31-351, IIROC Notice 17-0229, MFDA Bulletin #0736-M “Complying with requirements regarding the Ombudsman for Banking Services and Investments”.
- 4.7. We also continue to recommend that OBSI’s Terms of Reference and the internal complaint handling rules (be they policies or rules) of IIROC and the MFDA be amended to conform with NI 31-103.⁷ OBSI’s Terms of Reference and the SRO complaint handling rules should be revised to require firms to provide a substantive response to a complaint within 90 days, whether they use a second review process (an “internal ombudsman”) or not. Within the 90 days, firms may choose to provide a second level of review. However, they should not be permitted to take more than 90 days to do so.
- 4.8. Going forward, FAIR Canada urges the OSC, by itself or in concert with the CSA, to:
 - Take immediate action against registered firms that have repeatedly ignored their complaint handling obligations and refused to comply with OBSI’s recommendation, from the beginning of the OBSI complaint process;
 - Require registered firms to cease using the term “ombudsman” as part of their internal complaint handling process; and
 - Require registered firms to provide a prominent link to OBSI’s complaint handling process on their websites.

5. **Other Policy Areas**

Enforcement

- 5.1. FAIR Canada is pleased that the OSC wishes to increase the visibility and deterrent impact of its enforcement program. We encourage the OSC to prosecute wrongdoing such as fraud and other criminal activity through the use of criminal and quasi-criminal proceedings as these, we

⁷ See FAIR Canada and PIAC Joint Letter to OBSI Joint Regulators Committee (October 11, 2017), online: <<http://faircanada.ca/wp-content/uploads/2017/10/171011-Final-Joint-FAIR-Canada-and-PIAC-Letter-re-Use-of-Internal-Ombudsman-2.pdf>>.

believe, have a greater deterrent impact than the use of administrative sanctions.

- 5.2. While we encourage the OSC to collect penalties and fines in order to maximize the deterrent impact of its sanctions and increase confidence in our markets, we recognize there are limits in the ability to do so and, given limited resources, we would not wish to have this priority detract from efforts to identify and stop investors from being harmed by fraud and other wrongdoing.
- 5.3. In order to improve collection rates, we continue to recommend that firms be responsible for the fines of individual registrant employees. We also recommend that enforcement proceedings that are resolved through settlement agreements specifically address payment of fines to securities regulators and restitution or redress (including financial compensation) to investors.
- 5.4. FAIR Canada believes that better tracking of the prevalence and incidence of wrongdoing such as fraud and elder financial abuse complaints, investigations and proceedings is of importance. Police and other bodies will be more likely to dedicate resources to these issues when there is empirical evidence demonstrating how prevalent they are and how such crimes cost victims financially, emotionally and physically.
- 5.5. FAIR Canada is supportive of the OSC's whistleblower program. We encourage the OSC to publish an annual report on its whistleblower program. The report could indicate the number of tips received since the program began in July 2016, the number of investigations that have opened or have been materially assisted by tips and the number of proceedings commenced (and concluded). Such information should help with awareness of the whistleblower program.

Check Registration System

- 5.6. We recommend that the OSC work with its CSA colleagues to develop a better registration check system. While some improvements have been made, there are still problems with the current websites for retail investors. There is a need for a single, comprehensive tool that would allow investors to check the background of a potential advisor or investment firm. FAIR Canada calls for a user-friendly, one-stop tool where investors can access licensing, registration, disciplinary and background information (including proficiency and SRO membership) regarding advisers, dealers and their respective registered persons. Investor testing should be conducted to ensure the system is user-friendly and generates meaningful, helpful results.

Alternative Funds

- 5.7. FAIR Canada is of the view that while there may be some demand for alternative funds by retail investors, the initiative to broaden access to these funds is largely driven by the industry's desire to generate more fees. These funds will be mostly sold by financial advisors rather than bought by retail investors. Accordingly, we are opposed to the new framework which would give retail investors "access" to these funds until an applicable statutory best interest standard is implemented and advisor proficiency is increased.

Fintech

- 5.8. While supportive of innovation and supporting fintech's unique challenges in the securities industry, FAIR Canada cautions that fintech presents potential benefits and opportunities for consumers as well as risks to investor protection that should be examined and addressed.
- 5.9. In its efforts to support innovation and capital formation, the risks associated with fintech that impact financial consumers should not be overlooked. Such risks include: (i) technological errors such as deficient algorithms; (ii) failure to account in a timely fashion to changing financial circumstances of consumers; (iii) risk of platforms being operated by an unregistered entity; (iv) failure to prevent money laundering through failure to know your client; (v) financial exploitation of older investors through the accessing of funds online; and (vi) lack of transparency regarding fees and (vii) conflicts of interest.
- 5.10. This view is supported by a recent survey on fintech and technological innovations shaping new investment and financial products conducted by the North American Securities Administrators Association ("NASAA") members – state and provincial securities regulators in the United States, Canada and Mexico – about the challenges of adapting to new financial technology products and changes in how financial services are delivered to investors:

“One-third (34 percent) of securities regulators said the rapid development of financial technology is a positive development for investors, while 20 percent expressed concern with the potential negative impact of fintech on investors. Almost one-half (46 percent) said it is too soon to tell, citing benefits such as lower costs and greater accessibility to investments among groups not previously reached by traditional methods, but cautioning that sufficient investor protections must be in place so that easier access does not translate into greater exposure to risk or fraud.”⁸

FAIR Canada therefore recommends that the financial consumer perspective be part of a responsive regulatory approach in the area of fintech.

Cryptocurrencies and Initial Coin Offerings

- 5.11. FAIR Canada wishes to emphasize that despite the increasing popularity of cryptocurrencies, they remain extremely speculative, high-risk investments that are not suitable for most people. Cryptocurrencies can also be vehicles for individuals to carry out fraud and manipulation. As stated in CSA Staff Notice 46-307, cryptocurrencies raise investor protection concerns “due to issues around volatility, transparency, valuation, custody and liquidity, as well as the use of unregulated exchanges. Also investors may be harmed by unethical practices or illegal schemes, and may not understand the properties of the investment products that they are

⁸ North American Securities Administrators Association, *Rise of Fintech Raises New Concerns for Securities Regulators* (February 15, 2018), online: <<http://www.nasaa.org/44336/rise-fintech-raises-new-concerns-securities-regulators/>> and NASAA, *February 2018 Pulse Poll: Fintech* (February 2018), online: <<http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2018/02/NASAA-Fintech-Poll-Results.pdf>>.

purchasing.”⁹

- 5.12. With respect to Initial Coin Offerings (ICOs) the International Organization of Securities Commissions (IOSCO) stated in a communication from January 2018 that there are clear risks associated with ICOs, and the growing usage of ICOs to raise capital is an area of concern.¹⁰ FAIR Canada is pleased that regulators are attempting to address the use of ICOs to raise funds, as these offerings should generally be categorized as securities and registered with securities regulators.¹¹
- 5.13. However, FAIR Canada is concerned about exemptive relief for highly risky and speculative investments, particularly considering regulators’ own warnings regarding cryptocurrencies. FAIR Canada cautions against any pressure to reduce regulatory burden relating to ICOs, since there have already been well-documented and significant problems and losses related to cryptocurrencies.
- 5.14. FAIR Canada also encourages the OSC to err on the side of caution when considering applications from firms related to cryptocurrency investments – cryptocurrency investments are an area that regulators themselves have viewed as highly risky and ripe for fraud. According to NASAA, cryptocurrencies “and investments tied to them are high-risk products with an unproven track record and high price volatility. Combined with a high risk of fraud, investing in cryptocurrencies is not for the faint of heart.”¹² NASAA also surveyed securities regulators of which 94% viewed cryptocurrencies and ICOs as having a high risk of fraud, with all regulators surveyed agreeing that more regulation is needed for cryptocurrencies, in order to provide greater investor protection.¹³

Investor Office and Investor Advisory Panel

- 5.15. FAIR Canada strongly supports the mandates of the Investor Office and Investor Advisory Panel as these entities help inform the OSC as it engages in policy-making and operations and allow it to modernize its efforts in investor engagement, research, education and outreach. FAIR Canada is supportive of efforts to develop tailored solutions to reach the broad range of at-risk investor groups, including seniors, millennials, new Canadians and indigenous peoples.

⁹ CSA Staff Notice 46-307 *Cryptocurrency Offerings*, online: < http://www.osc.gov.on.ca/en/SecuritiesLaw_csa_20170824_cryptocurrency-offerings.htm>.

¹⁰ International Organization of Securities Commissions (IOSCO), “IOSCO Board Communication on Concerns Related to Initial Coin Offerings (ICOs)” (18 January 2018), online: <<http://www.iosco.org/news/pdf/IOSCONEWS485.pdf>>.

¹¹ For example. There were recent reports that the Securities and Exchange Commission in the United States sent subpoenas to dozens of people and companies behind ICOs that were not categorized as securities and registered with regulators. See Nathaniel Popper, “Subpoenas Signal S.E.C. Crackdown on Initial Coin Offerings” *New York Times* (28 February 2018), online: <<https://www.nytimes.com/2018/02/28/technology/initial-coin-offerings-sec.html>>.

¹² North American Securities Administrators Association (NASAA), “NASAA Reminds Investors to Approach Cryptocurrencies, Initial Coin Offerings and Other Cryptocurrency-Related Investment Products with Caution” (4 January 2018), online: <<http://www.nasaa.org/44073/nasaa-reminds-investors-approach-cryptocurrencies-initial-coin-offerings-cryptocurrency-related-investment-products-caution/>>.

¹³ *Ibid.* See also, NASAA “February 2018 Pulse Poll: Fintech” (February 2018), online: < <http://nasaa.cdn.s3.amazonaws.com/wp-content/uploads/2018/02/NASAA-Fintech-Poll-Results.pdf>>.

How Effective are Point-of-Sale and other Disclosure Documents?

- 5.16. In addition to working on new regulatory reforms and initiatives, the OSC should monitor and assess, through investor testing and otherwise, regulatory reforms that have already been implemented. It is important to understand the impact of recent regulatory reforms, particularly to the extent that such assessments can help us to learn the impact of the OSC's work. The OSC should make the results of any research or studies done in this regard public and should work to swiftly make any changes that are needed in light of its findings. For example, Point-of-Sale initiatives such as the Plan Summary document for Group Scholarship Plans should be reviewed in order to understand how they are being used and whether improvements can be made to their effectiveness.
- 5.17. FAIR Canada also urges the OSC to undertake investor testing of the risk acknowledgement forms used in connection with certain exemptions. Investor testing will allow regulators to determine whether investors understand the information that is being conveyed, how they are being used by investors and whether it helps protect investors. It will also allow regulators to determine whether any changes are needed to ensure that the risk acknowledgement forms being produced are in fact effective and useful to investors.

Syndicated Mortgages

- 5.18. FAIR Canada is pleased to see that the OSC is prioritizing the orderly transfer of syndicated mortgage investments. FAIR Canada looks forward to working with the OSC on exploring ways to build appropriate mechanisms and close regulatory gaps in order to ensure effective oversight and protection of 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 Frank Allen at [647-256-6693/frank.allen@faircanada.ca](tel:647-256-6693), Marian Passmore at [647-256-6691/marian.passmore@faircanada.ca](tel:647-256-6691) or Samreen Beg at [647-256-6692/samreen.beg@faircanada.ca](tel:647-256-6692).

Sincerely,



Canadian Foundation for Advancement of Investor Rights