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The Government of British Columbia, represented by its Minister of Finance
The Government of Ontario, represented by its Minister of Finance
The Government of Saskatchewan, represented by its Minister of Justice and Attorney General
The Government of New Brunswick, represented by its Minister of Justice
The Government of Prince Edward Island, represented by its Minister of the Environment, Labour and Justice and Attorney General
The Government of Yukon, represented by its Premier, Minister responsible for the Executive Council Office and Minister of Finance
The Government of Canada, represented by the Minister of Finance of Canada

(collectively, the "Participating Jurisdictions")

VIA EMAIL: comment@ccmr-ocrmc.ca

Dear Sirs/Mesdames:

Re: Cooperative Capital Markets Regulatory System
Revised Consultation Draft of Provincial/Territorial *Capital Markets Act* and Draft Initial Regulations

On behalf of Advocis, The Financial Advisors Association of Canada, we are pleased to provide our comments in regards to the revised draft provincial/territorial *Capital Markets Act* ("CMA") and draft initial regulations released in furtherance of the cooperative capital markets regulatory system (the "Cooperative System").

About Advocis

Advocis is the largest and oldest professional membership association of financial advisors and planners in Canada. Through its predecessor associations, Advocis proudly continues over a century of uninterrupted history serving Canadian financial advisors and their clients. Our 11,000 members, organized in 40 chapters across the country, are licensed to sell life and health insurance, mutual funds and other securities, and are primarily owners and operators of their own small businesses who create thousands of jobs across Canada. Advocis members provide comprehensive financial planning and investment advice, retirement and estate planning, risk management, employee benefit plans, disability coverage, long-term care and critical illness insurance to millions of Canadian households and businesses.

As a voluntary organization, Advocis is committed to professionalism among financial advisors. Advocis members adhere to a professional Code of Conduct, uphold standards of best practice,

participate in ongoing continuing education programs, maintain professional liability insurance, and put their clients' interests first. Across Canada, no organization's members spend more time working one-on-one on financial matters with individual Canadians than do ours. Advocis advisors are committed to educating clients about financial issues that are directly relevant to them, their families and their future.

Introductory Comments

We congratulate the Participating Jurisdictions on the release of the revised draft CMA and regulations as marking another major step towards establishing the Capital Markets Regulatory Authority ("CMRA") and making the Cooperative System a reality. We continue to support the Cooperative System as a long-anticipated and overdue restructuring of the securities regulatory landscape in Canada.

We recognize that implementing the Cooperative System across multiple provinces and territories, and interfacing that system with non-participating jurisdictions, represents a tremendous challenge and the Participating Jurisdictions have wisely adopted a platform approach where many details are addressed through regulation. Regulations are inherently more flexible than legislation, and that flexibility will be critical – particularly in the early stages as the Cooperative System goes into effect and operational adjustments will need to be made.

However, we are concerned that the Participating Jurisdictions are leaving the door open to using regulations to enact major changes to well-established securities laws – such as in regards to the legal regime for segregated funds, or the duty of care applicable to registrants. These are fundamental matters, and if they are to be changed, they should be done so only after considered debate, widespread stakeholder feedback, and ultimately, legislative amendment.

The gravity of these matters and their importance to Canada's financial services sector makes change by regulation inappropriate. Instead, any changes to fundamental concepts deserve the built-in safeguards of a fulsome legislative amendment. Therefore, we urge the Participating Jurisdictions to reconsider the extent to which they are proposing to grant the CMRA the authority to promulgate regulations that would change core tenets of Canada's securities regulatory system. It should not be the function of the Cooperative System to undercut the role of provincial legislatures in considering the merits of proposals that would bring about material change.

Discussion

(i) The regulation of segregated funds

The revised CMA retains provisions that would grant the CMRA the ability to make regulations governing segregated funds. While we certainly welcome the new section 202(2) as a requirement for ministerial-level deliberation before such a regulation can be promulgated, we believe that it is inappropriate to include any form of regulation-making authority in regards to segregated funds – it is tantamount to creating a "foot in the door" to effect major change to the financial services landscape by regulation, rather than through the legislative process.

We understand that the CMRA wishes to have this regulation-making power in order to "address any future changes in the financial sector" while also stating that that it is not the intention to regulate segregated funds upon the launch of the Cooperative System. But doing so, even eventually, would represent a tremendous shift in the financial services regulatory landscape and should be done with the utmost care and thought.

Segregated funds have an extensive regulatory history, being subject to three different regulatory regimes that are administered by two different levels of government for different purposes: by federal legislation/regulation as it pertains to solvency and corporate governance of life insurance companies; by provincial securities legislation/regulation as it pertains to the underlying fund; and by provincial insurance legislation/regulation as it applies to market distribution, consumer protection and generally-applicable elements of all life insurance contracts.

We certainly understand that the financial services landscape is constantly shifting and there may eventually be a need to fundamentally change the regulation of segregated funds – but, in that event, given the stakes involved, there should be a fulsome review to determine the best way forward, followed by any necessary amendments through the legislative process. We are purposefully asking for a more deliberate process to reflect the significance of the change being proposed. We believe that the type of landscape-changing authority proposed in the CMA, even with the added safeguard of ministerial-level approval, must be beyond the scope of regulation-based rulemaking.

If the Participating Jurisdictions are concerned about product arbitrage – which, in our opinion, is a legitimate concern – then they should seek to implement a more comprehensive solution to the problem along the lines of the Professions Model that we brought forward in our December 8, 2014 submission on the initial draft of the CMA.[1] Such a solution would address the arbitrage issue, as well as a variety of other consumer-facing issues that transcend product sectors but remain unaddressed under the proposed Cooperative System.

Otherwise, absent compelling evidence of a problem with current regulation that could not be properly addressed within the existing structure, the Participating Jurisdictions should ensure the CMA and its regulations avoid infringing on, and duplicating, the existing insurance-based regulation of the distribution of segregated funds.

(ii) Establishment of an Investor Advisory Panel

We are pleased that the Participating Jurisdictions are continuing to discuss the possibility of establishing an investor advisory panel ("IAP"), and we are in general support of language to that effect being included in the CMA. Along with the promotion of fair and efficient markets, one of the main tenets of securities regulation is to promote investor protection, and an IAP can provide useful feedback in that regard. However, we urge the Participating Jurisdictions to ensure that the IAP represents real-world investor perspectives, concerns and experiences, rather than the narrow – and often uninformed and unrealistic – views pushed by self-proclaimed "investor advocates".

[1] The submission is available at http://www.advocis.ca/regulatory-affairs/RA-submissions/2014/141208-Submission-to-CCMRS-re-Draft-Legislation-Final-2.pdf.

The best way for the IAP to achieve a balance of perspectives is to ensure that practicing financial advisors are represented on it – after all, of all potential constituents on the IAP, it is only the financial advisor who works directly with consumers on a day-to-day basis. Advisors are the front-facing representatives of the securities sector and they are uniquely positioned to relay the consumer's perspective at the IAP. They are able to provide practical, Main-street insights that lawyers, academics, regulators or dealer representatives simply cannot.

Moreover, the advisors on the IAP should be independent advisors – that is, they should not be affiliated with bank-owned or other large financial institution-owned dealers. This will ensure that they have the freedom to discuss major investor concerns, such as tied selling, undue influence and the commingling of confidential information without conflict of interest or fear of reprisal. They would also represent a much-needed and often underrepresented small business perspective, ensuring that any regulatory policy put forward by the IAP is both effective for protecting consumers and practical for the industry to implement.

(iii) Advisor incorporation

We note that the updated draft of the CMA includes progress towards allowing registered representatives to operate through a professional corporation – we appreciate that regulation-making authority has been granted in this regard, subject to the more stringent ministerial approvals required by section 202(2) of the CMA. However, rather than creating a pathway to incorporation, we believe that the outright ability to operate under a professional corporation should be included in the launch of the Cooperative System.

Incorporation is a modern and efficient business structure that offers many practical advantages and is widely used by small business owner-operators in other professions, such as lawyers, accountants and real estate agents. It promotes the viability of independent advisors by reducing administrative red tape: it makes little sense that dual-licensed advisors must maintain separate books and records for each of their insurance practice and securities practice, particularly as the advisor engages his or her expertise in both sectors to holistically service the same client. Incorporation is also beneficial to consumers as their affairs are dealt with by a corporate entity which provides continuity beyond any individual advisor and greatly assists in succession planning.

In recent years, Participating Jurisdictions have taken significant steps towards allowing for incorporation: in August 2014, the Provincial-Territorial Council of Ministers of Securities Regulation reiterated their commitment to the incorporation project, stating their intention to release draft legislation in the near term. And in December 2014, Alberta (which, at the time of writing, is not a Participating Jurisdiction) passed amendments to its *Securities Act* to accomplish this goal.[2] The self-regulatory organizations of the MFDA (through amendments to its Rule 2.4.1) and IIROC (through its November 2015 white paper that contemplates professional incorporation, amongst other issues) have also taken action to accommodate incorporation.

[2] Alberta passed Bill 5, *An Act to Amend the Securities Act, 2014*, in December 2014. However, the provisions dealing with incorporation have not yet been proclaimed into force.

Clearly, the momentum of policy development across the country is that incorporation will eventually be (and in many cases, already is) permitted, and there appears to be no major policy argument against doing so that cannot be addressed with reasonable safeguards, such as in regards to the liability of the registered representative for actions performed through the corporation. However, due to the piecemeal nature of Canada's securities regulation, wholesale change has been slow to materialize.

Advocis has long argued that securities regulators should level the playing field across provinces and platforms by establishing a permanent, legislated, solution that affords advisors the benefits of incorporation but does not compromise consumer protection. The Cooperative System represents an ideal opportunity to resolve this matter: by codifying incorporation into the Cooperative System's launch, the Participating Jurisdictions could demonstrate how the new entity is ushering in tangible, positive change to securities regulation in Canada – it represents a potential "quick win" for the new regulator, showing the public and non-Participating Jurisdictions how the Cooperative System can move a long-delayed effort forward, definitely and decisively, in a marked departure from the existing fractured regulatory system.

(iv) Duty of care

In regards to a registrant's duty of care to his or her client, section 55 of the CMA now states that "[a] registrant must deal fairly, honestly and in good faith with its clients and meet such other standards as may be prescribed." According to the accompanying commentary, it is the intention of the Participating Jurisdictions to empower the CMRA to make regulations regarding a registrant's duty of care, which could include the imposition of a best interest standard.

Even though any such regulations would be subject to notice and comment requirements and Council of Ministers approval, we believe that it is inappropriate to grant regulation-making authority in regards to the applicable standard of care. The standard of care is a fundamental aspect of a registrant's obligations, and changing that standard absolutely should not be in the regulation-making purview of the CMRA, even with Ministerial-level oversight. Instead, implementing such a change must reflect the gravity of the change and warrants nothing short of deliberative legislative amendment.

More generally, we are strongly opposed to a statutory best interest duty. Our full reasons behind our position are available in our 2013 submission,[3] but the key principles behind our position are as follows:

- **Canada already has a principles-based best interest standard that is well established in common law.** This common law duty serves clients and advisors alike extremely well, as it allows for the consideration of the specific relationship at issue and other important factors in context. Canada's common law best interest duty represents the type of principles-based regulation that regulators should be striving for more broadly.

[3] To view Advocis' 2013 submission to the Canadian Securities Administrators regarding a possible statutory best interests duty, please see http://www.advocis.ca/regulatory-affairs/RA-submissions/2013/Advocis-Response-to-CSA-Consultation-Paper.pdf.

- **A prescriptive statute-based best interest duty would create a variety of new problems.** Supplanting Canada's common law best interest standard with one based in statute would: (i) fail to recognize important differences among retail clients; (ii) impose significant additional costs on financial advisors – and ultimately, their clients; (iii) put well-accepted business models into jeopardy; (iv) detract from principles-based regulation; and (v) cause a misalignment of standards in the financial services industry.

- **The "solutions" of foreign regulators should not simply be imported into Canada, when the underlying problems are not at all comparable.** Although other jurisdictions such as the United Kingdom, Australia and the United States are considering, or have implemented, some form of statutory best interest duty, those jurisdictions have experienced their own unique structural problems that have harmed millions of domestic retail investors. Their regulators consequently faced enormous pressure to react on a grand (if flawed) scale. In contrast, Canada has not experienced similar confidence-shaking problems, so importing foreign regulatory proposals into our domestic market is not in the best interests of Canadian consumers.

Ultimately, this is a major issue that will have significant consequences for the entire securities sector. Regardless of the outcome, this is something that should not be promulgated at the regulation-making level.

Conclusion

We support the Participating Jurisdictions in their work towards establishing the Cooperative System. We encourage the development of an IAP that considers the entirety of the retail investor's perspective, and we believe the input of a professional, independent financial advisor would greatly improve the quality of the IAP's work. We further recommend that the Participating Jurisdictions seize this opportunity to allow for advisor incorporation – a policy which has momentum across Canada – which would show how the Cooperative System can bring about tangible improvement, in contrast to the existing fractured system of securities regulation.

We urge the Participating Jurisdictions to reconsider the CMRA's proposed regulation-making authority. While a platform approach allows for greater flexibility, that flexibility should not be used to effect major change to well-established securities laws, including in regards to segregated funds and the applicable duty of care. The Cooperative System should recognize and respect the primacy of the legislative process in bringing about fundamental change.

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We look forward to working with the Participating Jurisdictions as they take the next steps towards the establishment of the Cooperative System. Should you have any questions, please do not hesitate to contact the undersigned, or Ed Skwarek, Vice President, Regulatory Affairs and Public Affairs at 416-342-9837 or eskwarek@advocis.ca.

Sincerely,

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