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Re: Technology-led innovation and emerging services in the Canadian financial services sector

Dear Sirs/Madam,

We are writing in response to the Competition Bureau's draft public consultation report of November 6, 2017, entitled *Technology-Led Innovation and Emerging Services in the Canadian Financial Services Sector.*

Advocis — Who We Are

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 12,000-plus members, organized in 40 chapters across the country, are licensed to sell insurance products, including segregated funds, as well as mutual funds, and other securities. Advocis members provide comprehensive financial planning and investment advice, retirement and estate planning, risk management, employee benefit planning, disability coverage, and long-term care and critical illness insurance to millions of Canadian households and businesses.

As a voluntary organization, one established by an Act of the federal Parliament, Advocis is committed to professionalism among financial advisors. Advocis members adhere to our published *Code of Professional Conduct*, uphold standards of best practice, participate in ongoing continuing education programs, maintain professional liability insurance, and act in their clients' best interest. Across Canada, our members spend countless hours working one-on-one with individual Canadians on a gamut of financial matters. In addition, Advocis advisors are committed to educating clients about financial issues that are directly relevant to them, their families and their future. Our values and goals are protecting and promoting client service, client education, client freedom of choice, and, finally, of giving top priority to the client's interest as it exists in the totality of the advisor-client relationship. These are also the principles which inform much of our following analysis and argument.

Advocis and Fintech

As a national organization, Advocis has an exceptionally diverse membership base. A number of our members have developed fintech applications and software or launched successful fintech start-ups. Many more have been early adopters of fintech into their advisory practices. What follows reflects the priorities of Advocis' members and their clients.

Executive Summary

Advocis is in broad agreement with the Competition Bureau's 11 Key Recommendations which relate to general issues of fintech[1] policy, with the first four Recommendations on Lending and Equity Crowdfunding, and, with some minor caveats, the six Recommendations on Investment Dealing and Advice. For each of these recommendations, we offer a brief commentary which indicates how the Bureau's policy position will impact financial advisors and their clients, and where we think the Bureau's policy should be amended or revised.

1. The most significant amendment we propose relates to the need to let the comprehensive reform projects – Phase Two of the Client Relationship Model, and the Fund Facts requirements – have enough time to operate in conjunction with one other. We undercut these projects if the regulators do not gather and interpret sufficient data so that a proper evaluation can be made of what additional disclosure, if any, should be required of securities advisors and dealers.

[1] Throughout this submission we will use the portmanteau term "fintech" to refer to the new and innovative financial technology which has been emerging in the financial services sector in the 21st century.

2. We also provide an overview of where Advocis believes the digital advice platform is trending. At the present time, we believe that robo-advisors will more often than not *supplement* the work of professional financial advisors, rather than *supplant* advisors.

3. Accordingly, we take the position that digital advice platforms are not, in their current state, able to function as viable replacements for human professional financial advisors. We therefore strongly encourage regulators across the country to avoid falling into the same trap into which the United Kingdom's financial services regulator fell: that the advice gap which arose from the banning of embedded compensation and the raising of professional standards in the U.K. can be effectively addressed by the advent of robo-advisors and by governmental and regulatory encouragement that those citizens who can longer afford access to product sales and planning advice from a financial advisor can remedy their plight merely by turning to a digital platform. At the present time – and for the foreseeable future – the technology is simply not available for authorities to in good faith position robo platforms as viable, competent and cost-effective replacements for the experienced and professional financial advisor *qua* natural person.

4. This human aspect of the distribution of financial advice raises the issue of the traditional relationship of the advisor and client *qua* natural persons. In particular, we refer to the need of most Canadian households to have a have a long-term relationship with a financial advisor who is qualified to deliver the forms of advice which fall under what Morningstar Investment Management and Morningstar Canada label "gamma." We believe that any discussion of reforms which will impact the ability of how consumers may elect to pay for financial advice, or even access advice to begin with, need to conceptualize financial advice in a more comprehensive, holistic manner. The financial advice that most Canadians want and need is about much more than asset allocation during their 30s and 40s. Truly professional and truly valuable financial advice goes far beyond the chasing of alpha or beta.

5. Many fintech observers express caution about the possibilities for fintech-enabled fraud – e.g., the cautionary admonition to "think of a Ponzi scheme on steroids." To prevent the misuse of technology that would enable fraudsters to deploy bots which masquerade as legitimate fintech applications or firms, Advocis recommends that a registration system for fintech applications and platforms be implemented. The basis of this system would be a regulatory-issued reference number, similar to what the Canada Revenue Agency uses for registered charities. Consumers would be able to verify that the fintech

firm is in fact the "owner" of that registration number. The number could be required to be displayed on every item of promotional material intended for and correspondence with prospects and clients.

6. Finally, given that the draft report comes from the Competition Bureau, we have felt it appropriate to include a section on Pierre Lortie's recent commentary on the negative consequences which will be felt by ordinary Canadians – as well as our mutual funds sector – in the event that practice of embedding third party compensation is banned in the distribution of investment funds by one or more members of the Canadian Securities Association. Lortie's argument has received far too little attention from securities regulators, presumably because the anti-competitive effects of a commissions ban are not directly within their regulatory purview. We urge the Bureau to take Lortie's warnings seriously.

We also offer a number of policy recommendations, which range from the macro-regulatory level to the specifics of suitability requirements for securities transactions. We offer and explain these recommendations as they arise in the context of the recommendations made by the Bureau. In summary form, they may be categorized as follows:

General regulatory issues

- The development and governance of Canada's fintech sector can be facilitated through the application of a core set of regulatory concepts: that regulation be proportionally-based, technology-neutral, principles-based, and directed towards the functions of the intermediary.
- Canada should develop a national fintech strategy and committee.
- To promote fintech, regulators should promote collaboration between regulators and firms.
- Regulatory expectations of digital investment platforms must address the "digital dimension."

Fintech, financial advisors and clients

- Regulators must understand that current robo-advisor platforms are not a substitute for a long term relationship with a professional financial advisor.
- Regulation should not be based on the premise that digital investment platforms are moving toward supplanting financial advisors.

- Regulators must recognize the importance of gamma: full financial advice over time.
- Regulators should develop a better understanding of digital investment platforms and their relation with advisors and dealers – and with the consumer interest.
- Regulators can foster competition and positive consumer outcomes with a more comprehensive focus on the advisor-client relationship.

Improved reporting and disclosure outcomes for consumers, and financial literacy

Fintech can:

- promote price transparency and plain-language disclosure, and
- lead to improved levels of financial literacy and better client understanding of CRM2 reports; and
- eventually make bespoke reporting and disclosure scaled to a client's own level of financial literacy a reality.

Improved range of choice, easier access, and better decision-making outcomes for consumers

- Regulatory requirements should evolve with fintech developments in personal identity and information verification.
- Open APIs are poised to transform the financial services sector.
- Open APIs will promote account switching and enable rapid funds transfers, which will lead to more competition and innovation.
- Open-access fintech will facilitate sophisticated "comparison shopping" for consumers, but stringent standards will be needed to bring to market API-driven comparison tools for customers.
- Fintech can improve the client onboarding process and fulfillment of Know-Your Client (KYC) and Know-Your-Product (KYP) requirements.

Fintech-specific regulatory issues

Regulators should:

- establish the requirement for a designated "regtech" individual;
- identify barriers to fintech entry attributable to regulation;
- remove requirements on digital investment platforms which inhibit their ability to grow and compete with traditional intermediaries—such as the agent for service requirement;
- plug existing regulatory gaps with a fintech-specific registration system; and
- adjust the current securities passport system to make it fintech-friendly.

Finally, looking much further ahead, regulators should prepare for artificial intelligence and the eventual "black swan" fintech disruption of industry and regulation.

Part I. Advocis' Responses to the Competition Bureau's Key Recommendations

Throughout this submission we offer comment on those aspects of the recommendations which we believe to be particularly salient for financial advisors and their clients.

Recommendation 1
Regulation should be technology-neutral and device-agnostic.

Advocis agrees. Prescriptive rules on how an individual or corporate intermediary should comply with a regulatory or legal policy goal are almost always drafted with an eye to the currently available technology. For most of the twentieth century, the basics of commercial law were relatively stable. For example, until the advent of the fax machine, much of contract law dealing with when an offer is said to have been made or accepted was unchanged since the nineteenth century. Since the advent of digital technology, however, regulators and courts have been struggling to keep pace with technological change. Somewhat unfortunately – at least from the perspective of our domestic technological innovators — Canadians still routinely engage in commercial transactions in which the product or service provider requires a holographic or so-called "wet" signature (that is, a signature done in person with a pen) as evidence of agreement or consent.

Regulatory requirements should evolve with fintech developments in personal identity and information verification. A common requirement in retail financial services is the verification of one's personal identification and the collection of one's personal information on an in-person basis, typically through a face-to-face conversation. These legal requirements or company policies were perfectly sensible when for practical purposes almost all transactions occurred in-person at a retail branch. However, the ubiquity of the Internet and continuous improvements in mobile devices and applications have irrevocably altered how many consumers prefer to access retail financial services. Yet the all-too-common requirement for a wet signature acts as a regulatory barrier which needlessly prevents the widespread adoption of convenient and sufficiently secure new digital signature technology.

Accordingly, Advocis supports the Competition Bureau's call for technologically-neutral policies. Canadians need and deserve regulation which not only accommodates today's technology but does not function as a barrier to either innovative new technology or yet-to-be developed applications.

Recommendation 2
To the extent possible, regulation should be principles-based.

Advocis agrees. Regulation should be based on principles which lead the regulated intermediary to an expected outcome, rather than on strict rules which dictate how to achieve the desired outcome. Regulations that prescribe with procedural exactness *how* a person or firm must verify a piece of data, e.g., a consumer's identity, will limit the innovation of faster and less expensive modes of verification – such as remote identity verification through third-party sources or biometric applications.

Principles-based regulation (PBR) can afford regulators the flexibility to issue guidance which will still lead to the desired policy outcomes even as the technology of the day evolves. For example, a PBR approach to the problem of consumer identification would not set out an exhaustive list of specific and acceptable means of consumer identification; rather, it would require that that the financial intermediary be obligated to verify a consumer's identity through demonstrable diligence, such as by way of a sufficiently robust technological method which fulfills broadly conceived regulatory criteria designed to maintain sufficient levels of consumer protection. Properly drafted, monitored and enforced PBR will still protect both traditional and new policy goals, while better allowing for the timely implementation of new fintech applications, the development and deployment of which might otherwise be prevented by a rules-intensive prescriptive regime,

Recommendation 3
Regulation should be based on the function an entity carries out.

Advocis supports the Competition Bureau's call for function-based regulation. As much as practically possible, regulation in the retail financial services sector should be based on the actual tasks and functions carried out by a financial intermediary, and not on its notional legal status or corporate/organizational form. For example, if a retail chartered bank and a fintech start-up both engage in an identical consumer-focused activity, such as the distribution of mutual funds, then each should operate under essentially the same regulatory requirements in regard to the activity of fund distribution. Functionally-based regulation can help ensure that (1) all financial intermediaries shoulder as much as possible an identical regulatory burden, and (2) all consumers enjoy the same protections, regardless of whether the service provider is a retail bank or a fintech start-up.

Recommendation 4
Regulators and policymakers should ensure regulation is proportional to the risks that the regulation aims to mitigate.

Advocis agrees with the general principle that regulation should be proportional to risk. While much regulation in this area deals with requirements for deposit-taking institutions and is therefore removed from the ambit of Advocis' immediate regulatory concerns, Advocis believes that the principle that a costs entailed by a piece of regulation should be proportionate to the risks it seeks to address and eliminate (or at least mitigate) is a sound one, and too often ignored by securities regulators.

<u>The development and governance of Canada's fintech sector can be facilitated through the application of a core set of regulatory concepts</u>. This principle of proportional regulation, together with the requirements that regulation should be technology-neutral, principles-based, and directed towards the functions of the intermediary, can be used to help ensure that a fintech entrant can compete on a more level playing field with an incumbent entity offering the same service.

Advocis believes that the application by regulators of an ensemble of regulatory principles – proportionality, tech-neutrality, PBR in content and functional in approach – will also greatly reduce the risk of regulatory arbitrage.

Recommendation 5
Regulators should continue their efforts to harmonize regulation.

Advocis strongly supports the policy goal of national harmonization. While in the securities sector much has been done to harmonize regulation across Canada, the Competition Bureau correctly recognizes that among the inter-jurisdictional differences which still remain are several which will continue to inhibit the development of fintech in Canada, primarily through an unnecessary increase in a firm's compliance burden. Our patchwork of provincial and federal laws and regulations continue to make fintech firms' compliance with securities law slow, costly and unduly difficult: for example, at present, the provincial securities regulators have in place three separate equity crowdfunding exemptions; compounding this problem is the fact that the requirements which a fintech firm must fulfill to qualify for exemptive relief differ according to provincial jurisdictions. Given the recent delay in the advent of the much-anticipated Cooperative Capital Markets Regulatory System, Advocis is pleased the Competition Bureau is addressing the ongoing negative impact of the failure to develop a fully harmonized set of securities laws.

Recommendation 6
Policymakers should encourage collaboration throughout the sector.

Advocis agrees that policy makers – acting in concert with other stakeholders – should act to facilitate collaboration throughout the retail financial services sectors. More collaboration among regulators at all levels could help lead to a unified and internally coherent approach to regulating risk, market conduct and competition, as well as fostering innovation.

Recommendation 7
Policymakers should identify a clear and unified FinTech policy lead for Canada with federal, provincial and territorial expertise to facilitate FinTech development.

Advocis agrees that policymakers – again, acting in concert with other stakeholders – should identify and articulate a coherent fintech policy for Canada, one which pragmatically accepts Canada's constitutional division of powers, but which is nonetheless unified as much as possible across our federal, provincial and territorial jurisdictions. We note that Singapore and Switzerland have created new governmental offices to facilitate the development of a competitive and innovative fintech sector within their jurisdictions.

<u>Development of a national fintech strategy and fintech committee</u>. In Canada, a federal-provincial fintech body could, after proper input and consultations, develop a national fintech policy, after which the body could function as the "policy lead," and as a steering committee or gateway to other regulators and government agencies. It could also coordinate and lead the efforts of CSA members to provide domestic fintech firms with a "one-stop shop" of resources for information and assistance. A requisite condition for such a fintech body would be robust regulatory, ministerial and industry participation – and that participation should include representatives from the financial advisory and planning subsector. Too often the representation on a regulatory committee stops at the level of the dealer firm, and the perspective of the "advisor in the field" is lost and, with it, so is the impact of innovation and regulation on the consumer or client.

Recommendation 8
Regulators should promote greater access to core infrastructure and services to facilitate the development of innovative FinTech services under the appropriate risk-management framework.

Advocis believes that the issue of regulators acting to ensure better consumer access to core financial services is an important one, and deserves careful study and input from all stakeholders. Easier access to core fintech infrastructure – such as bank accounts and the domestic payments system – will be needed if new market entrants are to be able to develop and bring to market new fintech applications. This is especially true when the innovation takes the form of "overlay services" – such as foreign trading and exchange services – to Canadian consumers. When lack of regulation promoting access to existing infrastructure is the reason why firms, either foreign or domestic, decide not to enter our fintech sector, consumer welfare, marketplace competition, and fintech innovation are needlessly but often significantly diminished.

Recommendation 9
Policymakers should embrace broader "open" access to systems and data through application programming interfaces.

Advocis supports policymakers exploring with industry participation the idea of more "open access" to systems and data; this is what is known in the leading open access jurisdiction, the United Kingdom, as "open banking." The U.K.'s competition regulator, the Competition and Markets Authority (CMA) has spearheaded an "open banking" initiative which goes live in 2018 and promises to lead to greater consumer access to financial services and more competition in the banking sector. Although the Competition Bureau does not have the authority to implement a similar program in Canada, Advocis commends the Bureau for using its competitive review to make open access a priority issue for Canadian consumers, and for devoting a substantial part of its consultation paper, *Big Data and Innovation: Implications for Competition Policy in Canada*, to open-access developments in the U.K. and European Union.

<u>**Establishing an open access framework**</u>. We note that open access to consumers' data in Canada will require the development of a new regulatory framework which:

- sets out the conditions under which consumers may express their informed consent,
- establishes an appropriate risk-management framework which clarifies:

- the regulatory authorities to be responsible for monitoring, licencing and other oversight functions,
- the conditions which financial intermediaries must fulfill before open access is granted,
- which industry parties will bear legal responsibility and policy "ownership" of the key legal liability issues, and
- establishes an effective means of consumer redress.

Open-access fintech will facilitate sophisticated "comparison shopping" for consumers. If an appropriate regulatory framework can be established with a sufficient level of industry support in the retail financial services sector, then open access fintech can help consumers significantly. For example, it can overcome their unwillingness or inability to comparison shop for financial products and advice by way of "bespoke price-comparison applications." Such applications are essentially tools which provide price comparisons based on the individual consumer's actual behaviour patterns, preferences and historical usage of financial products and services, and not on the consumer's own and often faulty perceptions of his or her behaviour patterns, preferences and usage. This distinction is significant, since the application can use the insights from behavioural economics to help the consumer essentially overcome his or her own biases.

Such comparison tools will also help promote competitive switching by consumers to those financial products and services which better meet their actual needs.

Finally, by enabling a greater range of financial processes – including more complicated transactions – to be executed in the absence of a physical "bricks-and-mortar" location, or conceivably even a "bricks-and-mortar" branch network – financial services consumers who live in areas with little in the way of market competition will be able to enjoy the greater choice, lower prices, and other competitive benefits.

Recommendation 10 Industry participants and regulators should explore the potential of digital identification to facilitate client identification processes.

Advocis agrees that industry regulators and stakeholders should work together to explore the potential development and introduction of better modes of client digital identification.

Existing digital identification technology could be used by both new entrants in the retail financial services sector and incumbent service providers to reduce the time and lower the costs of customer acquisition. As well, digital identification technology could accelerate the process of switching client accounts, and reduced the costs to both firms and consumers.

Finally, numerous regulatory compliance obligations which require client identity verification could be automated through identity and authentication fintech. Indeed, many Canadians already access Government of Canada services by verifying their identity through SecureKey or through identity verification by their bank, based on their existing unique banking and log-in credentials. Advocis therefore strongly supports exploration of the potential benefits of using digital identification in client identification processes.

Recommendation 11
Policymakers should continue to review their regulatory frameworks frequently and adapt regulation to changing market dynamics (e.g. consumer demand and advances in technology).

Advocis supports in principle the concept of a continuing review of financial regulatory frameworks, if the goal is to reduce the often excessive compliance burdens placed on retail financial intermediaries, including financial advisors, dealer firms and managing general agencies.

In addition, reviewing and updating when necessary applicable laws and regulations so that they better reflect market developments in consumer demand and fintech's response to that demand should lead to better consumer protection outcomes. Obviously reviewing a regulatory framework to ensure it remains relevant in the context of future innovation, yet still achieves its consumer protection objectives in a way that does not unnecessarily inhibit competition is an excessively complicated task.

Part II. Advocis' Responses to the Competition Bureau's Recommendations on Lending and Equity Crowdfunding

Advocis recognizes that small- and medium-sized enterprises are often Canada's key drivers of economic growth, and that their continued success will be crucial to our long-term prosperity. Indeed, many of our members provide advice to the owners and operators of such enterprises, and also run financial advisory practices which in their own right are successful small- and medium-sized enterprises. Many of our members also operate as exempt market dealers and have Accredited Investor clients who needs may require access to exempt market products. Therefore we recognize that equity crowdfunding platforms at present face significant barriers which they must overcome if they are to be successful.

Among these barriers is the often-unaddressed issue of the lack of consumer confidence and trust in the equity crowdfunding platforms – a situation which results, in part, from the uncertainty inherent in the regulatory apparatus governing digital platforms. We are therefore pleased to see that the Competition Bureau has taken this opportunity to review this area of Canadian securities regulation with the goal of ensuring further exempt market innovation which also ensuring investor protection.

Recommendation 1
Securities regulators should continue to provide clarity and guidance regarding the regulatory framework for P2P [peer-to-peer] lending, including the requirements and process to obtain exemptive relief from KYC, KYP, suitability and prospectus requirements, as appropriate.

As an advocate for regulation which permits Canadians to access exempt market securities, provided that the necessary consumer protections are in place – such mandating sufficient disclosure obligations, or the requirement that an investor must be, when appropriate, an Accredited Investor – Advocis supports this recommendation.

Recommendation 2
Consumer protection regulators should ensure their guidance and regulations are technology-neutral and device-agnostic. Regulations should be written to achieve principles rather than to prescribe *how* those principles are met.

Advocis supports this recommendation, based on the reasons provided in our responses to the Competition Bureau's Key Recommendations 1, 2, 3 and 4, as set out above.

Recommendation 3
Securities regulators should continue to harmonize their approach to prospectus exemptions for innovative business models, including P2P lending and equity crowdfunding, to ensure differences in their laws do not unduly inhibit competition and innovation.

Advocis, as an advocate for regulation which ensures Canadians can access exempt market securities, provided, again, that the necessary consumer protections are in place, supports this recommendation.

Recommendation 4

Regulators contemplating "sandboxes" should look to other jurisdictions, such as the UK and Australia, for best practices and lessons learned with respect to FinTech lenders.

Advocis supports this recommendation, provided that regulators bear in mind that foreign jurisdictions developed their regulatory sandboxes and accompanying best practices as responses to their own unique regulatory problems. Thus the "lessons learned" from foreign jurisdictions may be irredeemably domestic in their nature and non-transferable to Canada's federal, provincial or territorial jurisdictions. Ultimately our regulators must develop their regulatory sandboxes as responses to our own uniquely local problems.

As well, the expertise of our own regulators should be taken into account – for example, the expertise of Quebec's Autorité des marchés financiers in dealing with derivatives securities, or of the Alberta Securities Commission in regulating certain securities and registrants in a manner appropriate for the raising and trading of capital in the oil and gas industry.

Part III. Advocis' Responses to the Competition Bureau's Recommendations on Investment Dealing and Advice

Given the overlap in the subject matter of Recommendations 1 and 2, we have combined our comments into a single response.

Recommendation 1

Regulators should continue their efforts to increase price transparency and plain-language disclosure. Prices for advice should be clear and easily understood by Canadians. Fees should be presented up front (i.e. in advance of purchase) and consumers' attention should be drawn to these fees.

and

Recommendation 2

Regulators should continue their financial literacy and consumer education efforts. In addition, consumers should be encouraged to ask about the fees they pay and to shop around. Price transparency in the MER and other fees should be made clear prior to purchasing a product.

Price transparency and plain-language disclosure at or before the point of sale: Advocis agrees. Both the point-of-sale Fund Facts disclosure and the final phase of the Client Relationship Model 2 (CRM2), have been in the marketplace for too brief a period to allow for accurate measurement of their combined impact on dealers, advisors and consumers. Advocis would suggest that at least 36 to 48 months of operation, with minor adjustments as needed by CSA members, will provide a rich enough data set to determine whether and what kind of additional disclosure may be needed.

Disclosure of the management expense ratios (MER): Advocis is in agreement with the Bureau regarding MER disclosure. Simply put, all components of the MER should be set out in plain language. Such disclosure would include commissions, operational expenses, taxes, and regulatory fees. We note here that the Competition Bureau has included in Recommendations 1 and 2 policies which address essentially the entire financial services industry as well as a narrower point about MERs. It may be worth stating that MERs are a mutual fund-specific ratio, and we query whether the identification of a single product is perhaps counter-productive to a general policy discussion of the overall consumer interest.

For example, every securities portfolio has a cost structure, and a mutual fund's embedded compensation (the "trailer fees") are not unlike the "professional fees" of a fee-based account, the "referral fees" of a portfolio manager, the "embedded commission" within a guaranteed income certificate or a bond, as well as several other forms of compensation currently used in the securities industry. We should pull back the narrow focus on mutual funds and broaden it to include the consumer's bottom line: *any* dollar taken from any investment has exactly same impact on return, no matter what label may be applied to the manner of compensation.

Encouraging consumers to ask about their fees and charges: Advocis agrees that both prospects and clients should ask all necessary questions to ensure that they fully understand the fees and charges they will pay to an advisor and to a dealer firm. We would therefore encourage the Bureau to inquire of other regulators and self-regulatory bodies if they routinely encourage Canadians to "comparison shop" among accountants, lawyers, engineers, dentists, veterinarians, etc., and to conduct that exercise primarily or solely on the basis of the service provider's fees. We believe that the present focus on fees comparison is unfortunately eclipsing what the real focus of consumers should be: ensuring that they receive "good value for the money spent." Costs, and cost comparisons, will be a major component of this revised focus, but certainly not the only one. (We will have more to say on this issue in our discussion of gamma, below).

Regulators can foster competition and positive consumer outcomes with a more comprehensive focus on the advisor-client relationship: Advocis therefore recommends that the narrow focus on fees be replaced with a broader focus on advisory skills, advisory services, and demonstrable historical evidence of having provide to satisfied clients professional-quality investment and/or insurance advice, products and services, as well as other forms of financial advice and planning. Investment dealers and advisors do in fact compete on both price and non-price elements, including the fees charged, the quality of customer service (e.g., the availability of the advisor to answer questions, the open office hours of their practice, etc.), the time and manner in which the advice is delivered, and the success of the investment portfolio or the investment's performance based on the advice proffered.

Fintech can lead to improved levels of financial literacy and better client understanding of CRM2 reports: With regard to CRM2, the promise of fintech is starting to be realized. At the recent regulatory "hackathon" – entitled RegHackTO – organized by the Ontario Securities Commission, a team from a leading software company demonstrated that it is possible to configure CRM2 disclosure information in a machine-readable format and provide it with an open API.

This means that a standard fintech application can be developed to perform analytics on the information and then create reports specifically tailored to the level of financial literacy of the report's consumer end-user. With such fintech, clients will no longer be limited to the "static" data reportage provided to them by their financial institution. Instead, they will be able to receive on demand up-to-date reports and dynamically track performance over any time period they desire.

The development through fintech of bespoke reporting and disclosure scaled to a client's own level of financial literacy will become a reality. Advocis notes that given the asymmetry of information inherent in many client-institution relationships, in order for price transparency to be effective, the client's fees, charges and costs should presented in a clear and understandable way, one which takes into account the individual's own level of financial literacy. Advocis believes that fintech products can help promote greater financial literacy among consumers and that policymakers should explore ways to leverage fintech to achieve this outcome.

Regulators must recognize the importance of gamma: full financial advice over time: Investors who use financial advisors are better off over time. In short, "advice matters," according to academic Claude Montmarquette, who co-authored *The Gamma Factor and the Value of Financial Advice* with Nathalie Viennot-Briot of the Montreal-based Centre for Interuniversity Research and Analysis of Organizations

(CIRANO)[2]. Montmarquette's study relied on a survey by Ipsos Reid for Power Financial Corporation of 487 households which had chosen and retained a financial advisor and of 1,097 households which did not have an advisor.

The key factors that affect the probability of a Canadian household having an advisor related to levels of income, savings capacity, age, educational level and financial literacy. But once an advisor is selected, it is the "gamma" factors of discipline and increased savings rate that are crucial features associated with *valuable* financial advice. Gamma seeks to measure the value of financial advice, as opposed to market returns (beta) or market outperformance (alpha). Montmarquette's study found that that the advised households accumulated 290% more assets on average, over 15 years, than the unadvised households.[3]

Another indication of gamma's importance lies in the fact that that many Canadians need *ongoing* access to an advisor who has the skills and experience to properly understand and respond to *all* of their financial needs. That is an advisory task which goes well beyond, for example, securities selection and asset allocation advice during the asset-accumulation stage. Indeed, of critical importance to the retiring Boomer generation is advice prior to and during their post-retirement period when they begin drawing down on savings and decumulating assets. In short, the truth is that digital investment platforms are at present not capable of delivering gamma to Canadians. This is truth which must inform any regulatory reform initiatives in the financial services sector.

Recommendation 3

Regulators should encourage the use of technology to facilitate account switching. The use of APIs may facilitate the creation of rich databases of price and fee information to facilitate shopping around. Similarly, the use of APIs to access consumers' portfolio information can help make switching easier. Regulators should reduce barriers to switching by allowing and encouraging firms to leverage technology such as e-signatures and digital identity verification to facilitate client onboarding.

[2] The Investment Funds Institute of Canada FIC. Presentation by Claude Montmarquette, "The Gamma Factor and the Value of Financial Advice." Toronto: November 7, 2016.

[3] See Claude Montmarquette and Nathalie Viennot-Briot, *The Gamma Factor and the Value of Financial Advice*, CIRANO Working Paper, August 1, 2016. Montreal: Centre interuniversitaire de recherche en analyse des organisations. Online at http://www.cirano.qc.ca/files/publications/2016s-35.pdf or https://www.ific.ca/wp-content/uploads/2016/11/The-Gamma-Factor-and-the-Value-of-Financial-Advice-November-7-2016.pdf/15371/+&cd=4&hl=en&ct=clnk&gl=ca.

Open APIs are poised to transform the financial services sector: Application programming interfaces or APIs are technical rules allowing pieces of software to interact by enabling us to share information, for example about our location. They are the hidden technological drivers behind many of the digital services we use on our smartphones and computers, such as applications like Uber, Facebook, and Google Maps.

API initiatives will allow consumers to access and compare current accounts using their own personal transaction data. In particular, open APIs can new opportunities afforded by the timely introduction of open data standards will enable change that is potentially very wide reaching. Under the right regulatory approach, and with support from the major stakeholders in Canada's financial services sector, consumers and intermediaries will quickly realize significant benefits from the new forms of client data integration now possible with new technology change. There is already a very active and growing fintech community which has been developing and introducing new products using existing digital technology. This could enable bank consumers to grant access to their bank data.

A fundamental barrier to competition arises from the fact that even when new entrants and smaller incumbents introduce a new product, it often takes a significant time to build and maintain consumer relationships. But API technology means that customers can enjoy greater responsiveness and lower prices from enhanced competition, which may be able to reduce the current position of advantage held by banks. Data integration can function as an incentive for banks to more aggressively compete with one another and make the market more attractive to new entrants in the banking, securities and insurance sectors, and foster further innovation.

Stringent standards will be needed to bring to market API-driven comparison tools for customers. Advocis encourages regulators to explore developments that will improve a customers' ability to access, assess and act on information that will help them find the best products and services for them. Clearly, the development of a safe and secure open API system in Canada will be a daunting technical task. The problems entailed by data integration will have some significant implementation costs, in particular for the banks. But the benefits to consumers will more than justify these costs. Moreover, our relatively small concentration of retail chartered banks means that reaching an industry-agreed-upon solution may well be easier for Canada than for many other jurisdictions, such as the United States. Putting retail consumers in control of their financial arrangements through open APIs will make the financial services sector work better for Canadians.

<u>**Open APIs will promote account switching, which will lead to more competition and innovation**</u>**:** It is a truism that a key element of a properly competitive market is the ability of consumers to easily switch between suppliers of a good or service. When it is easy for consumers to switch, they are more likely to do so when they are aware of more favourable offer. In response, a firm must ensure its prices and services deliver value to its customers: in the absence of that value, the firm risks losing those customers to the competitor. So, in a functionally competitive market, firms are incentivized toward continuously innovation, in order to and attract a larger share of consumers and stay ahead of the competition.

Account switching has long been a task that is difficult for both firms and clients to execute. First, there is the effort involved in switching financial advisors: finding and comparing prices, determining what services are offered and ascertaining their quality, the time needed to set up new accounts, the cost and time entailed by transferring assets or accounts (and the potential costs or penalties involved in selling investments early or, if necessary, cashing out), and any applicable account closure fees. As well, taxation concerns can also drive account changes. For example, in-kind transfers are only permitted if the receiving institution is able to carry the existing security within their structure. And, on occasion, investors don't switch in order to avoid paying taxes on embedded capital gains.

In light of these complexities – which go beyond mere information-gathering and can require a sophisticated analysis of the client's portfolio and tax position – it is imperative that fintech firms be enabled to realize their potential for radically reducing the resources expended in account switching. But to do that will require the creation of an open API system in Canada.

<u>**It is time to let fintech and APIs enable rapid funds transfers**</u>**:** At present, advisors who transfer funds from an account to their firm often experience unduly long wait times. Indeed, manual transfers can take up to a month to complete. In terms of the governance of "digital account switches and transfers," the rules of the Investment Industry Regulatory Organization of Canada (IIROC) mandate recourse to the Account Transfer Online Notification system (ATON), under which the maximum time experienced is usually 10 business days. Operated by the Canadian Depository for Securities Limited, ATON automates the exchange and confirmation of requests for transfer and asset list details between the deliverer and receiver of account transfers. ATON users include broker-dealers and other regulated financial firms such as banks, trust companies, intermediaries, investment fund dealers, insurance companies and credit unions.

One barrier to fintech associated with ATON lies in the fact that while the process is completed through computer networks, many institutions still require a paper form to be filled out and returned to effect the transfer. Moreover, some assets may not even be permitted to be switched, either because the product itself is proprietary and not offered by competing advisors (a common example is a guaranteed interest certificate), or because the accepting advisor does not sell those types or lines of investments. In these cases, consumers must resort to a manual account transfer, which involves cashing out investments at one institution, and then depositing and re-purchasing investments at the receiving institution. Moreover, various limits and hold periods can further slow this process of manual transfer.

While 10 days may not seem like a particularly long period of time to effect a detailed series of financial transactions, and the costs associated with the transactions may not seem particularly large in the context of saving perhaps thousands of dollars over the life of the investment, the "truth" for the consumer is that ours is a digital age: consumers now expect nearly-instantaneous execution of a transaction upon the clicking of a few buttons. Many in the Millennial generation may be deterred by the waiting period and the requirement to attend an office or fill out and fax or mail paper forms. This frustration will be especially acute when the consumer is registering for an online-only service and has to date completed most or all of his transactions online.

Regulation should promote the use of e-signatures and digital identity verification: Advocis agrees that industry regulators and stakeholders should work together to explore the potential development and introduction of better modes of client digital identification. Existing digital identification technology could be used by both new entrants in the retail financial services sector and incumbent service providers to reduce the time and lower the costs of customer acquisition. As well, digital identification technology could accelerate the process of switching client accounts, and reduced the costs to both firms and consumers. Finally, numerous regulatory compliance obligations which require client identity verification could be automated through identity and authentication fintech. Indeed, many Canadians already access Government of Canada services by verifying their identity through SecureKey or through identity verification by their bank based on their unique existing banking and log-in credentials. Advocis therefore strongly supports exploration of the potential benefits of using digital identification in client identification processes.

Fintech can improve the client onboarding process: A digital onboarding process can be a better way of ensuring that "all the boxes have been checked," all the necessary questions put to and understood by the client, and all the answers provided. Depending on the quality of the questionnaire and robustness of the process , thee onboarding process might be entirely automated and done electronically, thereby attracting more technologically-savvy consumers and those less inclined to meet with an advisor in person.

Recommendation 4
Regulators should continue to collaborate with robo-advisors on the design of regulation to facilitate entry of these low-cost alternatives to traditional advice—for example, by providing clarity and certainty in interpretation and expectations. Regulators should review their regulations periodically to ensure they do not place unnecessary burden on market participants.

Regulatory expectations of digital investment platforms must address the "digital dimension": The International Organization of Securities Commissions (IOSCO) reports that to date the regulatory focus on robo-advisors is typically in the form of rules setting out requirements for general product suitability, know-your-client, registration, training, disclosure, record-keeping and compliance. Only a few jurisdictions have also introduced specific rules or guidance to address the "digital dimension" of robo-advice and other forms of automated online advice and planning. IOSCO notes that the major digital risks associated with robo-advisors are:

- risks of errors in algorithms,
- risks of overly complex or overly simplistic algorithms, and
- risks of static client information.

Baseline requirements of regulators. Advocis believes that regulators must play a key role in ensuring that new technology is used in a way that serves the consumer interest. One way to do that is to ensure that digital investment platforms are both safe and accessible. A second, equally important way is that governments and regulators do not assume digital investment platforms to satisfactory replacements or substitutes for the traditional financial advisor.

Collaboration between regulators and firms: If Canada wants to become a leader in the fintech sector, it should learn from the experiences of other jurisdictions, including the United Kingdom and Singapore:

- the U.K.'s Project Innovate combines its innovation hub with a specialized staff unit to provide feedback to firms developing automated advice models; and

- Singapore's Smart Financial Centre is dedicated to facilitating collaboration among a diverse range of stakeholders: new entrants, financial institutions, academia and think tanks, legal professionals and government agencies.

Both jurisdictions have also adopted regulatory sandboxes for experimentation.

Regulatory sandboxes: At present, the Ontario Securities Commission and Québec's Autorité des marchées financiers are working closely with the fintech community to help innovative fintech firms enter the marketplace, including creating sandboxes to allow these businesses to engage in regulated activities for a test period without having to comply with certain securities requirements. For example, the OSC's Project LaunchPad work with robo-advisors illustrates how start-ups can productively engage with a branch of a regulatory agency. Sandboxes help fintechs by allowing them to experiment and help regulators by allowing them to monitor the fintechs, understand the unexamined barriers and watch for risks that may need to be addressed. The OSC LaunchPad initiative encompasses both concepts: it provides informal guidance to fintechs at an early stage about how securities regulation applies to them, and offering flexible approaches to regulatory requirements.

Developing new regulations: Regulations need to be written in such a way that traditional advisors firms may utilize the technologies. This means that established firms which by definition operate outside the regulatory sandbox environment should be able to enjoy the same relative "light touch" regulatory approach that start-ups do.

Recommendation 5
Regulators should consider providing firms with more freedom to automate additional processes, including analysis of KYC information and portfolio matching for suitability and portfolio rebalancing. The risks related to recourse, redress and enforceability can continue to be managed by designating responsible individuals within a firm.

Advocis agrees. Improving efficiencies in the process of managing many portfolios through the clustering of risk profiles of similar clients should be permitted. The process should be managed by a designated individual within the firm.

Should the role of the trustee be automated? If so, by who? Digital investment platforms are not only attempting to reduce the role of advice. Some fintech firms, such as the robo platform Wealthsimple Financial Inc., are now automating the role of the trustee. We query whether the Competition Bureau should examine the appropriateness of using an independent third party trustee service instead of the company-owned technology service trustee. The issue we believe should be explored is this: if small robos and other digital platforms follow Wealthsimple and enter the trustee administration space, what will be the impact on consumer protection? And will tax and investment reporting be compromised?

<u>Fintech and improving the process of satisfying Know-Your Client (KYC) and Know-Your-Product (KYP) requirements</u>**:** Robo-advisors like to advertise their competitive advantage – their speed and convenience, which are largely based on doing remote online transactions. And while suitability, KYC and KYP obligations are important consumer protection measures, the manner in which they are currently expected by regulators to be carried out is creating a barrier to competition for robo-advisors. Traditionally, advisors meet the KYC requirement and perform suitability assessments through conversations, meetings and phone calls with clients. Robo-advisors, on the other hand, use online questionnaires and text-based chats to collect KYC information.

Here we would suggest that regulators look to the United Kingdom, where the Financial Conduct Authority (FCA) has issued guidance to address "not-in-person KYC information collection." The FCA places a clear onus on questionnaires and their design to ensure they collect sufficient information to understand the client. In Canada, our securities regulators have generally embraced this way of conducting suitability analysis, and the CSA issued guidance in 2015 to online portfolio managers setting out expectations for the collection of KYC information online.

Fintech has recently shown much promise in this area: at the recent RegHackTO event – organized by the Ontario Securities Commission's Project LaunchPad – the winning team, Existence Labs, focused on proof-of-compliance within the KYC process, and was able to create a digital trail of unforgeable cryptographic signatures and timestamps, all of which amount to irrefutable time-based evidence of compliance. (Notably, the team leader of Existence Labs earned a seat on the OSC's Fintech Advisory Committee).

Another firm at RegHackTO developed a blockchain-based application which allows investors to store, maintain and share one or more suitability profiles with deal firms. This application transforms the suitability information stored by dealers from something that is static, repetitive, potentially inconsistent and possibly out-of-date, into a powerful tool for investors and dealers and which reduces dealers' costs.

To promote fintech, establish the requirement for a designated "regtech" individual: Advocis supports the idea of a designated individual bearing responsibility and encourages regulators to look to Australia for an idea of how develop a fintech regime based on mandatory designated individuals. In 2016, the Australian Securities and Investments Commission (ASIC) released *Regulatory Guide 255 – Providing Digital Financial Product Advice to Retail Clients*. This document provides guidance on the collection of KYC information via online questionnaires and outlines ASIC's expectations for how firms should monitor their systems to ensure they meet all applicable suitability requirements.

Regulatory Guide 255 states that a licenced advice provider must ensure there is a person within their licensed advisory firm who understand the algorithmic technology employed in providing the advice *and* is able to properly review the advice generated. While this individual is not required to review every single transaction or planning decision, he or she must be available to ensure the consumer protection standards of suitability, KYC and KYP are being met. *Regulatory Guide 255* requires that regular verifications be conducted on the algorithms and on the recommendations issued by the firm's software. Finally, the guide sets out clear expectations regarding how the firm is to filter out clients for whom robo-advice is not appropriate, and of the kind of information which clients should receive which explains the limitations of the robo-advice they've been provided with.

Recommendation 6

Regulators should continue to promote the existing passport system to facilitate Canada-wide market entry by FinTech companies, and continue efforts to ensure such systems adapt and remain relevant in an increasingly digital world.

Advocis agrees with this recommendation.

Identify barriers to fintech entry attributable to regulation: The regulation of financial services in Canada is fragmented, overlapping and unduly complex. In a regulatory ecosystem with thirteen provincial or territorial jurisdictions, plus a federal one, it is often the case that even if the majority of provinces attempt to promote innovation in a particular sector or industry, a firm which operates across all of the jurisdictions is incentivized to simplify its compliance program by adhering to the most restrictive regulatory regime in which it operates. The firm's decision is driven by the determination of what approach will ultimately be less expensive to the firm: the cost of applying one set of restrictive compliance regimes on a nation-wide basis, or the cost of applying up to thirteen different compliance regimes.

Remove requirements on digital investment platforms which inhibit their ability to grow and compete with traditional intermediaries: While registration itself does not present a significant barrier to entry for robo-advisors, a number of requirements imposed on registered investment dealers can create unintentional barriers to small and or start-up fintechs. To meet their requirements under securities law, robo-advisors must a have an agent-for-service in each province where they provide services to clients, as well as pay registration fees in those provinces. The agent-for-service requirement is to ensure that a natural person is present to accept service of process should the advisor firm be sued in that particular province.

An example of regulatory cost-inflation – the agent-for-service requirement: As robo-advisors, digital platforms do not realize a competitive advantage from maintaining a physical human presence in every province in which they operate; they do not need a human person to offer a physical point of sale or to facilitate identity verification for anti-money-laundering purposes. Requiring a robo-advisor, which is based on a business model of keeping costs as low as possible by leveraging technology which may be operated from a single location or in "the cloud" to maintain multiple human employees across Canada is a needless regulatory barrier.

Plug existing regulatory gaps with a fintech-specific registration system: Advocis believes that it is critical that all fintech firms be registered somewhere in Canada. At present, a financial advisory Artificial Intelligence bot which does not offer for sale any financial products, and only sells advice, does not have to carry a license or be registered *anywhere*. In the absence of regulation which will address this issue, we can eventually expect a wave of online fraud and potentially significant consumer harm, once the technology is available to enable bots to convincingly pose as legitimate and sophisticated digital platforms.

To prevent the misuse of technology that would enable fraudsters to deploy bots which masquerade as fintech applications or firms, Advocis recommends that a registration system for fintech applications and platforms be implemented. The basis of this system would be a regulatory-issued reference number, similar to what the Canada Revenue Agency uses for registered charities. Consumers would be able to verify that the fintech firm is in fact the "owner" of that registration number. The number could be required to be displayed on every item of promotional material intended for and correspondence with prospects and clients. Currently, nothing of this nature has been implemented.

Adjust the current passport system to make it fintech-friendly: Given provincial jurisdiction over securities regulation in Canada, the "passport" system has been developed to provide a much-needed measure of regulatory harmony between most of the provincial securities regulators and to enable firms to raise capital more quickly and easily. A fintech-based passporting system such as the one outlined in the CSA's guidelines for regulatory sandboxes could be designed to run longer than the exemption period granted by the regulator in the province which originated the exemptive relief. This would mean that a passport for a CSA-approved fintech platform could operate for a much longer period of time across multiple provincial jurisdictions and – if our fintech partnership agreements with the United Kingdom, Australia and other jurisdictions permit it – enable the platform to more quickly establish permanent operations in other countries. Advocis encourages further exploration of this concept.

Part IV. The Impact on Competition in Canada's Securities Sector From Banning Embedded Compensation

With regard to the possible banning of embedded compensation on securities such as mutual funds and reduced competition, we would refer to Pierre Lortie's comments on the banning of commissions working to the advantage of large, well-entrenched and vertically-integrated financial institutions, and to the detriment of smaller, independent dealers and would-be new market entrants. Lortie's argument is nuanced and given that it has been to date largely if not entirely ignored by regulators, we take this opportunity to quote it at length:

> Industry pricing structures tend to evolve until they reach an optimal balance between countervailing forces and, from thereon, remain in equilibrium unless a disruptive shock occurs. This has been the case for financial advice... The fact that [Canadian] "advice channels" have retained the dominant share of mutual fund retail markets *in the face of robust competition from strong competing channels and credible financial-product alternatives constitutes solid evidence of the optimality of the bundle pricing structure for large segments of the retail market*.
>
> The bundling of financial advice with financial products such as mutual funds has a major impact on the structure of the industry, a consideration rarely addressed in the literature and policy debate. The efficiency of the arrangement allows the development and growth of a horizontal industry structure where product manufacturers and distributors are distinct organizations. From an economic and social point of view, *the horizontal industry structure where several manufacturers distribute their financial products through unrelated financial intermediaries is far superior to a vertically integrated structure* where the great majority of financial

> advisers are limited to "selling" the financial products "*manufactured*" by their employer, *in that it promotes market transparency, competition at both the product and distribution levels and a focus on investment performance.*
>
> The corporate interests of independent dealers and mutual fund manufacturers are not perfectly aligned. It is the mutual fund manufacturers′ interest to grow the value of the assets in their funds, which, in practice, means increasing the number of investors. To achieve this objective, mutual fund fees must be set at a level low enough, and structured in such a way as to not to discourage non-affluent investors. For their part, dealers need to ensure that the marginal cost of serving a new retail client is covered. The embedded fees with a trailer-commission approach is an efficient arrangement to reconcile these conflicting objectives since this pricing formula circumvents the main resistance of a large segment of retail investors to invest through the advice channel and provides the dealer with a stable and adequate stream of revenues. *This equilibrium state can be shattered by major changes in the industry structure or by regulations* [i.e., the banning of embedded third-party compensation]*. This has happened by regulatory fiat in the United Kingdom, Australia and The Netherlands* [emphases added].[4]

While the specific recommendations made by the Competition Bureau do not directly reference any of the recently proposed bans on embedded compensation in the sale of mutual funds or other securities — which, after all, is a matter of provincial jurisdiction — Advocis would note that the information asymmetry and principal-agent aspects of the embedded compensation issue are being addressed by a levelling of the playing field between fee-based advisors and advisors who rely on third-party embedded compensation; in specific, this is currently being done through the increased disclosure contained in the mandatory Fund Facts document and the new fees and charges reporting obligations that have recently taken effect under the final phase of CRM2.

[4] Pierre Lortie, A *Major Setback for Retirement Savings: Changing How Financial Advisers Are Compensated Could Hurt Less-Than-Wealthy Investors Most*. University of Calgary, The School of Public Policy. In *SPP Research Papers*, Volume 9,Issue 13 (April 2016). Online at https://www.policyschool.ca/wp-content/uploads/2016/05/financial-advice-lortie.pdf+&cd=1&hl=en&ct=clnk&gl=ca.

PART V. CONCLUSIONS AND NEXT STEPS

Advocis believes that Canadian securities regulators are to be commended for their efforts to embrace fintech through initiatives such as the OSC LaunchPad, the CSA Regulatory Sandbox, the British Columbia Securities Commission's Tech Team and the AMF's FinTech Support Team.

Similarly, the Competition Bureau deserves considerable praise for this draft report, *Technology-Led Innovation and Emerging Services in the Canadian Financial Services Sector.* The report sets out a number of ways regulators and industry stakeholders can improve competition and consumer outcomes in the financial services sector by encouraging the introduction of innovative fintech solutions.

Current robo-advisor platforms are not a substitute for a long term relationship with a professional financial advisor.[5]

The report also makes several recommendations for enhancing competition, including that securities regulators should continue to work with robo-advisors to help facilitate the development of cheap alternatives to traditional advice – in specific, to work "on the design of regulation to facilitate entry of these low-cost alternatives to traditional advice." This should be an area of concern to Canadians and their regulatory authorities. Advocis urges against robo-products being held out as the solution to any advice gap which emerges in the event of a ban on embedded commissions. This "robo-as-saviour" approach has been tried for over three years in response to the advice gap in the United Kingdom and it has failed utterly.

Do not base regulation on the premise that digital investment platforms are moving toward supplanting financial advisors. Advocis is in the unique position of representing the full range of financial advisors, including bank-employed, MFDA-licenced advisors, IIROC-registered advisors, advisors employed by dealer firms of all sizes, advisors who run their own independent advisory practices, advisors who are registered portfolio managers, and so on. At present, we can state that a great many advisors across all distribution channels believe that digital platforms can work *with* advisors, rather than *compete* against them in a zero-sum competition with them. These advisors also believe that the advent of robo-advisors will create competition which will reduce investors' costs. In other words, we should not assume that digital platforms will simply "replace" financial advice. As an example, consider the source of a major competitive advantage for Wealthsimple Financial Inc. The reason why its MERS are

[5] See the discussion regarding gamma in the text related to 1 and 2, above.

lower in comparison to other robo-advice platforms lies in the fact that it has automated the back office compliance and trustee services. These innovative operational advantages place Wealthsimple far ahead of most of its competitors.

As the fintech sector develops, some robo-advice applications and digital investment and insurance platforms will be competing directly with some financial advisors, while simultaneously co-operating with other types of financial advisors. Indeed, digital platforms have been asking advisory firms to introduce clients to them for a number of years.

Better understanding of digital investment platforms and their relation with advisors and dealers – and the consumer interest. Again, the case of Wealthsimple is illustrative of how the fintech industry is developing in Canada. At the time of writing Wealthsimple is running a comprehensive and widely-placed television advertising campaign. It is significant that the campaign's advertisements do not criticize the financial services industry's existing advice channels, such as banks and advisors. In fact, the Canadian Imperial Bank of Commerce recently announced it is in negotiations to "partner" with Wealthsimple. Wealthsimple's decision not to run an advertising campaign which positions itself as a "disruptor" in the retail financial services sector is a direct consequence of its apparent business plan to access new clients through referrals from financial advisors.

Clients of Wealthsimple (or of other robo-advisor entities) can pay an agreed-upon referral fee to the advisor. This arrangement is contingent upon the dealer signing a referral agreement. A referral means the assets leave the dealer firm and thus reduces the value of the dealer, and potentially access to and control of future earnings from client). But from the consumer's point of view, the total MER is reduced, since the portfolio is comprised of index units. The dealer firm is thus placed under pressure by a digital investing platform, while successful advisors are attracted to such platforms as a way of reducing their compliance costs.

Looking much further ahead: Preparing for artificial intelligence and the "black swan" fintech disruption of industry and regulation. Finally, it should be noted that anecdotal reports have been made at recent industry conferences in North America that certain institutions in the United States are suggesting that Artificial Intelligence (AI)-driven applications with natural language capabilities are perhaps closer to fruition than the AI mainstream thinks. While this is not a consensus view, the idea that an "AI financial advisor" could be in the offing is a daunting prospect, one which would have the obvious capacity to *truly disrupt* retail financial services and would immediately necessitate a massive overhaul of our financial regulatory system. At some point, regulators will have to begin preparing for such a "black swan" regulatory disruption.

Next steps: While the Competition Bureau's report did not address insurance, Advocis would be happy to discuss with Bureau representatives how their proposed policies will impact the distribution of insurance advice and products, including life insurance and those insurance products which contain an investment component, as well as financial advisors who are life agents, and their clients.

As well, we would like the Bureau to know that Advocis recently established a Technology Task Force which, among other projects, is currently examining the role of fintech from a public policy and regulatory perspective. The Task Force will welcome any opportunity to assist government and regulatory agencies as they develop public and industry policies.

Should you have any questions about our responses, or wish to discuss any of these issues further, please do not hesitate to contact the undersigned, or Ed Skwarek, Vice President, Regulatory and Public Affairs at 416-342-9837 or eskwarek@advocis.ca.

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