2010 Ontario Pre-Budget Submission

to the

Legislative Assembly of Ontario

Standing Committee on Finance and Economic Affairs

February 2010

Advocis®

The Financial Advisors Association of Canada

Executive Summary

- Professional financial advisors make a significant contribution to Ontario's economy. They are a vital resource, working with Ontarians to enable them to reach their financial goals and ensure their long-term financial security. Unfortunately, regulation tends to be skewed in favour of the business model of the largest market participants and imposes ever-increasing compliance burdens on small business financial advisors. As a result, professional financial advice is becoming less affordable and less accessible for consumers.
- The ability of Ontarians to plan, to save consistently and to invest prudently in order to ensure their long-term financial security has implications for the government's ability to pursue its priorities of job creation, health care, education, strong fiscal management and economic growth.
- Ontarians are best served by a competitive market for financial services that continues to offer consumers a range of choices, including access to small business financial advisors.
- Advocis strongly supports reforms to facilitate retirement saving and improve retirement income adequacy for all Canadians now and in the future.
- Financial services regulation should protect consumers without burying financial advisors under excess regulatory compliance burdens that have no proven consumer protection benefit.
- Governments and regulators should, in regulating the financial services industry, recognize the contribution of professional associations such as Advocis in helping financial advisors meet high standards for education, proficiency and ethical conduct.
- Advocis strongly supports the promotion of a sound retirement income system in Canada, and reforms to improve retirement income adequacy for Canadians now and in the future.

<u>Summary of Recommendations</u>

RECOMMENDATION 1: The Ontario Ministry of Finance should make it a priority to ensure that small business financial advisors and planners remain a vital part of a diverse and competitive financial services sector that offers consumers ample choice as to products and providers, and access to professional, independent financial advice.

RECOMMENDATION 2: The Ministry of Finance should establish clear policy objectives for its financial services regulators so that regulatory initiatives do not place an unfair burden of regulation financial advisors and planners.

RECOMMENDATION 3: Financial services regulators should consider principles and outcomes-based approaches before proceeding to impose prescriptive rules-based regulation.

RECOMMENDATION 4: The Ministry of Finance should require regulators, before imposing new regulatory requirements, to ensure that:

- the problem that the regulation is supposed to address is clearly identified;
- a robust objective cost-benefit analysis has been undertaken that considers the real costs to market participants of increased compliance burden as well as costs and benefits to consumers; and
- the viability of less prescriptive outcomes-based approaches is appropriately assessed.

RECOMMENDATION 5: The Ministry of Finance should encourage the regulators to work with the SROs (MFDA and IIROC) to ensure that financial advisors are consulted (independently from their dealer members) at an early stage in the policy development process whenever regulatory proposals are likely to affect them.

RECOMMENDATION 6: The Government should encourage small and medium-sized businesses to establish pension plans for their employees. Specifically:

a) Public policy should focus on how to improve the regulatory environment for defined contribution plans as the focus has been, to date, on defined benefit plans;
b) Regulations for defined contribution plans, including locking-in rules, should be harmonized between provinces and federally, to reduce complexities and costs for employers and employees;
c) The simplicity and transparency of defined contribution plans should be fostered through various measures such as having a limited range of investment options for most members of the plan and safe-harbour protection for employers or groups who follow such procedures;
d) Private sector retirement savings plans should have mandatory enrollment for employees, with opting out provisions, as the default option. This will likely result in more employees being a member of an employer sponsored plan; and
e) The Province should encourage the federal government to consider a number of tax changes such as contributions to retirement savings plans being determined on a life-time average basis; ability to make past service contributions to defined contribution plans; and increasing the age limit for contributions to retirement savings plans.

I. Introduction

Advocis appreciates the opportunity to make a pre-budget submission to the Legislative Assembly of Ontario Standing Committee on Finance and Economic Affairs (the "Committee").

Advocis – who we are

Advocis, The Financial Advisors Association of Canada, is the largest and oldest voluntary professional membership association of financial advisors and planners in Canada. Our association was founded in 1906, as the Life Underwriters Association of Canada.

More than five thousand members of Advocis in Ontario provide comprehensive financial planning and investment advice, retirement and estate planning, risk management, employee benefit plans and disability coverage, to more than a million Ontario households and businesses. Our members are provincially licensed to sell life and health insurance and mutual funds and other securities. Advocis members are for the most part independent owners and operators of small businesses, entrepreneurs who create thousands of jobs in every community across the province and Canada. Advocis members maintain lasting relationships with their clients based on trust. They help clients, young and old, individuals, families and businesses, to set financial goals, manage risks, save consistently and invest prudently.

Advocis members embody professionalism based on education, best practices, and high standards of proficiency and ethics. Advocis promotes the professionalism of financial advisors through:

- Advocis' Code of Professional Conduct;
- Guidance on best practices;
- Errors and omissions insurance coverage that protects consumers;
- Professional designations supported by a comprehensive curriculum and rigorous standards – Advocis' Chartered Life Underwriter (CLU) and the Registered Health Underwriter (RHU); and educational support for the attainment of the Certified Financial Planner (CFP); and
- Mandatory competency-based continuing education.

Advocis believes that:

1. **Ontarians should have ample access to professional financial advice, products and services and should be able to choose among a diverse range of financial service providers.**

2. **Independent-minded, entrepreneurial, small business professional financial advisors provide valuable service to Ontarians in delivering professional financial advice, products and services and have a significant place in the financial services sector.**

3. **The existing regulatory framework, and the direction in which regulation is being developed, does not favour choice and a diverse range of choices for Ontarians and is limiting access to professional financial advisors. The regulatory framework and the compliance burdens that are being imposed are skewed in favour of larger, integrated financial institutions.**

There are approximately 25,000 financial advisors and planners in the province of Ontario that help millions of people and businesses in their communities. Many are self-employed proprietors of small businesses that employ many people in their communities. In addition, a significant number of advisors are employees of mid-to-large sized financial institutions and dealers. Professional financial advisors are a vital part of the financial services marketplace and of their communities.

The past year has been difficult for many sectors of the economy. Advocis members have fared relatively well given that they develop long lasted relationships with their clients and assist them through all economic and financial market cycles. Advocis and its members did not ask the Government of Ontario for a handout or a subsidy.

Advocis is not calling for less regulation, but for more appropriate and effective regulation that will protect the public without hampering the ability of professional financial advisors to serve Ontarians in these challenging times.

We are calling on the Government to embrace smart, principles-based regulation that focuses on desired outcomes and recognizes the value of financial advisors to Ontarians, and engages financial advisors appropriately as stakeholders in the regulation of financial services to bring about a more level playing field in the financial services marketplace.

Consumer protection, access and choice

Consumers of financial advice, services and products need to be adequately protected and regulation should reflect the following:

- Consumers should be protected from the pressures that arise in the context of tied selling;
- Consumers' privacy should be protected;
- Consumers should receive advice about insurance products, including incidental insurance products, from advisors who are proficient, licensed and appropriately supervised;
- Consumers should have access to an effective consumer redress system.

Value of financial advice

Public policy should recognize the importance of access to affordable professional financial advice in helping Ontarians meet their long-term financial goals. Professional financial advisors are financial educators.

No one spends more time with consumers, explaining financial concepts and products, than the financial advisor.

Ensuring that Ontarians continue to have access to affordable financial advice that is provided by professional financial advisors will help make Ontarians more financially literate.

However, financial literacy and financial education are not a substitute for professional financial advice. Consumers should not be expected to serve as their own financial experts; they need access to affordable professional financial advice to help them achieve good financial outcomes and achieve their financial goals over the long term.

II. Supporting the Business of Financial Advisors

A diverse financial services sector is essential to ensuring that consumers continue to have access to the professional financial advice they need. That access is threatened by the increasing burden of detailed, compliance-heavy, rules-based regulation that typically favours the business model of large financial entities. Increasing compliance costs are more easily borne by large financial institutions and their compliance departments, which benefit from economies of scale, than by smaller enterprises.

Professional financial advice is becoming less affordable and less accessible for Ontarians. The increasing cost of providing financial services to Ontarians by financial advisors threatens to make professional financial advice unaffordable. All regulated financial service providers are obliged to cover a wide range of costs if they are to remain in business. They have to pay for legal and regulatory advice, compliance staff, regulatory fees, SRO membership, increased liability risks, time spent explaining forms to clients, etc. The increasing regulatory burden and cost of compliance for smaller market participants is contributing to increased concentration in the delivery of financial products and services. Ever fewer, large financial entities offer consumers less choice, particularly in smaller communities.

Skewed regulation disadvantages smaller enterprises

In our experience, financial services regulators prefer to regulate large enterprises. It is administratively simpler and more efficient for the regulators to deal with a few large organizations, than with a myriad of smaller ones. The regulators apparently consider that the smaller enterprises and independent practitioners represent an outmoded and declining business model.

Regulators prefer to deal with large players as they are able to devote substantial resources to consultation and to managing their relationships with the regulators. Their resources and scale enable them to develop and administer large-scale compliance systems. They tend to be the main stakeholder at the table with the regulators, and accordingly are able to influence the direction of regulation to ensure that it accommodates their business models.

In developing regulatory policy, regulators are largely indifferent to the impact on small practitioners and their requirements to hire dedicated compliance staff, lawyers, accountants, information and records managers in order to meet regulatory standards that have been designed with and for the larger players. The larger players, on the other hand, have no great difficulty meeting these types of requirements.

Regulation that only “works” for large enterprises threatens the long-term viability of smaller players such as small financial advisory businesses. Just as the capital markets regulators across Canada accommodate small issuers and do not apply a “one size fits all” approach to the raising of capital, so too should securities and mutual fund regulators accommodate smaller enterprises by ensuring that regulation also works for smaller enterprises.

RECOMMENDATION 1: The Ontario Ministry of Finance should make it a priority to ensure that small business, and entrepreneurial financial advisors and planners continue to be a vital segment of the financial services sector in order to create diversity in the marketplace, provide ample choice for consumers and allow consumers to access professional, objective financial advice.

RECOMMENDATION 2: The Ministry of Finance should establish government policy objectives for its financial services regulators so that:

- **Regulatory initiatives do not place an unfair burden of regulation on one segment of the industry versus another and maintain a level playing field at all times; and**
- **New regulations are examined carefully to determine if they have major implications for consumer choice.**

III. The Need for Smarter Regulation

The direction of regulation in Ontario makes it increasingly difficult for financial advisors to serve Ontarians. A better, smarter approach to regulation is required.

More and more rules from the Ontario Securities Commission, the Mutual Fund Dealers Association (MFDA) and the Investment Industry Regulatory Organization of Canada (IIROC) are imposing large compliance costs on financial advisors, often without clearly offering meaningful consumer protection benefits.

Increasing compliance costs present a competitive challenge to small, independent financial advisors. These costs are more easily borne by large financial institutions and their compliance departments, which benefit from economies of scale, than by the smaller enterprises that offer alternatives to consumers. This ultimately threatens consumer access to independent financial professionals.

Flexible, principles-based regulation (PBR) that focuses on desired outcomes offers a smart alternative to the rule-bound approach designed for large compliance departments and employee sales-forces. Emphasis should be placed on compliance with general principles, and less emphasis on detailed rules, in order to achieve desired outcomes. It is important for regulators to work with industry and professional associations to develop standards that protect the consumer. This approach promotes the professionalism of financial advisors, and results in a smarter, more flexible and more efficient approach to regulation.

Rules that impose additional compliance burdens on compliant advisors do not serve the public interest. Regulators should focus the majority of their efforts on enforcement and punishing misconduct and fraud in the marketplace.

As an example of effective PBR, insurance regulators in Ontario and across Canada have worked with the insurance industry to implement a largely principles-based approach to conflict of interest and product suitability applied to insurance advisors and companies when recommending insurance products to clients. In 2006, the Canadian Council of Insurance Regulators and Canadian Insurance Services Regulatory Organizations recommended principles to promoting best practices and managing conflicts of interest. The CCIR Principles emphasize:

1. Priority of the client's interest;
2. Meaningful disclosure of real or perceived conflicts of interest; and
3. Product suitability.

These principles have been communicated to the entire industry and insurance regulators have found that a significant proportion of advisors and companies are adhering to them. The reason for this is that the industry was tasked with developing the specific guidelines and requirements in order to ensure the principles are adhered to, and the industry responded quickly. The insurance industry has the flexibility to devise the most appropriate guidelines that will result in the highest degree of adherence and compliance. Advocis strongly believes that this approach works for consumers, advisors, companies and regulators and needs to be integrated into the securities regulatory framework.

RECOMMENDATION 3: Financial services regulators should consider principles-based approach to regulation focused on achieving outcomes, before proceeding to impose prescriptive rules-based regulation.

Justifying regulation should be mandatory

Regulators should be required to justify prescriptive regulations that add to the cost of professional financial advice. If regulation is not clearly necessary and cost-effective, and is not clearly superior to less prescriptive measures, it should not be imposed.

Whenever rules and regulations are proposed, they should be supported by credible cost-benefit analysis and consideration of less burdensome alternatives. All too often, prescriptive regulation has been proposed and implemented without serious consideration of costs and benefits and without consulting all relevant key stakeholders, including consumers.

RECOMMENDATION 4: The Ministry of Finance should provide a mandated guideline to the regulators, and to the recognized SROs that are supervised by the regulators, to ensure that any new regulatory requirement that may increase regulatory and compliance burdens and costs in the financial services sector is fully justified. In particular, regulatory requirements that are likely to increase regulatory and compliance burdens and costs should be supported by:

- **a clearly articulated statement of the problem or problems that the regulation is meant to address;**
- **credible cost-benefit analysis that takes into account the costs to market participants of increased compliance burden and potential costs and benefits to consumers; and**
- **an assessment of the viability of less prescriptive outcomes-based approaches.**

IV. Improving the Policy Development Process

The policy development process of the OSC and through the OSC's recognized SROs, the MFDA and IIROC (the SROs), would be improved, if financial advisors were recognized as important stakeholders, who should be at the table, especially at the early stages of regulatory policy development. [See APPENDIX A, Financial Services Regulation in Ontario: The Key Players for an outline of the regulatory framework of financial advisors].

The SROs understandably look to their member firms as their primary stakeholders when consulting on regulatory proposals. Historically, the regulatory staff of the SROs has given little consideration to the impact of regulatory proposals on financial advisors. Financial advisors who are often Approved Persons or sales representatives of SRO members are not usually consulted about initiatives that will affect them directly, especially in the early stages of regulatory policy development.

Financial advisors deal directly with consumers, and would bring an important perspective to the table. We strongly believe that any initiative that will change how financial advisors interact with their clients should have their input. As the largest association of financial advisors, Advocis wishes to be involved in developing, reviewing and commenting on proposals that will affect our members, the advisor community and consumers.

It is our hope that other Canadian regulators will follow the example set by insurance regulators as a model for undertaking meaningful public consultations with consumers, financial advisors and other market participants. Our experience has been that insurance regulators interact with stakeholders much more effectively at early stages of regulatory policy development. The Financial Services Commission of Ontario does a significant amount of work in identifying problems or potential problems, and in gathering the appropriate information and statistics to support its views in cooperation with the industry before it proposes regulatory changes. In addition, insurance regulators often look at industry best practices and outcomes-based principles as one option to deal with issues that may arise.

RECOMMENDATION 5: The Ministry of Finance should develop policies and procedures for regulators (including SROs) to ensure that all stakeholders that are likely to be directly affected by regulatory proposals are consulted at an early stage in the policy development process.

Ontario's ongoing role in securities regulation

The Government of Ontario needs to maintain a strong role in shaping securities law and policy in Canada. We accordingly encourage the Ontario government to ensure that through the establishment of a Canadian Securities Commission that it maintains an ongoing strong role in regulatory policy development.

V. Improving Retirement Income and Financial Security of Canadians

Advocis strongly supports the promotion of a sound retirement income system in Canada, and reforms to improve retirement income adequacy for Canadians now and in the future.

Advocis released a study in September 2009 entitled *"Encouraging Small and Medium Sized Firms to Participate in Pension Plans"*. The study promotes discussion of the public policy issues around how to increase pension plan participation and promote a sound pension system. The study examined existing barriers to establishing and maintaining pension plans and incentives to encourage small and medium sized employers to participate in pension plans. In addition, the study looks at other key aspects of the retirement income system in Canada and offers some practical solutions to improving the system.

Many Canadians will not have adequate income at retirement. Only one-third of Canadian households are currently saving at levels that will generate sufficient income to cover their non-discretionary expenses in retirement.

Employer-sponsored pensions are an important source of retirement income. Retirement income adequacy will likely decline if employment pension coverage continues to decline:

- The number of Canadian employees who are participating in any form of employer sponsored pension plan has been declining; and
- Two-thirds of Canadian employees do not have an employer-sponsored pension plan.

The study concludes that the most appropriate type of employer sponsored pension plan is a defined contribution (DC) pension plan, especially for small and medium sized businesses.

RECOMMENDATION 6: As provincial and federal governments work towards cooperative approaches to the issue of reform of the retirement income system, Advocis urges the government to consider the following recommendations in order to encourage small and medium sized businesses to set up pension plans for their employees:

a) Public policy should focus on how to improve the regulatory environment for defined contribution plans as the focus has been, to date, on defined benefit plans;
b) Regulations for defined contribution plans, including locking-in rules, should be harmonized between provinces and federally, to reduce complexities and costs for employers and employees;
c) The simplicity and transparency of defined contribution plans should be fostered through various measures such as having a limited range of investment options for most members of the plan and safe-harbour protection for employers or groups who follow such procedures;
d) Private sector retirement savings plans should have mandatory enrollment for employees, with opting out provisions, as the default option. This will likely result in more employees being a member of an employer sponsored plan; and
e) The Province should encourage the federal government to consider a number of tax changes such as contributions to retirement savings plans being determined on a life-time average basis; ability to make past service contributions to defined contribution plans; and increasing the age limit for contributions to retirement savings plans.

VI. Conclusion

Government should offer ongoing direction to regulators to ensure that Ontarians have access to professional financial advice and choice in financial services. Accordingly, **we urge the Ministry of Finance to offer direction to the Ontario Securities Commission, and through the OSC to MFDA and IIROC, with the primary goals of:**

- preserving consumer choice and access to professional financial advisors and to a range of choices in the financial services marketplace;
- ensuring that financial regulation is even-handed and does not favour large players and their economic model over small, entrepreneurial financial advisors;
- ensuring that independent financial advisors are consulted as key stakeholders in respect of proposed regulatory initiatives that affect them;

- ensuring that new rules and compliance burdens are only imposed when necessary to address clearly identified problems, and only after less costly principles-based approaches have been considered; and
- encouraging regulators to conduct objective cost-benefit analysis of regulatory proposals before implementing them.

As provincial and federal governments work towards cooperative approaches to the issue of reform of the retirement income system, Advocis urges the government to consider its recommendations in order to encourage small and medium sized businesses to set up pension plans for their employees and to improve the retirement income system in Canada.

Advocis would welcome the opportunity to work with the Ontario Ministry of Finance to provide further input regarding our recommendations.

APPENDIX A

Financial Services Regulation in Ontario: The Key Players

The Ontario Securities Commission (OSC) is the Ontario government agency that administers the Ontario Securities Act and regulates investment and mutual fund dealers and their salespersons who distribute financial products. The primary mandates of the OSC are investor protection and fostering of fair and efficient capital markets. The OSC is accountable to and subject to oversight by the Minister of Finance. OSC rulemaking is subject to approval by the Minister.

The Financial Services Commission of Ontario (FSCO) is the Ontario government agency responsible for administering the Insurance Act and regulating the insurance industry, in particular the distribution of insurance products to consumers. FSCO reports to the Minister of Finance.

Much of the day-to-day regulation of investment dealers and mutual fund dealers and their sales forces is undertaken by two self regulatory organizations (SROs), the Investment Industry Regulatory Organization of Canada (IIROC) and the Mutual Fund Dealers Association of Canada (MFDA).

Both IIROC and the MFDA have been formally recognized as SROs by the OSC. They are subject to regulatory oversight by the OSC and other provincial securities regulators.

Oversight

The OSC and FSCO, as government agencies, are responsible for carrying out their legislative mandates and are subject to direction by the Minister of Finance. They also are responsible for carrying out their mandates in a manner that is consistent with government policy.

The Government of Ontario historically has accorded wide latitude to the OSC and FSCO in carrying out their mandates, and does not interfere in their exercise of the agencies' quasi-judicial functions. The Government also has historically refrained from other, "political" interference in the agencies' activities.

Ultimately, the government through the Minister of Finance is responsible for supervising these government agencies (and their oversight of the SROs) so that they carry out their mandates in a manner that is consistent with the goals of government policy.

The Province of Ontario is participating in the initiative to establish a Canadian Securities Commission (CSC), which, if fully implemented, will supersede the OSC.