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December 4, 2015

Ken Woodard
Director Communications & Membership Services
Mutual Fund Dealers Association of Canada
121 King Street West, Suite 1000
Toronto, ON M5H 3T9

VIA EMAIL: kwoodard@mfda.ca

Dear Mr. Woodard:

Re: Mutual Fund Dealers Association of Canada
Consultation Paper on Standards for Use of the Title "Financial Planner"

On behalf of Advocis, The Financial Advisors Association of Canada, we are pleased to respond to the consultation paper issued by the Mutual Fund Dealers Association of Canada ("MFDA") in regards to its review of the standards for use of the title "financial planner" (the "MFDA Consultation").

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.

PROTECTING CONSUMERS BY RE-THINKING FINANCIAL SERVICES REGULATION

We agree with the MFDA that there are serious issues with the existing regulatory structure: consumers regularly place their trust in financial intermediaries who boast of professional-sounding titles when, in reality, these titles are not backed by meaningful standards of professionalism and proficiency.

However, we believe that the problem runs much deeper than what is outlined in the MFDA Consultation – the problem is not limited to financial planning, but to the entire scope of financial advisory activities (of which financial planning is just one aspect) that involve retail consumers. The problem is not limited to the mutual funds sector, but permeates all financial product sectors, and also afflicts advisory activities that do not involve the sales of any products at all.

Before delving into the issues, we wish to state clearly that effective regulation must be crafted from the perspective of the consumer – and the reality is that, for the majority of consumers, it is the advisor who serves as their gateway to the financial services industry. So any regulatory initiative that purports to enhance consumer protection must recognize the central role of the advisor-client relationship. And the very best way to do this is to professionalize financial advice in Canada.

Therefore, our submission sets out to accomplish the following:

1. We will explain the **problems with the existing regulatory framework**, including and going beyond those discussed in the MFDA Consultation.

2. We will demonstrate that **financial planning is an integral component of financial advice**.

3. We will explain why **financial planning must not be regulated as a standalone activity** if the ultimate goal is to improve consumer outcomes.

4. We will provide our **comprehensive solution to the problem**, which goes beyond titles, the alphabet soup of designations and product sector silos to truly protect retail consumers.

We are heartened to see that regulators such as the MFDA and governments such as the Province of Ontario are taking a serious look at the regulation of retail intermediaries in the financial services sector – we have long advocated for such reform. We believe that this is a historic opportunity to truly get regulation right and set in place a framework that fundamentally improves the consumer experience. So rather than settling for incremental, narrow and patchwork improvements, it is critical that comprehensive, structural reform be on the table.

1. PROBLEMS WITH THE EXISTING REGULATORY FRAMEWORK

The *ad hoc* development of the regulatory and legal governance of Canada's retail financial sector has resulted in a framework which, while effective and efficient in many aspects, has a number of interstitial gaps – areas of financial activity which lack proper regulatory oversight (or, at times, any oversight at all). It is through these gaps that a number of Canadians' legitimate financial interests are at risk of slipping. While the public should be able to place their confidence in their financial advisor, trusting that he or she meets rigorous standards of professionalism, proficiency and accountability, the reality is that this is not always the case. In fact, the public is exposed due to four major flaws in the existing framework.

A. Anyone can call him- or herself a financial advisor and offer financial advice, including planning.

As pointed out in the MFDA Consultation, across Canada (other than Quebec), anyone, regardless of their training, experience or education, can hold themselves out to the public as a financial advisor, financial planner, investment advisor, or countless other titles. Neither the title of "financial advisor" nor the scope of the work under that title is protected in law, so there is nothing to prevent an unscrupulous, incompetent or merely inexperienced individual from calling themselves a financial advisor and offering what is purported to be financial advice to the public, even if they have no training, experience or financial acumen.

This is an extreme risk which must be addressed; time and again, consumer surveys have shown that most consumers mistakenly believe that titles such as financial advisor are regulated and someone holding themselves out as such has earned the right to do so through education and experience. In professional-style principal-agent relationships, consumers routinely put their faith in the title as a proxy for expertise, but unlike doctors, lawyers or architects, anyone can claim to be an advisor or offer financial advice and planning – which leaves the public needlessly vulnerable to incompetence or outright fraud.

B. Existing regulation focuses on products, at the expense of proper regulatory oversight of the most critical aspect of the retail financial sphere – the ongoing relationship between financial advisors and their clients.

Much of our existing regulatory framework does not reflect the daily reality of how most Canadians access financial advice and planning. This is because existing regulation is largely based on the type of product being sold to the retail consumer. For example, insurance products, mutual funds or other securities are regulated by entities including the Office of the Superintendent of Financial Institutions, provincial insurance regulators or insurance councils, provincial securities commissions, and self-regulatory organizations such as the MFDA and the Investment Industry Regulatory Organization of Canada ("IIROC"). Each regulator has its own standards and requirements, and while they are strong at regulating their member insurance carriers and mutual fund or securities dealers, including regulating the constant product innovation in the industry, they do not have a collective focus on the retail consumer's overall advice-receiving experience.

Considering the issue from the consumer's perspective throws the problem into stark relief: many advisors hold multiple licenses which allows them to provide consumers with risk management and wealth solutions from across the insurance, mutual fund and securities sectors. As a practical matter, most consumers do not conceive of the retail financial services industry as structured in such rigid "silos." Nor should they be expected to understand the legal rules and regulatory processes which have produced our "siloed" model. Instead, consumers work with their advisors to develop holistic financial plans which reflect their circumstances, and not a piecemeal delivery of advice which reflects the regulatory happenstance of how our system developed. Above all, Canadians want assurances that their advisors are professional, knowledgeable and accountable, so that their advisor can provide the complete coverage they need.

Most consumers are not particularly interested in knowing that product *x* comes from the insurance universe and product *y* comes from the mutual fund universe – and as product features converge, it is increasingly difficult for consumers to tell them apart. But, in the current regulatory framework which is focused so closely on product sales, it is often the case that the advisor/client relationship is not governed by a single regulatory entity, but by a combination of them. The result is that the protections which consumers do receive vary widely, as they are based on the sector from which the underlying product originates. We have seen the importance of this distinction coming to light if problems arise, leaving consumers confused and disappointed.

We believe that consumers should enjoy the material and psychological comfort and security that comes with knowing that stringent and uniform protective safeguards have been embedded in the rules and principles which govern their relationships with their advisors. Canadians deserve access to *formally professionalized* advisor/client relationships which are not dependent on the nature of the underlying products that they purchase to fulfill their financial plans. Underpinning the advisor/client relationship with a level of professional protection is to accord that relationship a level of legal recognition and protection which is much more fundamental than that offered by product regulation. For example, minimum and uniform standards of ethical and professional conduct and other professional safeguards should be in place across all retail-facing subsectors of the financial services industry. There should be an overarching code of conduct and an industry-wide requirement to maintain responsible levels of errors and omissions insurance, neither of which exists today.

This sectoral approach also reveals why the existing regulatory framework cannot effectively regulate today's holistic advisory relationships. Certain stakeholders may suggest that regulation of financial advisors should fall under the auspices of existing regulatory bodies, and it is true that in recent years, some have given greater attention to the advisory relationship – for example, through the Client Relationship Model reforms of the Canadian Securities Administrators ("CSA") members. Despite this laudable effort, existing regulators are structurally limited by their jurisdictions of authority; for example, even if a provincial insurance regulator were to completely overhaul its expectations of licensees, those changes would only impact the consumer's relationship in regard to his or her purchases of insurance products – leaving the consumer's experience with mutual funds unaffected.

In an ideal world, all regulators would set comparable standards so that the client would be equally protected, regardless of the product's origination. But a century of experience and general common sense tells us that when you have multiple regulators that were created on the basis of regulating products, not advice, which already have standards that (in some cases) vary widely from each other, coordinating policies on financial advice is nearly impossible. And even if regulators did manage to agree to a uniform set of policies, those policies would do nothing to capture those individuals who are not registered at all, such as a fee-only planner who does not sell product.

C. <u>There is no firm, clear, and universal requirement for advisors to keep up-to-date their core areas of knowledge.</u>

One of Advocis' core membership requirements is that advisors keep their knowledge up to date by completing continuing education courses each year, including courses on professionalism and ethics. But for the same reasons discussed above, the regulatory requirements for continuing education are completely variable based on the product's sector of origination. For example, Ontario requires that life insurance licensees commit to 30 hours of continuing education every two years, without requiring a minimum learning component on professionalism or ethics. Several provinces do not have any CE requirements with respect to insurance licensees. And while IIROC has continuing education requirements for registered representatives, the MFDA states that continuing education "should be provided" to its approved persons.[1] And those advisors who are not registered with any regulator have no continuing education requirements whatsoever.

An advisor who does not keep his or her level of industry knowledge current is an advisor who fails to properly serve their clients and very likely puts their clients at risk. Moreover, the fields of knowledge with which an advisor should be adequately familiar are continually expanding. Competition among insurance carriers and distributors and between fund companies and securities dealers is fierce, so product change and innovation is a constant. Therefore, static knowledge quickly becomes obsolete and impedes the ability of advisors to act in the best interests of their clients. Advocis believes that all individuals who offer financial advice and planning to retail consumers should be required to complete continuing education on a regular basis, with an emphasis on education related to professionalism and ethical conduct.

D. There is no effective, industry-wide disciplinary process.

The majority of advisory relationships are beneficial to the public, but some inevitably do not work out as anticipated by the parties. Sometimes, this is the clear fault of the advisor. Accordingly, the industry requires a strong and effective disciplinary process, one which will ensure that those advisors who have committed misconduct are appropriately disciplined, and which will also protect the public and deter other advisors from similar misbehaviour.

Provincial insurance regulators or securities self-regulatory organizations ("SROs") such as the MFDA or IIROC, are each empowered to impose a variety of sanctions, including the stripping of an advisor's license or registration. However, the limitations of the existing product-based regulatory framework become most apparent when considering the gaps which open when one considers the practical impact of three regulatory authorities investigating and acting on matters of discipline: each regulator's enforcement powers are limited to its respective sector. Suppose, for example, an advisor engages in misconduct so egregious in the course of selling a mutual fund that the MFDA determines he or she is unfit to work in the fund industry and, as a consequence of this finding, it revokes his or her registration. In such a case, there is nothing to prevent this same advisor from continuing to provide advice, and selling segregated funds through his or her insurance license.

We believe this sector-hopping represents unacceptable consumer risk. The type of serious misconduct which warrants an advisor's outright expulsion from one sector, such as fraud or gross negligence, is clearly indicative of that advisor's inadequate commitment to ethical and professional conduct. This is not a sector-specific concern. It is, rather, an industry-wide concern, which is the same as saying that it is a consumer concern. Permitting such an advisor to continue to offer "advice" to any consumer is a disservice to the public. And even if that advisor is eventually identified and removed by other regulators in their respective sectors, that person can simply continue offering advice on an unlicensed basis since the scope of work is not protected: for example, he or she could "advise" clients to invest in an affiliate's Ponzi scheme.

Also, currently lacking is an effective, accessible and industry-wide mechanism through which the public can easily verify their advisor's credentials and disciplinary history. While several regulators, SROs and industry bodies do maintain websites where the public can search for information on their advisor, the

[1] We are cognizant of the MFDA's June 2015 consultation which considers whether it should require mutual fund dealer representatives to fulfill continuing education requirements.

information returned is confined to the particular entity's sector. As discussed above, the general public does not understand the difference between the various regulatory bodies and is not likely to canvass the registries or databases of each regulator to investigate a potential advisor. In the example above, if a prospective client were to review their advisor's credentials and work and disciplinary history solely through the insurance regulator's website, the client would not be aware of the advisor's expulsion from the mutual funds sector. The client might then mistakenly believe that the advisor's overall disciplinary history was clean.

Advocis strongly believes that consumers should have a one-stop access point for reviewing a prospective advisor's complete disciplinary history that is not limited to the domain of one sector's regulator. It must also capture those individuals who offer advice and planning without the sale of product who are therefore not registered with any existing regulator. That is, rather than being based on today's ad hoc and largely archaic regulatory structure, this critical consumer tool must be reconceived at the level of the advisor/client relationship, in order to properly ensure regulation is informed by the consumer's perspective as seen from the practical reality of day-to-day consumer experience.

These four major shortcomings of the existing regulatory framework expose consumers to unnecessary and unacceptable risk. They arise from the fact that current regulation does not reflect the modern, holistic and cross-sectoral approach to financial advice and planning that most consumers want, require and receive. Fortunately, these risks are largely avoidable, with minimal disruption to the retail financial services sector, if the proper regulatory solution is put in place.

2. THE ACTIVITY OF FINANCIAL PLANNING IS INTRINSICALLY PART OF THE LARGER PRACTICE OF PROVIDING FINANCIAL ADVICE

Advocis believes that before any truly effective and comprehensive reform can be undertaken to address the problems listed above, stakeholders (including regulators) must acknowledge the practical reality for consumers and advisors: financial planning is intrinsically part of the larger practice of providing financial advice. This means that any regulatory reform in the financial planning sector will fail unless this foundational reality is recognized at the outset of any reform effort.

This reality is true whether one looks at it from the regulator's perspective, from the client's point of view, or from the standpoint of the practitioner. It becomes clearly evident when one reviews the requirements stipulated in the rules, policies, bulletins and notices of the MFDA or IIROC and – using Ontario as our baseline province in this submission – regulators such as the Ontario Securities Commission ("OSC") and the Financial Services Commission of Ontario ("FSCO"). As well, financial planning and other forms of financial advice is provided by advisors who are members of organizations such as Advocis, and advisors who are employed by insurers subject to the Canadian Life and Health Insurance Association ("CLHIA"). Advocis assists its members in providing financial planning and other kinds of client advice with its code of conduct and best practices manual; the CLHIA issues best practices and guidance notices for advisors with regard to life and health insurance products.

"Financial advisor" is a term freely used by the public and is generally understood to refer to an individual who provides consumers with financial planning and other forms of financial advice. The term has evolved in response to the evolution that has taken place in the industry. Originally there were very clear distinctions between the various financial sectors – between insurance, mutual funds and other types of securities, for example – and indeed this fact remains evident in the language employed by the various regulators to identify the individual intermediary and the activities he or she offers to consumers. The MFDA refers to a financial advisor as an “approved person,” FSCO refers to him or her as an “agent,” and IIROC as a “registered representative” or “investment representative.”

But from the consumer’s perspective, it is increasingly one advisor who holds multiple licenses who is providing them with holistic financial advice. It is not at all surprising, therefore, that consumers relate to the title of “financial advisor” much more readily than to the terminology employed by regulators. It is the confusion over industry nomenclature which is helping to motivate financial advisors and their clients to join with regulators and spearhead the next stage of structural evolution that is taking place in regulation.

Given this emerging regulatory reality, it is Advocis’ view that proper definitions and protections must be put in place to ensure that consumers know that they are dealing with proficient professionals who are appropriately registered and regulated.

Defining financial advice to reflect the realities of the practitioner and the needs of the consumer

For the purposes of our submission, therefore, Advocis has developed the following definitions that have been crafted from existing regulatory requirements established by FSCO, the MFDA, IIROC, and the OSC. Working from these definitions will assist in illustrating the path that Advocis believes is necessary to ensure that appropriate regulation is developed by an appropriate regulator to ensure that the advisor/client relationship operates at its peak efficiency.

> “financial advice” means the process of engaging in the business of advising others with respect to the planning and/or the execution of advice in respect of selecting, purchasing, or selling financial products to meet investment, risk management, or risk mitigation objectives.
>
> “financial advisor” means any person who engages in the business of providing financial advice to others, including the collection and analysis of information about a person or business:
>
> (a) to identify needs and risks;
> (b) to establish financial objectives;
> (c) to establish strategies to address identified needs and risks, and achieve the established financial objectives; and
> (d) to continuously monitor the needs and risks and the progress toward achieving the established financial objectives which would include any one or a combination of the following:
> (1) the monitoring of cash flow management;
> (2) capital needs assessment;
> (3) education planning;
> (4) retirement planning;
> (5) investment planning;
> (6) taxation and estate planning;
> (7) insurance planning;
> (8) business succession planning; or
> (9) employee benefits planning.

Clearly the scope of these activities is such that any financial advisor registered or operating under the rules of the MFDA, IIROC, OSC or FSCO will be caught by this definition. We are not asserting that all financial advisors are engaged in financial planning at the same high standards as those who have attained specialized designations. But the proposed definition does delineate the basic parameters regarding the minimum actions that a financial advisor must perform and the minimum standards to which he or she must adhere. The definition also affirms that an advisor, whether or not he or she also has a financial planning designation, must meet the *de minimus* standards of the Know Your Client ("KYC") and Know Your Product ("KYP") rules, as well as the various prescribed suitability requirements, all of which are key components of financial planning.

> "financial planner" means a financial advisor holding a recognized specialist designation, including:
>
> (a) Certified Financial Planner® (CFP®), sponsored by the Financial Planning Standards Council;
> (b) Personal Financial Planner (PFP®), sponsored by the Canadian Securities Institute;
> (c) Certificate in Financial Planning (Planificateur financier [Pl. fin.] designation), sponsored by Institut québécois de planification financière (IQPF);
> (d) Chartered Financial Consultant (CH.F.C.®), sponsored by Advocis, the Financial Advisors Association of Canada;
> (e) Chartered Life Underwriter® (CLU®), sponsored by Advocis, the Financial Advisors Association of Canada; and the
> (f) Registered Financial Planner® (R.F.P.®), sponsored by the Institute of Advanced Financial Planners

Per this definition, we recommend that the above six designations be recognized as advanced financial planning designations, going beyond the four identified in the MFDA Consultation.

As we will demonstrate below, these definitions reflect the daily reality of advisors and consumers, and they allow one unified professional body to oversee all financial advisors, including specialists. Indeed, this form of oversight is optimally efficient, as to do otherwise would require adding additional regulatory layers and complexity. Moreover, another layer of regulation would not solve the problem of regulatory arbitrage and would leave unaddressed the gaps caused by the silos which separate the insurance and securities sectors at the advisor/client level.

From the consumer's perspective, all financial advisors engage in some form of financial planning

It is crucial to understand that, from the perspective of the consumer, all financial advisors conduct a baseline level of financial planning, as required under the regulations of the OSC, FSCO, MFDA and IIROC. Within the broad pool of financial advisors, there are industry-developed designations which enable a financial advisor to further specialize in the more detailed aspects of various dimensions of advice giving, such as taxation, estate planning, and health insurance, for example.

The reality of the financial advice sector is depicted in Figure 1. All financial advisors (the largest of the Venn circles) must possess the basic skill level to engaging in client-appropriate financial planning. Within the total advisor population, we see the ongoing development of more stringent specializations with respect to certain sub-fields of the advice process. These sub-groupings reflect specializations which go beyond the benchmark of skills which the average financial advisor would be required to meet. These specializations are useful to many consumers – and at times are necessary for those clients who require the development of more complex advice and planning goals and objectives.

Figure 1. A depiction of the interrelationship between the total population of financial advisors and prominent specialist subgroups. For example, advisors who are CLU®, CH.F.C.® or CFP® designation holders are members of specialized groups within the larger population of financial advisors. Overall, the field of financial advice is populated with a range of designations, including a number of popular, long-standing financial planning designations.

So, within the family of financial advisors there is the presence and opportunity of smaller subgroups of specialists who wish to operate in advanced areas of planning. Such specialization is common in established professions; indeed, it is analogous to the medical profession, where all doctors must meet a minimum standard to be called a medical doctor or MD. But within the field of MDs we have smaller groups of MDs who have specialized. Every member of the profession is a doctor, but only those who have completed additional training and course work are allowed to use designations which identify their specialization, such as cardiologist and oncologist.

To further the analogy, consider a proposal to regulate only the subgroup of advanced specialists, as opposed to the entire group of medical doctors. Such an option would be a wholly inadequate policy response: the risk to consumers would be overwhelming if anyone could hold out as a doctor and operate largely or completely unregulated. Similarly, to regulate only financial advisors who have completed a specialized designation program would be a wholly inadequate policy response, as this too would expose consumers to risk. Yet this is what some within the financial advice community are suggesting be implemented as a program of policy reform.

Financial planning is recognized as a necessary component of securities advice

Financial planning is a necessary component of providing financial advice or making a recommendation on a security – regardless of whether it is a bread-and-butter money market fund or a sophisticated exempt market security.

A. The CSA

For example, National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* ("NI 31-103"), requires a registrant to take reasonable steps to ensure that, before it makes a recommendation to, or accepts an instruction from, a client to buy or sell a security, or makes a purchase or sale of a security for a client's managed account, the purchase or sale is suitable for the client.[2] In addition, the related Companion Policy 31-103, in section 3.4 [Proficiency – initial and ongoing], states that an individual "must not perform an activity that requires registration unless the individual has the education, training and experience... including understanding the structure, features and risks of each security the individual recommends."[3]

B. The MFDA and IIROC

At the Ontario Roundtable Sessions entitled *Investigating the Merits of More Tailored Regulation of Financial Planners in Ontario*, the Ministry of Finance was explicit that individuals holding out as financial advisors or as financial planners were to be the chief subject of the review. In its submission to the Ministry after the Roundtables, the MFDA stated that part of what its regulated members do for their clients is in fact financial planning. In its submission the MFDA notes that it regulates "81,184 Approved Persons (partners, directors, officers, compliance officers, branch managers, employees and agents of the dealer who are subject to the jurisdiction of the MFDA)" and then observes that many of these persons in fact conduct financial planning activities on behalf of their clients:

> *MFDA Regulation of Financial Planning Activities*
> In the course of providing advice to clients, many Approved Persons of MFDA Members *engage in activities that may be considered financial planning in nature*. These activities are often incidental to the advice or recommendation provided to the client and may include general asset or portfolio allocation advice, tax planning, estate planning or a comprehensive needs analysis. Many Approved Persons of MFDA Members also hold financial planning designations such as the CFP, PFP and RFP.

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[2] National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations*, p. 44. Online at https://www.osc.gov.on.ca/documents/en/Securities-Category3/ni_20150111_31-103_unofficial-consolidated.pdf.
[3] Companion Policy 31-103 CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations*, p. 150. Online at https://www.osc.gov.on.ca/documents/en/Securities-Category3/ni_20150111_31-103_unofficial-consolidated.pdf.

> The jurisdiction of the MFDA is not limited to product regulation. The MFDA regulates the advice provided by Members and their Approved Persons to clients in relation to their accounts. Suitability requirements under MFDA Rules apply not only to the product but also to the advice and recommendation to the client. Similarly, know your client information, which is required to be collected under MFDA Rules by Members and their Approved Persons, is not intended to apply solely to the sale of the product and is used more generally to assess the suitability of the advice and the investment strategy. *The MFDA regulates the financial planning activities of Members and their Approved Persons that are provided as part of this comprehensive advice process.*[4]
>
> (emphasis added)

MFDA Policy No. 2 *Minimum Standards for Account Supervision*, MFDA Rule 2.2.4 *Updating Client Information*, MFDA Member Regulation *Notices Know-Your-Product* (MSN-0048) and *Suitability* (MSN-0069) all provide further guidance on these ongoing obligations for securities registrants.

IIROC, like the MFDA, requires that its members engage in the same level of basic planning activity in the sale of securities to clients. For example, IIROC Rule 1300 *Supervision of Accounts*, IIROC Rule 2500 *Minimum Standards for Retail Account Supervision*, and IIROC Guidance Note 12-0109 *Know Your Client and Suitability*, all require that the dealer member or its registered representative maintain compliance with IIROC's various KYC obligations and investment suitability requirements. For example, IIROC Guidance Note 12-0109 requires that KYC information be collected and assessed and product suitability obligations be fulfilled. IIROC Rule 1300 requires that the dealer member, when accepting a client order, when providing a recommendation to a client, or when certain triggering events occur, use due diligence to ensure that the order, recommendation or account position is suitable for the client "based on factors including the client's current financial situation, investment knowledge, investment objectives and time horizon, risk tolerance and the account or accounts' current investment portfolio composition and risk level."[5]

Financial planning is recognized as a necessary component of insurance advice

A. <u>FSCO</u>

FSCO has in recent years placed a special emphasis on providing regulatory oversight and guidance for the province's insurance-licensed financial advisors (and their clients) with regard to the suitability of product recommendations, the disclosure of conflicts of interest, and the ability of consumers to make informed decisions.

From 2013 to 2015, FSCO engaged with industry stakeholders in the conduct of its comprehensive *Life Insurance Product Suitability Review (Point-of-Sale)*. This review focused on how effective advisors are at ensuring product suitability for clients when engaged in the process of recommending life insurance products. This stakeholder review was undertaken with a special focus on "practices in the field," on determining the level of product knowledge possessed by the average consumer, and on how best to

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[4] Mutual Fund Dealers Association of Canada, "Financial Planning Consultation Submission to the Ontario Ministry of Finance," February 5, 2014, p. 2. Online at www.fin.gov.on.ca/en/consultations/rfp-submissions/mutual-fund-dealers-association-of-canada.pdf.

[5] See Investment Industry Regulatory Organization of Canada, IIROC Rule 1300 Supervision of Accounts, 1300.1(p) to (s). Online at www.iiroc.ca/Rulebook/MemberRules/Rule01300_en.pdf.

address any information deficits on either side of the advisor/client relationship, including through enhanced product disclosure and by ensuring professional-level advice is consistently provided through the use of best practices to ensure that advisors ask clients the correct questions to gather the necessary data for a proper needs analysis so the insurance advice will meet the client's financial needs and objectives. In sum, FSCO was acting to ensure that advisors were meeting *de minimus* standards of proficiency when providing planning advice prior to a product sale.

In its *Life Insurance Product Suitability Report* of September 2014, FSCO set out the findings of the review and affirmed that its recommended "best practices are largely being followed i.e. the actual practices do reflect the needs based sales practices described in *The Approach: Servicing the Client Through Needs-Based Sales Practices*."[6]

B. CLHIA

In addition, the CLHIA Reference Document of February 2013 entitled *IVIC Suitability Needs-Based Sales Practices* sets out the three steps for advisors to follow: fact-finding, needs assessment and recommendations and advice. The document is explicit about the nature of the practices the advisor is expected to carry out:

> The task of the advisor is to identify the financial needs of the consumer to ensure the IVIC product is suitable for them in light of their particular circumstances and then assist the consumer in understanding how the product meets his or her financial needs.[7]

The CLHIA document further notes that:

> Each of these steps requires skill and judgment on the part of the advisor. As noted in *The Approach*, the specific questions the advisors should ask will vary depending on the circumstances of the individual client and the complexity of the products being considered... the advisor must decide on an appropriate level of inquiry and choose an approach that will effectively elicit the information required to identify the client's needs. The process of assessing needs... requires that the advisor make judgements about the priorities of the client and differentiate between wants and needs.[8]

The CLHIA is explicit about the planning entailed in providing advice to a client with regard to product suitability; the advisor is expected to ask "More detailed questions following the preliminary assessment focus on acquiring a better understanding of the client's needs to *help determine whether or not an IVIC can form part of a suitable product allocation.*"[9] (emphasis added)

As for CLHIA Guideline G2: *Individual Variable Insurance Contracts Relating to Segregated Funds* (January 2011), it requires that the segregated fund's "Fund Facts should, in section 7, state "in plain language for the average retail consumer" who the fund is for:

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[6] See Financial Services Commission of Ontario, *Life Insurance Product Suitability Review (Point-of-Sale)*. Online at www.fsco.gov.on.ca/en/insurance/Pages/eblast-point-of-sale-sept-2014.aspx.
[7] Canadian Life and Health Insurance Association, Reference Document: *IVIC Suitability Needs-Based Sales Practices* (February 2013), p. 2.
[8] *Ibid.*
[9] *Ibid,* p. 4.

Item 7 – Who is this fund for?

Provide details regarding the type of investor the segregated fund would be suitable for stating the advantages and any necessary cautions or warnings. Suitability should be tied to the fundamental investment objective of the fund and risk category assigned in Item 5 above.[10]

Finally, the CLHIA's consumer brochure, *Key Facts About Segregated Funds Contracts*, sets out quite clearly the nature of this financial planning the consumer should expect from his or her advisor:

> Your advisor will provide you with written disclosure about the companies he/she represents, any conflicts of interest and how he/she is paid. The insurance advisor's professional qualifications permit him/her to help you analyze your retirement income planning, estate planning and insurance needs, make recommendations that meet those needs and provide ongoing services, such as beneficiary changes, reviewing and updating your investment strategy and rebalancing your portfolio.[11]

C. Provincial insurance councils

A cursory review of the Canadian Insurance Regulators Disciplinary Actions database indicates that insurance councils also recognize the central role held by financial planning in the advice which advisors provide to their clients.[12] It is telling that in several recent cases from the Insurance Council of British Columbia, the disciplined advisors were ordered to take CFP® and/or CLU® courses.

For example, in the May 1, 2014 decision of *In the Matter of the Financial Institutions Act (RSBC 1996, c. 141) and The Insurance Council of British Columbia and Grant Sheldon Persal,*[13] the Council found that the life agent, among other issues, advised his clients to purchase an insurance product that they did not fully understand. In reaching its decision, the Council summarized the investigation and review done by its Review Committee, which examined a number of precedents. For example, the Council noted that:

> In *J. Duke*, the licensee made inappropriate recommendations to a client regarding investments in exempt market securities in light of the client's age, risk tolerance, and financial profile. The licensee was an experienced insurance agent who knew, or ought to have known, the risk posed by the investment was too high for his client and he should not have recommended the investments. The licensee's licence was suspended for 12 months, [and] he had a condition imposed on his licence that required him to complete courses necessary to obtain the Chartered Life Underwriter designation or the Certified Financial Planner designation.[14]

Accordingly, in its decision, the Council imposed on the life agent's licence a requirement that the agent, following completion of his suspension, must successfully complete at least one course, per licence year, toward either a CLU® designation or a CFP® designation, until his successful completion of all of the courses required to attain either designation.

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[10] Canadian Life and Health Insurance Association, Guideline G2: *Individual Variable Insurance Contracts Relating to Segregated Funds* (January 2011), p. 77.
[11] Canadian Life and Health Insurance Association, *Key Facts About Segregated Funds Contracts*, p. 7.
[12] The Canadian Insurance Regulators Disciplinary Actions database offers public access to regulatory decisions issued by insurance regulator members of CISRO and CCIR. The database is at http://decisions.cisro-ocra.com/ins/en/nav.do.
[13] Online at http://decisions.cisro-ocra.com/ins/bcic/en/item/71642/index.do?r=AAAAAQAddW5zdWl0YWJsZSBmaW5hbmNpYWwgcGxhbm5pbmcB.
[14] *Ibid.*, p. 8.

Similarly, in *In the Matter of the Financial Institutions Act and the Insurance Council of British Columbia and Wei Kai Liao*,[15] the advisor had two clients make complaints about the life and critical illness policies he had sold, in addition to investment loan/leveraged investment recommendations. The Council ordered that:

> A condition is imposed on the Licensee's life and accident and sickness insurance licence that requires him to successfully complete one of the following courses during each of the next four licence periods commencing with the current licence period:
>
> a) Certified Financial Planner 231 - Financial Planning Fundamentals
> b) CFP 232 - Contemporary Practices in Financial Planning
> c) CFP 233 - Comprehensive Practices in Risk & Retirement Planning
> d) CFP 234 - Wealth Management & Estate Planning.

In 2012 Lambert John Schmid was found to have failed to conduct a sufficient needs analysis in selling life policies to a married couple. Among other disciplinary measures, the Council imposed on Schmid's life and accident and sickness insurance licence the requirement that he successfully complete all of the courses in Advocis' Best Practices program, or a similar program approved by the Council.[16]

If these cases are not regulatory recognition of life-licensed advisors providing financial planning, then it is hard to see just what would qualify as financial planning.

Financial planning is recognized as a necessary component of financial advice by industry associations and designation-granting bodies

Industry groups and designation-granting bodies such as Advocis and the Financial Planning Standards Council ("FPSC") have developed mandatory rules and guidelines, and codes of conduct, to which their members (Advocis) or holders of their advanced designations (both Advocis and the FPSC) must adhere. These designations and related educational programs enable financial advisors to develop additional skills sets and areas of specialized knowledge in order to enhance the planning services they provide to clients who require more detailed or sophisticated forms of planning. Prominent examples are the CLU® and the CFP® designations. In addition, the basic rules and obligations for advisors in regard to the minimum and necessary financial planning obligations required for all advisors in the securities sector by IIROC, the MFDA and the OSC and, in the insurance sector, by FSCO and the CLHIA, are echoed on the FPSC website for CFP® designation holders, as well as in the Advocis *Best Practices Manual*.

As the FPSC notes in its consumer guide *10 Questions To Ask Your Financial Planner*, the nature of the services provided by a CFP® designation holder vary widely, ranging from financial planning to product advice to more specialized areas:

> The services a financial planner offers will vary and depend on their credentials, registration, areas of expertise and the organization for which s/he works. Some planners offer *financial planning*

[15] Online at http://decisions.cisro-cra.com/ins/bcic/en/item/100203/index.do?r=AAAAAQAEbGlhbwE.
[16] *In The Matter of the Insurance Council Of British Columbia ("Council") Report of Council in the Matter of the Financial Institutions Act (The "Act") (R.S.B.C. 1996, C.141) and Lambert John Schmid* (March 5, 2012). Online at http://decisions.cisro-ocra.com/ins/bcic/en/63693/1/document.do.

> *advice* on a range of topics but do not sell financial products. *Others may provide advice only in specific areas such as estate planning or taxation*. Those who sell financial products such as insurance, stocks, bonds and mutual funds, or who give *investment advice*, must be registered with provincial regulatory authorities and may have specialized designations in these areas of expertise.[17]
>
> (emphasis added)

Advocis' Best Practices Manual emphasizes the central importance of financial planning in typical advice transactions, which fall far outside the ambit of a formal financial plan: the section entitled "KYC – Know Your Client" begins as follows:

> *Gathering the Client Data - Know Your Client*
>
> Best Practice Principle: "Know your client" (KYC) is about more than meeting regulatory requirements.
>
> Tip: Basic KYC is only a starting point in the information required to effectively analyze a client's situation. Adding incremental data enables advisors to add increasing levels of service and advice.
>
> *Gathering detailed information about a client is nothing new to an advisor who has been doing comprehensive financial plans. However, in recent years, tougher compliance laws have forced all advisors, even those who operate in a very "transactional" manner, to collect more robust KYC information.* Quite frankly, to do anything else would be like a doctor who spends most of his time writing prescriptions to deal with symptoms rather than doing examinations and tests for a deeper understanding that can lead to a cure.[18]
>
> (emphasis added)

Financial planning is recognized as a necessary component of financial advice by the Canada Revenue Agency

It is worth considering how the Canada Revenue Agency ("CRA") treats the activities of financial advisors and planners. With regard to the tax treatment of advice dispensed by advisers and planners, one is not permitted to treat as tax deductible on one's income tax return any fees one was charged for advice and planning.[19] Typically, however, one is permitted to deduct "investment counsel fees" for specific securities transactions. From a policy perspective, these securities transactions are executed with the aim of generating taxable income. But – and this is significant – one cannot claim as tax deductible the trailing commission: this fits with the general principle that financial planning is not tax deductible – since trailers pay for the planning activities of an MFDA or IIROC dealing representative, and hence are not tax deductible, just as other, more "official" forms of financial planning are not tax-deductible. Indeed, from the CRA's point of view, planning activities are less about generating taxable income and more about sheltering income from tax.

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[17] Online at www.fpsc.ca/10-questions-ask-your-planner.

[18] For more on the Advocis Best Practices Manual, please contact Advocis at info@advocis.ca.

[19] Canada Revenue Agency, IT238R2 - *Fees Paid to Investment Counsel*. Online at www.cra-rc.gc.ca/E/pub/tp/it238r2/ it238r2-e.html. The CRA notes that fees paid for other types of advice, such as financial planning, are not within the provisions of paragraph 20(1) (bb), and are not deductible. As well, commissions are specifically excluded from the definition of investment counsel fees. So commissions paid to advisors to execute transactions, or front- and back-end mutual fund commissions, are generally not deductible.

Thus, from the tax treatment point of view of the individual retail investor or consumer, certain activities done by advisors — such as charging a trailing commission and providing various forms of advice pursuant to it — coincide conceptually with the same planning activities done by those individuals holding out as financial planners. *This reinforces the notion that planning is a subset of advice, and is conducted by MFDA or IIROC dealing representatives as well as by CLU® or CFP® designation holders.*

Therefore, the central components of financial planning are <u>already</u> part of the licensing requirements for all financial advisors

Consumers seek a wide array of financial planning advice, based on their personal financial circumstances, stage of life and retirement goals. This advice ranges from the relatively straightforward (e.g., the selection of a GIC), to the complex, such as estate and trust planning and more sophisticated wealth management strategies. Regardless of the complexity of the advice being sought, advisors must always demonstrate the required competencies and ensure the advice is appropriate by adhering to the basics of the applicable KYC requirement – his or her life and financial situation, his or her needs and goals, and level of risk tolerance – and applicable KYP requirements – such as the suitability of the product or service for the client, aswell as its benefits and potential risks. Obviously an advisor who follows MFDA Rule 2's obligations on suitability and KYP obligations when providing mutual fund advice to a twenty-year-old who is making his first mutual fund purchase should not be held to the same standard of planning proficiency as an advisor who is drafting a comprehensive financial plan which includes a will and a trust for an upper-middle-class family, for example. Each level of advice should and does have different knowledge requirements. But in both situations, it cannot be denied that rules governing licensees and their conduct incorporate financial planning.

3. <u>Financial Planning Must Not be Regulated as a Standalone Activity if the Ultimate Goal is to Improve Consumer Outcomes</u>

One of the most crucial questions posed by the MFDA and others, including Ontario's Expert Committee, is whether regulators should regulate only those advisors who hold advanced designations (including the four identified in the MFDA Consultation), or whether all consumers deserve higher standards – and not just those who can afford them.

As demonstrated above, rules regarding licensing under the MFDA, IIROC, OSC and FSCO regimes all require that financial advisors conduct elements of financial planning, with advisors who achieve CLU, CFP or other advanced advisory designations undertaking a further degree of specialization to offer clients a more complex form of financial planning in the course of providing financial advice. However, not every client requires the services of such a specialist.

All of this effectively undercuts the position articulated by certain stakeholders that holders of only certain planning designations (including the CFP, FPI, PFP or RFP designations set apart in the MFDA Consultation) provide financial planning, or that financial planning is somehow a discipline and career distinctly and categorically separate from the field of financial advice. Indeed, advisors who hold advanced planning designations are simply able to provide a more detailed, specialized and rigorous form of financial planning.

Without diminishing the value of advisors who hold advanced financial planning designations, concern over consumer access to financial advice leads us to note that some of these advisors operate from a fee-based or even fee-only platform. The preferred methods of compensation used by these advisors undoubtedly impact the desire of consumers to seek out advice, and their ability to pay for it. Moreover, fee-only advisors represent a small proportion of the market – it is estimated by PricewaterhouseCoopers in its *Sound Advice: Insights into Canada's Financial Advice Industry* report that there are approximately 450 fee-only advisors in all of Canada.[20]

We believe they serve an important niche within the population who can afford their services. Moreover, it is often these planners who stand out through their demonstrable commitment to professional levels of proficiency, ethics and continuing education. But they simply do not represent a viable advice channel for the vast majority of consumers. Besides the fee-only group, there are also advisors who focus on estate planning, wealth transfer, health insurance, living benefits and similar areas of concentration – and to do so, they hold advanced designations that signify their expertise in that area of planning.

In practice, few consumers can afford a stand-alone comprehensive financial plan, as this typically requires an outlay of several hundreds or even thousands of dollars at once. Instead, the vast majority of consumers who receive planning receive it to varying levels and degrees through their advisors who engage in financial planning prior to making product recommendations. Accordingly, we remain at a loss to understand how one can conceive of financial planning as a stand-alone profession that is separate from advice. For most consumers, the planning they receive is aimed at addressing specific life events, such as saving for a home or determining whether the client is able to afford retirement.

Consumers often do not directly pay for this planning, as the planning is usually followed by the sale of products in order to ensure the plan's fulfillment. It is these product sales which compensate the advisor for his or her efforts. Most consumers receive their planning and advice in this manner because it is accessible and affordable. We believe that all consumers deserve to enjoy the benefits of enhanced professionalism in the industry and to be able to trust that their advisor is qualified and competent; this right should not be restricted to a narrow subset of the population that can afford comprehensive financial plans offered through advanced designation holders, as doing so would not serve the larger public interest. Therefore, we urge regulators and governments to be cognizant of the planning and advisory needs of the majority of the public as it considers reforms.

As we have seen, all financial advisors must engage in fundamental forms of financial planning, and certain financial advisors may elect to undertake further specialized forms of more sophisticated financial planning. Given all of this, what perspective does the advisor in the field have on regulatory reform – especially that of the advisor who may be characterized as an "advanced planning" provider? We would note that Advocis is uniquely positioned to provide a practitioner's perspective on regulatory reforms which would impact financial advisors and planners: our association is composed of financial advisors, many of whom have acquired specialist financial planning designations (among other advanced designations). In our experience, these are advisors who have acquired designations such as the CLU or CFP, and are already committed to meeting – if not exceeding – higher requirements in terms of

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[20] See the Appendix for PricewaterhouseCoopers, *Sound Advice: Insights into Canada's Financial Advice Industry*, July 2014, p. 15. "Fee-only planners" are defined as "financial advisors that provide objective financial counselling and associated services for a negotiated fee and who do not directly offer either proprietary or third-party financial products" (p.15).

advising and planning proficiencies, standards of ethical conduct, and the maintenance of an appropriate standard of industry knowledge through ongoing continuing education.

4. <u>Our Solution: Raising the Professional Bar by Professionalizing Advice</u>

As we have argued throughout, retail consumers of financial products need to be assured that they are accessing affordable, professional-grade financial advice. This means that consumers of financial products, advice, and other services, including planning, need to know that any individuals who provide financial advice, whether or not that individual uses the title of "financial advisor" or some variant thereof, has met rigorous initial and ongoing proficiency standards. The least expensive and intrusive way to accomplish this is through establishing the provision of retail- or consumer-level financial advice as a recognized professional activity.

This, in turn, requires the creation of a professional organization for financial advisors, the authority of which would be delegated in statute by a province's Minister of Finance to a delegated administrative authority ("DAA"). Under a DAA, the province would still retain overall accountability and control of relevant enabling legislation and monitor and remain accountable for the overall performance of the authority. Additionally, DAAs have reporting obligations to the government, such as annual reports and audited financial statements, and can be subjected to operational reviews.

The current web of regulatory relationships produces unnecessary complexity for all stakeholders—bringing about increased compliance costs and needless confusion for consumers. As an example, Ontario's current situation is demonstrated in Figure 2.

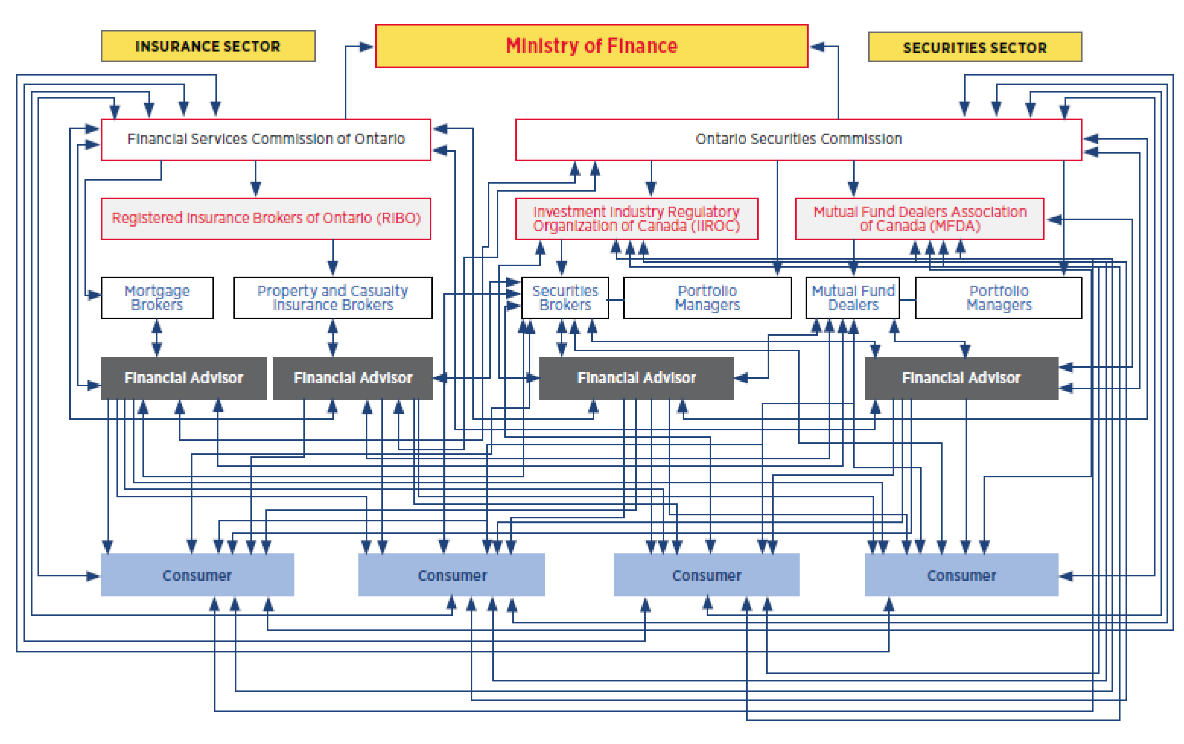

FIGURE 2. Ontario's current regulatory structure has become bewilderingly complex. Clearly the needs of consumers and advisors has outgrown and outpaced the existing and largely product-based model which currently regulates Ontario's financial services industry. Each one of the blue lines represents a compliance requirement or other form of regulatory activity – which in the end are passed on to the Ontario consumer.

By creating a DAA, the regulatory landscape can be reconfigured to provide comprehensive, efficacious, and cost-effective consumer protection. DAAs are not-for-profit corporations that assume the day-to-day operational responsibility for licensing, education, complaints handling, inspection and enforcement matters as described in government legislation. DAAs immediately reduce the government's "fiscal footprint": the DAA's employees are not public servants and they are self-financing, largely through fees paid by the governing body's members. This model has gained acceptance in several provinces: notable examples include Ontario's Travel Industry Council, Alberta's Boilers Safety Association, and the British Columbia Safety Authority.

The DAA model removes silos at the consumer level and plugs a major gap in the regulatory framework

The DAA would focus on the financial advisor and consumer relationship. In doing so, it will remove oversight of retail consumer services provided by financial advisors from the MFDA, IIROC, OSC and FSCO and consolidate it under a unified consumer protection rubric. Such consolidation eliminates the present state of consumer and advisor confusion by introducing a coherent regulatory structure to the advisor/client relationship. While the silos which currently exist between the insurance and securities sectors at the product level will remain intact in order to preserve existing regulatory expertise, the silos would be removed at the level of the advisor/client relationship.

The proposed new regulatory approach will not disrupt any existing product-related regulation; however, if governments are considering a further rationalization of the system, then we would note that a review of the existing SROs for regulatory and cost efficiencies would be more easily managed in this consumer-focused model. It is critical to recognize the efficiency and cohesiveness to be found in the well-defined regulatory accountabilities inherent in a single professional body; such a model can remove confusion, cost, duplication and overlap; quickly address sector-specific problems; and simplify what is currently an unreasonably confusing system for consumers. The expected result would be enhanced levels of consumer protection and satisfaction.

A new DAA focused on financial advice and the relationship between the advisor and client will eliminate much of the duplication and confusion that currently exists under the product-oriented model. In contrast to the existing web of regulatory oversight represented in Figure 2, Figure 3 below illustrates the simplicity that can be achieved with a DAA which focuses on the advisor/client relationship.

Advocis believes that a truly industry-wide effort to regulate all financial advisors will enable the industry to move beyond the status quo and enhance public trust in the advice industry and, to an extent, in the capital markets. Just as importantly, an industry-wide DAA will eliminate less-reported by equally problematic regulatory hazards, such as regulatory arbitrage and capture. Promoting professionalism in all advice-based, retail-focused relationships between intermediaries and consumers in the financial services sector may in fact be the most effective way to inculcate an enhanced commitment to ethical and professional conduct. Excluding financial advisors – whether in title or in scope of practice, or both – from any such reform effort will virtually guarantee its failure. As we have repeatedly stated: Canadians deserve better.

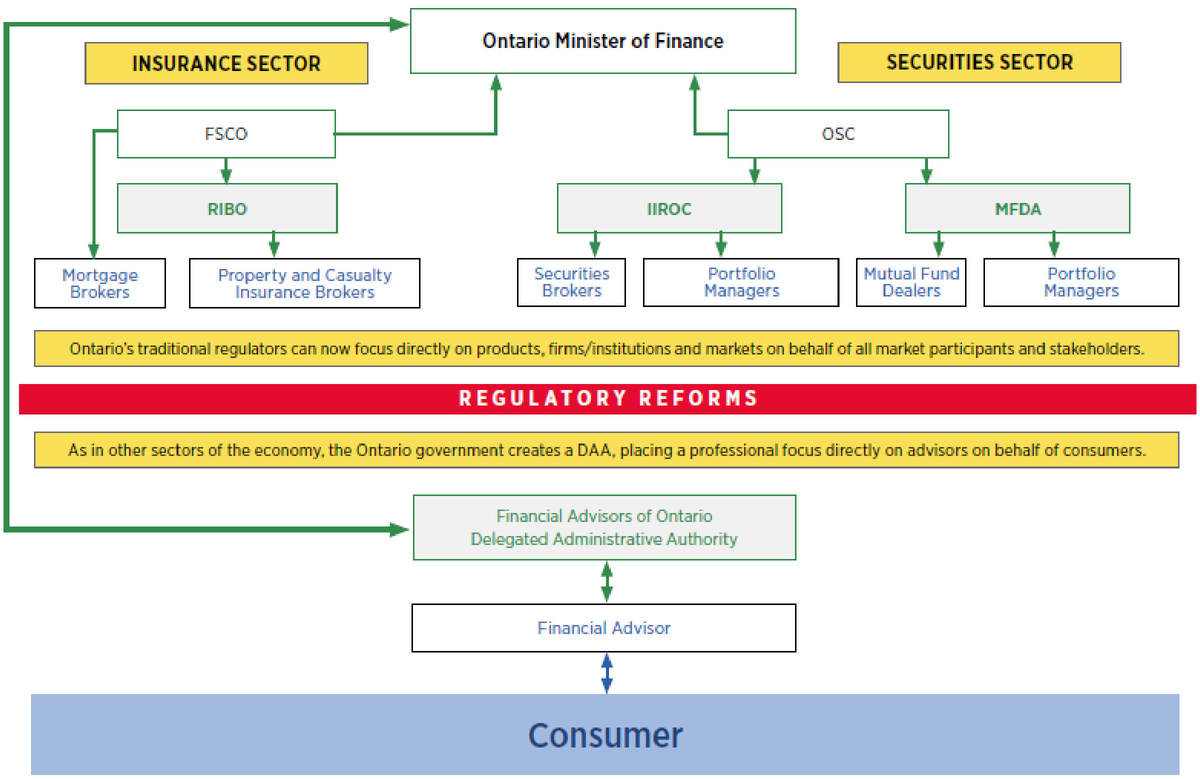

FIGURE 3: This chart shows how a DAA could provide cross-sectoral, consumer-focused regulation and sets out the parameters for a potential reform of the delivery of advice to Ontario's financial consumers.

To see how we can give consumers the regulatory system they deserve, it is first necessary to understand in more detail the current system, which we believe is an impasse of sorts – one which prevents the introduction of smaller, smarter and more targeted regulation with a consumer focus. What follows are key structural and operational details of the DAA.

Licensing and registration requirements

Under the proposed DAA, the consumer's assurance that his or her advisor has met or exceeded the initial proficiency standards would be derived from the fact that every person who is licensed or registered to sell financial products has met the initial requirements for membership in the DAA. Further, the DAA would be able to develop categories and subcategories for membership, as conceptualized in Figure 1, which would recognize the areas of specialization reflected, for example, in designations such as the CFP and the CLU.

<u>*Mandatory membership and unity of oversight:*</u> Under the DAA, membership would be mandatory for all of the province's financial advisors. Such mandatory membership addresses the concerns raised above with respect to title and scope protection. The result would be that individuals who hold themselves out as financial advisors, in title or in scope, would be required to be licensed. Licensing is currently split between three regulators: FSCO, the MFDA and IIROC. It would make sense if licensing was handled by a single source, as this would provide a great deal of efficiency. It would also result in a single entity for

consumers to consult with respect to the licensing of anyone holding out or purporting to be a financial advisor.

Education, training and ethical responsibilities

Advocis believes that proficiency standards and continuing education are cornerstones of professionalism. Under a DAA model, the DAA would establish initial proficiency standards for financial advisors, and would administer, monitor and enforce continuing education requirements designed to ensure that all financial advisors maintain a high standard of proficiency. The DAA would be required to actively administer their codes of conduct, so that the public is assured that the DAA's member advisors understand and fulfill the ethical obligations they owe to their clients.

Individuals who elect to hold themselves out as competent practitioners in areas of professional specialization, such as financial planning, would be required to maintain in good standing the necessary recognized designations. The designation programs would be provided by organizations which the DAA has vetted and determined that their designation program meets the province's standards for specialization. This mandatory review would help address the problem associated with the alphabet soup of accreditations, certificates and designations that currently exist and are misleading to the public. It would also allow for those legitimate designation programs which currently exist to continue to provide the specialized education products which advisors and their clients want.

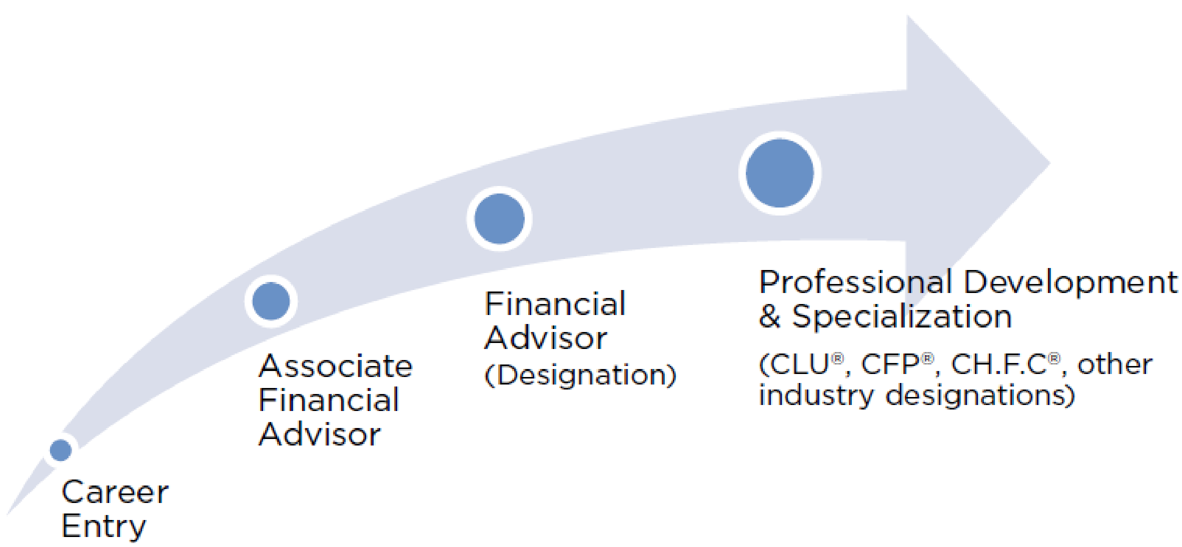

FIGURE 4. The financial advisor's career path and professionalism: a DAA would work with government and stakeholders to establish entry requirements for the profession. Figure 4 demonstrates the development of a financial advisor from the initial entry into the profession all the way through to the attainment of one or more specialist designations, which are for those advisors who wish to acquire deeper knowledge and professionalism.

<u>*Continuing education (CE) requirements*</u>: The DAA's annual continuing education requirements would focus on the financial advisor's duties to clients. These CE requirements would complement and build on the practice proficiency standards and CE requirements of regulators. However, all members would be required to fulfill ongoing CE requirements, which would have a structured component, including

mandatory professional ethics and conduct requirements. These would include course requirements established by professional associations identified by the DAA as proficient in providing CE.

A code of professional conduct: All financial advisors would be required to subscribe to the DAA's code of professional conduct, and abide by their DAA's rules of professional conduct in all of their dealings with third parties (i.e., the application of the code and rules would not be limited to the financial advisor/client relationship). Any code of professional conduct would of necessity establish and explicate:

- the priority of the client's interest over those of the advisor;
- issues of misconduct (including criminal convictions and regulatory infractions);
- the duties surrounding conflicts of interest; the duty to provide competent service;
- the duty to act with honesty and integrity;
- the duty to preserve and protect client confidentiality; and
- the duty to cooperate with the regulators.

An errors and omissions insurance requirement: All financial advisors, and their corporations and/or agencies, would be required to carry professional liability insurance relating to the activities they ordinarily engage in as financial advisors.

Titles and designations of individuals who engage in financial planning and/or the giving of financial advice

As we have repeatedly argued, Advocis believes that regulating the usage of the title "financial advisor" is timely, appropriate and necessary. Financial advisors are one of the last groups of specialized practitioners whose professional title is not regulated by law. While other professions such as medicine, law and engineering have had their professional titles regulated for over a century or more, in recent years many other areas of professionalized activity have become similarly regulated. For example, in Ontario, the title of "Social Worker" is restricted to registrants of the Ontario College of Social Workers and Social Service Workers; in Alberta, titles offered by the Alberta Boilers Safety Association and the Petroleum Tank Management Association are restricted to registrants of these professional bodies.

With so many people struggling to meet their retirement goals, with new families starting out without proper financial planning in place, and with government policies increasingly shifting the responsibility for its citizens' future financial needs onto individuals, now is the time to regulate the use of the professional title of "financial advisor." To recognize those advisors who have obtained additional education, we suggest they be recognized as being specialists in their area of expertise. This would be analogous to what the Law Society of Upper Canada offers: all its members must satisfy baseline standards, but through its Certified Specialist program, it also recognizes those practitioners who are experts in, *inter alia*, criminal law, family law or real estate law.

With regard to advisor designations, the DAA would identify those designations that meet the defined expectations of those holding out as having completed an advanced designation program in relation of financial planning, such as a CLU or CFP. Advocis has of course long been committed to the provision of high-quality designations for financial advisors which will ensure that consumers are working with a person who has met sufficiently advanced proficiency standards. The following designations would be granted initial proficiency recognition, provided that the advisor is in good standing with one of the relevant designation-granting bodies:

- Chartered Life Underwriter (CLU), sponsored by Advocis, the Financial Advisors Association of Canada;
- Certified Financial Planner (CFP), sponsored by the Financial Planning Standards Council;
- Personal Financial Planner (PFP), offered by Canadian Securities Institute;
- Certificate in Financial Planning (Planificateur financier [Pl. fin.] designation), sponsored by the Institut québécois de planification financière (IQPF);
- Registered Financial Planner (RFP), sponsored by the Institute of Advanced Financial Planners;
- Chartered Financial Consultant (CH.F.C.), sponsored by Advocis, the Financial Advisors Association of Canada; and
- Chartered Financial Analyst (CFA), sponsored by the CFA Institute.

Under the proposed model, all financial advisors who hold themselves out as financial planners would be required to hold in good standing one of the above-noted financial planning designations. A DAA which established a "certified specialist" program would satisfy both the government's objective of protecting all consumers who receive financial advice with baseline standards, while providing the motivation for advisors to continue their education and achieve a specialization as a key competitive advantage in the marketplace.

Specific activities that should be included or excluded in a regulatory scheme

Included activities: Subject to several narrow and easily identifiable exceptions listed below, everyone who sells financial products to consumers, and everyone who offers financial advice and/or planning to the public, would be subject to regulation under the DAA model. This would include:

- individuals who are licensed to deal with the public with regard to life and health insurance under insurance legislation;
- individuals who are registered by a securities regulator in any advisor category under National Instrument 31-103 and are licensed to sell or provide advice to the public with respect to financial products;
- individuals who hold themselves out by titles or claimed credentials that suggest financial advice-giving expertise, such as "financial advisor," "investment advisor," "wealth planner," "wealth advisor," "financial planner," "estate planner," and "retirement planner" or such other titles as may be designated by regulation, regardless of whether they are required to be licensed or registered to sell or provide advice regarding financial products; and
- individuals who hold themselves out as pensions or group benefits consultants who are not otherwise captured by the criteria above.

Excluded activities: It is important to note that the DAA model will not capture job-related activities executed by these clearly identifiable classes of financial services practitioners whose activities may be characterized as a form of "financial advice," such as:

- mortgage brokers and real estate agents;
- bank tellers who offer advice about deposit products;
- licensed accountants who provide financial advice ancillary to their provision of accounting and tax advice; and
- lawyers who offer financial and tax advice ancillary to providing legal advice.

Costs and other burdens of regulation

The current regulatory burden on financial advisors and their firms is compounded by the fact that financial advisors are required to address regulation from different sectors that are directed to their conduct and relationship with consumers. Indeed, a financial advisor working with a single client and recommending products from the insurance and securities sector will have different obligations, depending on whether the product falls under the purview of FSCO, the MFDA, or IIROC. The result is that under the current system a financial advisor is spending an inordinate amount of time ensuring compliance with respect to the regulatory requirements of various sectors, as well as explaining to clients why they must treat the recommendation of the segregated fund differently from a mutual fund, and why the conversation with respect to an exchange-traded fund is different yet again. This level of complexity is the result of an outdated mode of regulation that is focused on product and was developed at a time when this made sense.

Regulation must be changed to recognize that an evolution has taken place in the provision of financial products and services and the advice which accompanies them. In short, the existing product-based regulatory framework is not adequate for governing the advisory relationship: it simply does not reflect the manner in which consumers receive advice today. Therefore, at least some new regulatory infrastructure will be required.

Many of the commentators at the Ontario Ministry of Finance's 2014 Roundtable *Sessions Investigating the Merits of More Tailored Regulation of Financial Planners in Ontario* on Friday, January 10, 2014 and Tuesday, January 14, 2014, were concerned about new regulatory costs that would be borne by firms and ultimately passed onto consumers. We agree with this policy position – we have no desire to create a costly new structure that renders the entire industry less competitive; after all, it is our members who are working with consumers face-to-face, and they will be the ones having to explain these costs to an unimpressed audience.

Fortunately, a new DAA to oversee the conduct and proficiency of all financial advisors does not require significant resources to implement. Nonetheless, there will be certain new costs associated with the proposal, including the cost of developing databases and websites, and establishing the disciplinary and hearing process. Yet these initial costs will be offset by the reduction in costs as existing regulators who were created to oversee brokers, dealers, and products will be able to focus their expertise on these issues and the delegated oversight of financial advisors that these entities have assumed will be transferred to the new DAA.

Notably, these costs are largely fixed costs that are required to set up base infrastructure; the variable costs of adding an additional advisor or planner to the structure are minimal. In fact, the greater the number of advisors in the structure, the lower the cost per advisor, which would mean that the membership fee payable by each registrant would be smaller if all advisors and planners are captured.

This is in contrast to statements made by certain proponents at the Ministry's roundtables; some participants suggested that regulating all advisors would be too ambitious and costly – instead, they argued, the regulatory initiative should focus only on financial planners. In truth, if regulation were to focus exclusively on planners, the fixed cost of that base infrastructure would have to be amortized over a much smaller base, resulting in much higher fees per planner. These financial planners would have to respond to the new and increased regulatory burden by jettisoning their less remunerative clients, as has happened in the United Kingdom with the advent of the Retail Distribution Review.

Public regulation is, of course, costly to taxpayers, at least some of whom do not consume the regulated service. In the case of self-regulation for financial advisors, the costs would be borne by the regulated actors in the financial advice sector, who would seek to split the costs of regulation only with those consumers using financial advice, further reducing costs for the end user or consumer. Therefore, we believe that any argument that governments or regulators should focus on professionalizing financial planners only on the basis of cost considerations is both contrary to the public interest and at odds with the economics of establishing regulatory infrastructure. As such, it is wholly inconsistent with sound public policy.

Regulation of compensation

The DAA would determine what the appropriate compensation models would be. Advocis believes in allowing consumers to choose the type of payment mechanism through which they wish to engage with their financial advisor, whether it is based on commission, a percentage charge on assets under management, or an hourly fee.[21] Our research indicates that removing choice will result in less access to financial advisors by those most in need of advice. Consumer outcomes in the United Kingdom and Australia – jurisdictions which introduced commission bans – demonstrate that eliminating embedded compensation drives advisors from the industry and forces the remaining advisors to increase their fees, thereby pricing advice beyond the reach of broad swaths of the population.

While the vast majority of consumers do not want to pay an hourly rate for financial advice, this option should remain, since it does accommodate the needs of a small but lucrative segment of consumers. Allowing for choice will ensure all consumers have access to advice, can grow their wealth, achieve their life goals, and mitigate against risks associated with their lifestyle and unique personal needs and characteristics. As a consumer's wealth grows, he or she may at any time choose to move from a commission based model to an hourly fee or an assets under management model – depending on which model is most economical for them.

Complaints and discipline mechanisms

What would the role of a DAA be when it comes to advisor discipline? Can a DAA be expected to handle complaints about its own members? Is the current set of mechanisms for the handling of client complaints and the meting out of discipline – which is admittedly patchwork by nature – at all sufficient to the tasks at hand? These are legitimate questions. As we will see below, anecdotal evidence suggests that registrants who are members of an SRO commit fraud or other forms of financial malfeasance at a lower rate than non-SRO registrants.

The Canadian Foundation for Advancement of Investor Rights ("FAIR Canada"), has issued two reports in the last four years which examine advisor malfeasance. It outlined a series of recommendations in an August 2014 report, including the idea that Canadian regulatory agencies must collaborate more

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[21] See the Appendix for Advocis, *Banning Embedded Compensation And Imposing A Statute-Based Fiduciary Duty* – Regulatory Affairs Bulletin #052- 04/13 (April 2013) and for Advocis' submission in response to the Canadian Securities Administrators' *Consultation Paper 33-403 – The Standard of Conduct For Advisers And Dealers: Exploring The Appropriateness of Introducing a Statutory Best Interest Duty When Advice is Provided to Retail Clients* (February 20, 2013).

effectively, especially in the tracking of fraud complaints, that regulators should publicize the results of their findings, and that governments and regulators in provincial capitals and in Ottawa should implement a national whistleblower program. In examining investment fraud in Canada, the definition of investment fraud was limited to fraud involving securities that directly affect individual retail investors, such as Ponzi schemes and boiler rooms. The report reviewed all of the fraud cases that were concluded by the CSA in 2012. The CSA's *2012 Enforcement Report* was the first to include a specific, stand-alone category for fraud. Upon FAIR's review of these cases, it was stated that the "overwhelming majority of the cases (fifteen out of eighteen) involved perpetrators who were not registered."[22]

In February 2011, FAIR Canada released *A Report on a Decade of Financial Scandals*, which reviewed fifteen of the largest and most high profile securities-related scandals from 1999 through the end of 2009. This report emphasized the fact that "the Canadian securities regulatory system is complex and fragmented. There are thirteen provincial and territorial securities regulators and two national SROs... With this bewildering array of regulators, investigation agencies and prosecutors, no one agency has ultimate responsibility for combating investment fraud."[23] It also stated that five of the 15 cases reviewed involved firms and individuals *not registered* with securities regulators and about 22% of the total loss could be traced back to non-registered individuals and firms.[24] More interestingly, while "approximately 78% of the Total Loss was attributable to registered firms or individuals," only "some 17% of the Total Loss involved registered firms or individuals who were also subject to the supervision of an SRO. It would therefore appear that registrants that are directly regulated by a provincial securities commission (but not an SRO) represent a much greater risk of investment fraud losses by investors than registrants that are also SRO members."[25]

Advocis has long advocated for the need to introduce a true system of professional accountability for financial advisors, one which is integrated across all consumer sectors in Canada's financial markets. A DAA would be empowered to suspend or revoke membership, or impose various conditions on membership for unprofessional conduct, including violations of regulatory requirements, failure to cooperate with regulators, and criminal and regulatory offences. Actions or omissions which impugn or bring into disrepute the advisor's professional integrity or competence, or that of the profession as a whole, and their suitability to offer financial advice to the public, would be reviewable.

As noted above, a regulatory requirement that advisors must be in good standing with a DAA would prevent unscrupulous individuals from simply moving to a different financial sector and seeking licensing or registration. The resulting regulatory umbrella created by this DAA model would close current gaps in the enforcement and disciplinary reach of regulators, by ensuring that individuals who violate industry requirements in any one sector would not be permitted to continue activity in the industry without proper review. A DAA would have discretion with regard to the investigation of complaints and the initiation of professional discipline.

In terms of the particulars of how the DAA model would handle issues of enforcement and discipline, the guiding principle would be the promotion of the public interest. Accordingly, the DAA should be a

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[22] FAIR Canada, A Report on a Canadian Strategy to Combat Investment Fraud (August 2014), p. 20. Online at http://faircanada.ca/wp-content/uploads/2014/08/FINAL-A-Canadian-Strategy-to-Combat-Investment-Fraud-August-2014-0810.pdf.

[23] FAIR Canada, A Report on a Decade of Financial Scandals (February 2012), p. 2. Online at http://faircanada.ca/wp-content/uploads/2011/01/Financialscandals-paper-SW-711-pm_Final-0222.pdf.

[24] *Ibid.*, p. 19.

[25] *Ibid.*, p. 20.

not-for-profit entity dedicated to financial advisor professionalism in the public interest. It is essential that the DAA be entirely independent from financial institutions, as well as product manufacturers and distributors.

The governance arrangements of a DAA would ensure that it would have public directors on its Board, and also on any board committee responsible for professional conduct and discipline. The following features would define the basic parameters of a DAA's disciplinary process:

- **a show-cause requirement:** the DAA would be entitled to require an individual who has had his or her license or registration suspended, cancelled or made subject to ongoing conditions in other jurisdictions, to show cause why he or she is fit to be accepted as a member or to continue as a member of the DAA;

- **effective sharing of membership information:** the DAA and other regulators would inform each other in a timely manner with regard to any changes in the membership and licensing or registration status of individuals. Upon being informed that the licensing or registration status of a member has been suspended, revoked, or made subject to conditions in any other jurisdiction, or that the member is the subject of disciplinary proceedings in another jurisdiction, the DAA would take appropriate steps. Similarly, regulators in other jurisdictions would initiate a review of the licensing or registration of an individual upon being informed by the DAA in one province that an individual has been suspended, or made subject to conditions, or that his or her license or registration has been revoked, suspended or made subject to conditions by another regulator;

- **a complaints and disciplinary process:** there would be no duplication of process or procedure here, as the DAA would not duplicate the enforcement and disciplinary functions of regulators. The DAA would assume the oversight currently residing with the MFDA, IIROC and FSCO in relation to the conduct and competency;

- **a priority given to matters of public protection:** as well, a DAA, in its complaints and disciplinary processes, would give priority to protecting the public by ensuring that only one body is overseeing conduct and redress. This ensures that consumers are no longer confused about which sector's regulator they need to raise their complaint with as all conduct issues related to the advisor/client relationship are addressed by the DAA in the first instance;

- **timely initiation of proceedings:** a DAA would be entitled to initiate disciplinary proceedings where there is reason to believe that a member has violated the code of professional conduct. Public directors of the association would participate in directing the investigation of complaints and the initiation of disciplinary proceedings. The association would be entitled to initiate disciplinary proceedings whenever it considers it appropriate to do so, and would be empowered, in the course of its disciplinary process, to suspend or terminate membership, and to impose conditions on membership;

- **oversight of issues relating to advisor competence and incapacity:** a DAA could investigate a member's competence and capacity to provide services to the public, and initiate proceedings and suspend or revoke membership or impose other conditions; and

- **imposition of appropriate and effective administrative sanctions:** a DAA would have the authority to suspend or terminate membership, and to impose conditions on membership for administrative reasons, including for non-payment of fees, for failure to fulfill continuing education requirements, and for suspension or termination of licensing or registration by a regulator in other jurisdictions.

- **a central consumer-facing registry:** The members of the DAA would be required to participate in a public registry of financial advisors, which would be accessible on the internet and through other appropriate modes of public inquiry. The public registry would enable any member of the public to conveniently access information about an individual's qualifications, registration/licensing status, and professional conduct as a financial advisor. Such a registry would include a history of all sustained complaints and disciplinary action, as well as information on any confirmed breaches of any section of the DAA's code of professional conduct.

CONCLUSIONS AND NEXT STEPS

We are in agreement with the MFDA that the regulatory landscape needs reform – the modern financial services sector has outgrown its product-based roots and it is time to take a closer look at the intermediaries who are at the core of the consumer's experience with the industry. Consumers should be able to trust that industry titles and designations are meaningful, and that those trumpeting such titles meet high standards of proficiency and ethics.

However, we strongly disagree with the proposition in the MFDA Consultation that the focus of these efforts be limited to financial planners, and specifically the four designations identified by the MFDA. We have argued that financial planning is an inexorable component of financial advice – all advisors conduct a degree of financial planning, as codified in existing practices, with specialist financial planning designations existing for those advisors that wish to enhance their planning skills further.

But relatively few consumers can afford a standalone holistic financial plan or access financial planning services separate and apart from a product transaction. If the goal of regulatory reform is to truly enhance consumer outcomes, then, it must address the manner in which the majority of consumers access financial advice and planning services. Therefore, governmental and regulatory efforts must encapsulate all intermediaries who purport to offer financial advice or planning to the retail public.

The most efficient and impactful way of doing this is to move away from product-based silos. The creation of a delegated administrative authority which reports directly to the Minister of Finance, with the concurrent divestment of those responsibilities from existing SROs, will elevate the regulatory importance of the advisor-client relationship in acknowledgement of that relationship's central importance to the consumer. The DAA will be better able to ensure advisor competency, ethics and discipline – but most importantly, it will align consumer expectations about advisor and planner titles, training and proficiency with regulatory reality.

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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