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The Government of British Columbia, represented by its Minister of Finance
The Government of Ontario, represented by its Minister of Finance
The Government of Saskatchewan, represented by its Minister of Justice and Attorney General
The Government of New Brunswick, represented by its Minister of Justice
The Government of Prince Edward Island, represented by its Minister of the Environment, Labour and Justice and Attorney General
The Government of Canada, represented by the Minister of Finance of Canada

(collectively, the "Participating Jurisdictions")

VIA EMAIL: commentonlegislation@ccmr-ocrmc.ca

Dear Sirs/Mesdames:

Re: Cooperative Capital Markets Regulatory System
Commentary on Draft Legislation

On behalf of Advocis, The Financial Advisors Association of Canada, we are pleased to provide our comments in regards to the draft legislation released on September 8, 2014 in furtherance of the cooperative capital markets regulatory system (the "Cooperative System").

About Advocis

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

As a voluntary organization, Advocis is committed to professionalism among financial advisors. Advocis members adhere to a professional Code of Conduct, uphold standards of best practice, participate in ongoing continuing education programs, maintain professional liability insurance, and put their clients' interests first. Across Canada, no organization's members spend more time working one-on-one on financial matters with individual Canadians than do ours. Advocis advisors

are committed to educating clients about financial issues that are directly relevant to them, their families and their future.

Introductory Comments

Advocis has long supported the concept of a national securities regulator to the extent that it harmonizes securities regulation across the country and minimizes regulatory duplication and inter-provincial barriers to capital markets. We applaud the Participating Jurisdictions for proposing the Cooperative System as an outstanding example of how federalism can respond to modern economic needs within the framework of Canada's constitution.

The Participating Jurisdictions' release of the draft provincial *Capital Markets Act* ("PCMA") and federal *Capital Markets Stability Act* ("CMSA", and together with the PCMA, the "Draft Legislation") is a major milestone towards the realization of the Cooperative System. We appreciate that the PCMA is based on existing provincial securities legislation, as many aspects of Canada's securities regulatory regime work well, while the CMSA creates several new regulatory powers intended to manage systemic risk. In our view, the release of the Draft Legislation provides a rare – perhaps generational – opportunity to fundamentally rethink securities regulation and address longstanding structural issues.

On that basis, we raise the following points of discussion that we believe would enhance the Draft Legislation and the operation of the Cooperative System, both for independent financial advisors and the millions of Canadian households that they serve:

(i) The need for principles-based regulation;
(ii) Re-examining the role and regulation of financial advisors;
(iii) The regulation of segregated funds;
(iv) Advisor representation in the Cooperative System;
(v) Advisor incorporation; and
(vi) Checks and balances in the Draft Legislation.

We discuss each of these points in turn.

Discussion

(i) <u>The need for principles-based regulation</u>

We urge the Participating Jurisdictions to approach the development of the Draft Legislation, including all related regulations, instruments and policies, using a framework of principles-based regulation ("PBR"). In a PBR environment, the regulator determines the overarching goals to be achieved, and the regulated industry works hand-in-hand with regulators to design the rules and procedures that will achieve those goals.

PBR allows for smarter and stronger regulation because the avoidance of a rule or policy based on mere technical interpretation becomes nearly impossible: registrants must satisfy both the spirit and the letter of the rule. It places greater emphasis on individual accountability: without

prescriptive rules for dictating compliance, the individual is ultimately responsible for achieving the intended regulatory outcome through his or her own decisions.

Advocis' *Code of Professional Conduct*[1] mirrors this approach through the establishment of broad principles regarding business conduct; the Code specifically addresses the best interest of the client and the need to act with integrity and competently, and in accordance with the spirit and letter of the law. These general principles are supported by explanatory notes and demonstrate the positive effect that PBR can have through allowing those who are regulated to help define the details.

PBR also demands an increased role for industry associations and professional bodies to share insights about business practices with regulators and to help develop pragmatic and workable solutions to reach shared goals. Guidance developed by industry makes use of the industry's time-tested expertise and results in a closer fit with commercial good practice. This collaborative approach avoids prescriptive "top down" rules that can create a variety of unintended consequences and seriously harm the viability of small businesses. It also creates the salutary effect of greater industry "buy-in", as industry desires to be part of the solution.

PBR results in more effective delivery of the regulatory outcome that the regulator seeks to secure, reduced compliance costs for industry, and reduced resource demands on the regulator. Given the tremendous benefits of PBR, we urge the Participating Jurisdictions to utilize this framework wherever possible in developing the Draft Legislation for the Cooperative System.

(ii) Re-examining the role and regulation of financial advisors

Prudent regulation should ultimately be about balancing consumer protection with the need to foster an environment where businesses (and particularly, small businesses) can succeed, always with a focus on the consumer's perspective. And the cornerstone of most Canadians' experience with the securities sector is the relationship they have with an advisor.

From the perspective of consumers, a financial advisor is an expert who gathers information about the client's financial situation, and helps establish goals and a roadmap to achieve those goals. To this point in the relationship, the financial advisor is operating independently and not as the agent of any particular dealer. It is only when the advisor identifies one or more products that can achieve the client's plan, and the client accepts the recommendation, that the financial advisor also assumes the role of agent for the dealer in the execution of the trade. However, the current regulatory structure does not recognize the multi-faceted role of the advisor and focuses instead on the dealer firm registrant, largely seeing the advisor as an agent or employee of the dealer.

For example, most provinces have delegated significant oversight responsibilities to SROs such as the MFDA and IIROC. The regulatory focus of these SROs is to address the risks that are inherent to their dealer-members in their business with clients and the handling of client assets, which is a role the SROs perform reasonably well. However, SROs are also responsible for the oversight of financial advisors, and the rules they promulgate demonstrate a lack of understanding of the role played by advisors. This is not surprising, given the remoteness of the relationship that exists

[1] Available at http://www.advocis.ca/forPublic/codeConduct-pub.html.

between the SROs and the advisor: in the eyes of SROs, advisors are mere "approved persons" or "registered representatives" rather than critical participants in the client experience.

The role of the financial advisor is too important to the consumer experience to be treated as an afterthought. 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, but the reality is that this is not always the case. In fact, the public is exposed due to four major flaws in the existing regulatory framework, none of which will be addressed by the Cooperative System:

(a) Anyone can call themselves a financial advisor and offer planning and advice.

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 nor the scope of work is protected, so there is nothing that prevents someone from calling themselves an advisor and offering what they purport to be financial advice to the public, even if they have no training, experience or financial acumen.

This is an extreme risk that must be addressed; time and time again, 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. Consumers 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 – which could leave the public vulnerable to outright fraud or incompetence.

(b) Existing regulation is focused on the sales of products, not the ongoing relationship of trust between financial advisors and their clients.

The existing regulatory framework does not reflect the manner in which most consumers receive financial advice. Existing regulation of financial products is based on the type of product sold, whether mutual funds, other securities or insurance products (in the case of multiple-licensed advisors, which include the vast majority of our members).

In practice, the consumer does not think of the financial industry in such "silos". Instead, consumers visit their financial advisor to develop holistic plans, and the advisor uses their knowledge and experience to recommend a portfolio of suitable products to fulfill those plans across the mutual fund, securities and insurance worlds. That is, it is often the case that the client-advisor relationship is regulated not by a single entity, but by a combination of them.

Most consumers are not particularly interested in knowing that product *x* falls within the insurance universe and product *y* falls within the mutual fund universe – instead, they want their advisor to be professional, knowledgeable and accountable, so that the advisor can provide the complete coverage they need. But in the current regulatory framework, the protections that consumers receive do vary based on the sector of the product's origination. We have seen the importance of this distinction coming to light when problems arise, leaving consumers confused and disappointed.

We believe that consumers should enjoy high degrees of protection throughout their advisory relationship that is not dependent on the nature of the underlying products in their portfolios. There should be an overarching code of conduct, high initial and ongoing education standards and a requirement to maintain responsible levels of errors and omissions insurance, none of which exist today.

This sectoral approach also highlights why existing SROs cannot effectively regulate the advisory relationship. While we recognize that SROs have, in recent years, been more attuned to the client-advisor relationship, such as through the Client Relationship Model reforms, they are structurally limited by their jurisdiction of authority; for example, even if IIROC were to completely overhaul its expectations of registered representatives, those changes would only impact the consumer's relationship in regards to his or her purchases of IIROC-regulated securities products – the consumer's experience for insurance products or mutual funds would be unaffected. Since the current SRO-based structure will persist under the Cooperative System, so will these consumer protection vulnerabilities.

In an ideal world, all regulatory authorities would set uniform, principles-based standards so that the consumer would be equally protected, regardless of the product's origination. But our 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, with standards that (in some cases) vary widely from each other, asking them to coordinate policies on financial advice is an exercise in futility. And even if most regulators did agree to a uniform set of policies, such as through the implementation of the Cooperative System (for the securities sector, at least), those policies would do nothing to capture those individuals who are not registrants of any regulator, such as the fee-only planner who does not sell products.

(c) There is no firm and clear requirement for advisors to keep their knowledge current.

One of Advocis' core membership requirements is that advisors keep their knowledge current 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 complete 30 hours of education every two years, without any special provision for professionalism or ethics, whereas some other provinces do not have any requirements at all for their licensees. And while IIROC has continuing education requirements for certain registered representatives, the MFDA is still contemplating its requirements and, in the meantime, only states that continuing education "should be provided" to its approved persons. And those advisors who are not registered with any regulator have no continuing education requirements whatsoever.

An advisor who does not keep their knowledge current is an advisor that puts their clients at risk; in this industry, competition amongst insurance carriers and distributors, and securities dealers is fierce, so product change and innovation is constant. Therefore, static knowledge quickly becomes obsolete and harms an advisor’s ability to properly serve their clients.

Advocis believes that all individuals offering financial advice to the retail consumer should be required to complete continuing education on a regular basis, which includes an emphasis on education related to professionalism and ethics.

(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 planned and, sometimes, this is the fault of the advisor. The industry requires a strong and effective disciplinary process to ensure that those advisors who have committed misconduct are appropriately disciplined in the interest of protecting the public and deterring others from similar behaviour.

Individually, regulators are empowered to impose a wide variety of sanctions, including stripping advisors of their license or registration. However, the limitations of the existing product-based regulatory framework are most apparent when it comes to discipline: each regulator's enforcement powers are limited to its respective sector. This means that, for example, if an advisor commits misconduct in the sales of mutual funds that is so egregious that the MFDA determines he is unfit to work in the industry and revokes his registration, there is nothing that prevents that same advisor from continuing to advise on and sell segregated funds through his 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, speak to that advisor's conduct and ethics and are not sector-specific concerns; letting such an advisor continue offering "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 could "advise" clients to invest in an affiliate's ponzi scheme.

Also currently lacking is an easy mechanism for the public to verify their advisor's credentials and disciplinary history. While regulators do maintain websites where the public can search for information on their advisor, the information returned is only applicable to the regulator's sector. As discussed above, the general public does not understand the difference between the various regulatory bodies and is not likely to canvass each one to look up their advisor. In the example above, if a prospective client were to look up the advisor on only the insurance regulator's website, the client would not see the advisor's expulsion from the mutual funds sector. The client might then mistakenly believe that the advisor's overall disciplinary history was clean. This problem would still exist under the Cooperative System as it would pertain only to the securities sector.

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 or planning without the sales of products who are therefore not registered with any existing regulatory authority. That is, rather than being based on the archaic sales-based regulatory structure, this critical consumer tool must be designed from the consumer's point of view.

These four major shortcomings of the 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 that most consumers receive, and unfortunately, the Cooperative System would not address these concerns.

Our proposal for advisor regulation: Raising the Professional Bar

Fortunately, Advocis has developed a solution that is simple, straightforward, and does not require significant government resources to implement.

Called *Raising the Professional Bar*, our solution requires that anyone who holds himself out as a financial advisor, or who is in the business of offering financial advice or planning services to the retail public, be a member in good standing of an accredited professional association. We have enclosed a copy of the proposal with this submission; the details are provided therein, but below is a summary of its key features.

To be accredited, the professional association would be required to have certain characteristics, including: a code of conduct; a requirement that members maintain errors and omissions insurance; initial proficiency and continuing education requirements; and a complaints and disciplinary process that empowers the association to suspend or cancel the advisor's membership.

The association would also maintain a public-facing database whereby consumers can conduct a "one-stop" check of a prospective advisor's credentials and disciplinary history. Unlike the registries currently maintained, which only contain information pertaining to the advisor's activities in the regulator's respective sector, the association's registry would be based on the *conduct* of offering advisory services to the retail public. It would therefore transcend product sectors. This focus on scope of work and conduct would also capture those advisors and planners who are currently not registrants of any regulator.

The solution could work hand-in-hand with existing SROs and the Cooperative System, complementing each other's work without overlapping responsibilities. For example, if the MFDA suspends an advisor's registration due to fraud or gross negligence, the association would also suspend that advisor's membership on matching terms; this would effectively prevent that advisor from potentially harming clients in the insurance sector while he waits out the MFDA suspension. This gives true effect to the intent behind sanctions, rather than their too-often current role as a simple administrative barrier that can be subverted.

The solution provides benefits to all market participants: first and foremost, consumers would benefit from knowing that all advisors meet proficiency requirements, just as they do with their architects or engineers. They would also benefit from the simple way to verify their advisor's credentials and disciplinary history, without having to navigate the maze that is the current regulatory landscape. Finally, they would enjoy the support of a disciplinary system with teeth: it would be a system that actually protects the public, rather than potentially off-loading one sector's problem onto another sector and a new set of unsuspecting consumers.

Financial advisors would also benefit from enhanced public trust, status and confidence as true professionals, and we know that our members would be very supportive of unethical colleagues who tarnish their collective reputation being removed once and for all. Participating Jurisdictions would benefit from enhanced consumer outcomes, including reduced public financial reliance, and the expertise and support of professional associations in crafting and implementing their policy agenda. Product providers and distributors would benefit from the professionalism of the advisors who represent their companies to the public on a day-to-day basis.

The solution would also be an excellent opportunity to put PBR into action: it would bring industry associations to the table and would leverage their expertise to good use in an area that has not been well-addressed by existing regulation. By adopting this solution, the Participating Jurisdictions would signal that, in the new Cooperative System, the advisor-client relationship is of critical importance and would be a clear example of the Cooperative System bringing about a tangible improvement to securities regulation in Canada.

We have discussed the solution with provincial governments across the country and many have expressed interest in promulgating legislation that would move it forward. In fact, in February 2014, legislation was introduced in Ontario that would implement the solution by recognizing professional associations as delegated administrative authorities of the financial advisory profession.[2] While that particular bill died on the order paper with the calling of the Ontario election, we believe that given its strong multi-party support, a similar bill will be reintroduced in the current session.

This is only an introduction to our solution; there are many more details in the enclosed document and we strongly encourage the Participating Jurisdictions to review it as part of its current work. We believe that the proposal strikes a careful balance between leveraging the strengths of the existing regulatory framework and adding those elements that would truly allow for increased professionalism and consumer protection in the industry.

(iii) <u>The regulation of segregated funds</u>

Financial products are becoming increasingly complex, offering a combination of characteristics that cross traditional product sectors. For example, segregated funds are subject to three different regulatory regimes, administered by two different levels of government for different purposes: by federal legislation/regulation as it pertains to solvency and corporate governance of life insurance companies; by provincial securities legislation/regulation as it pertains to the underlying fund; and by provincial insurance legislation/regulation as it applies to market distribution, consumer protection and generally-applicable elements of all life insurance contracts.

Given this convergence in financial products, we have expressed the belief that great care must be exercised to ensure the fair and equitable treatment of stakeholders in different sectors. We believe that the existing regulation of segregated funds is working well; absent compelling evidence of a problem with current regulation that could not be properly addressed within the existing

[2] The text of the bill is viewable at http://www.ontla.on.ca/web/bills/bills_detail.do?locale=en&BillID=2934.

structure, the Participating Jurisdictions should ensure the Draft Legislation and regulations avoid infringing on, and duplicating, the existing insurance-based regulation of the distribution of segregated funds.

However, the CMSA appears to do just that. In Section 2 of the CMSA, "security" is defined as including "any contract, instrument or unit commonly known as a security", which could capture the concept of segregated funds. Note that the PCMA, as well as existing provincial securities acts, include a carve-out to exclude segregated funds by explicitly stating that the concept of "security" excludes "a contract of insurance issued by an insurance company governed by the laws of Canada or of a province". The CMSA should be modified to include a parallel carve-out.

The existing insurance-based marketing and distribution regulatory requirements for segregated funds have proven effective in protecting consumers. Segregated funds, like other life insurance products, are subject to the provisions in provincial insurance acts and guiding principles set out by the Joint Forum of Financial Market Regulators in their 2005 document *Principles and Practices for the Sale of Products and Services in the Financial Sector*, which was endorsed by all provincial insurance and securities regulators across Canada.

Like all other life insurance products, the marketing and sale of segregated funds is subject to the three key principles-based recommendations for managing conflicts of interest established by the Industry Practices Review Committee of the Canadian Council of Insurance Regulators ("CCIR") and the Canadian Insurance Services Regulatory Organizations in 2006:

- *priority of client's interest* – an insurance intermediary (broker or agent) must place the interests of insurance policyholders and prospective purchasers ahead of his or her own interests;
- *disclosure of conflicts or potential conflicts of interest* – consumers must receive disclosure of any actual or potential conflicts of interest associated with a transaction or recommendation; and
- *product suitability* – the recommended product must be suitable to the needs of the consumer.

In addition, advisors are required to follow the steps set out in the Canadian Life and Health Insurance Association Guideline G2, *Individual Variable Insurance Contracts (IVICs) Relating to Segregated Funds*, which has been endorsed by the CCIR. These steps include delivery of the Information Folder and compliance with revised point of sale requirements as set out by the Joint Forum in Framework 81-406, *Point of sale disclosure for mutual funds and segregated funds*. Insurance regulators are also currently in the midst of updating their suitability processes to reflect recent industry change.

It is important to keep in mind that the existing exemption for segregated funds was crafted to serve an important consumer protection purpose: as an insurance policy, the Canada Revenue Agency permits a death benefit to a beneficiary to bypass the estate of unitholders. If segregated funds are redefined as securities, the estate planning decisions of millions of Canadians would potentially be at risk. Such a change would be an enormous disservice to the public and we find it unlikely that the Participating Jurisdictions intended to bring about this result.

In our view, the existing regulatory framework governing segregated funds is appropriate and can deal effectively with any emerging issues. The Participating Jurisdictions must ensure that in developing the Cooperative System, the current regulation of the distribution of segregated funds remains intact.

(iv) Advisor representation on Authority

The Cooperative System will be administered by an Authority that is supervised by an expert board of independent directors (the "Board"). According to the commentary released contemporaneously with the Draft Legislation, the Participating Jurisdictions intend the Board to be composed of experts who collectively possess a wide-ranging span of capital markets expertise and are broadly representative of all regions of the country.

We concur that the Board should represent the spectrum of participants in the securities market – doing so will result in regulation that is reflective of the diverse needs of all stakeholders. In selecting candidates for the Board, we believe that market expertise should be given greater weight than geographic representation. Further, we strongly recommend that, as one of the constituencies to be represented on the Board, a seat be reserved for a representative of financial advisors.

We understand that this is a significant request, but given the critical importance of advisors to the consumer's experience in the securities market and the fact that the existing product-focused regulatory structure does not properly recognize the role of advisors, we believe that a reserved seat is warranted.

It is notable that of the constituencies that may be represented on the Board, such as dealers, fund manufacturers, leading academics, or purported "investor advocates", none have as much direct contact with consumers as financial advisors. Advisors are the front-facing representatives of the securities sector, and meet with consumers on a daily basis to discuss their needs and concerns. Advisors are uniquely positioned to raise the consumer's perspective at the Board; we strongly believe that the Board would be incomplete without advisor representation.

(v) Advisor incorporation

One of the key benefits of the Cooperative System is that it will harmonize provincial securities acts across the country, eliminating variations across provinces that have served as longstanding irritants for stakeholders who operate in more than one jurisdiction. A notable example of such an ongoing problem pertains to advisor incorporation: advisors are permitted to incorporate their practices in most, but not all, provinces. This is exacerbated by the variability across platforms: in most provinces, MFDA registrants have been granted the option to incorporate, but IIROC registrants have not, and in comparison, insurance licensees have been able to incorporate for many years.

Incorporation is a modern and efficient business structure that offers many practical advantages and is widely used by small business owner-operators in other professions, such as lawyers,

accountants and real estate agents. It would promote the viability of independent advisors by reducing administrative red-tape: it makes little sense that dual-licensed advisors must maintain separate books and records for each of their insurance practice and securities practice, particularly as the advisor engages his expertise in both sectors to holistically service the same clients. Incorporation is also beneficial to consumers as their affairs are dealt with by a corporate entity which provides continuity beyond any individual advisor and greatly assists in succession planning.

Advocis has argued that securities regulators should level the playing field across provinces and platforms by establishing a permanent, legislated, solution that affords advisors the benefits of incorporation but does not compromise consumer protection. Over the years, provinces have committed to making the changes needed to allow for incorporation; in fact, in August 2014, the Provincial-Territorial Council of Ministers of Securities Regulation reiterated their commitment to the incorporation project, stating their intention to release draft legislation in the near term. And in November 2014, Alberta (which, at the time of writing, is not a Participating Jurisdiction) followed through by introducing amendments to its *Securities Act* to accomplish this goal. However, due to the piecemeal nature of Canada's securities regulation, wholesale change has been slow to materialize.

The Cooperative System, through its harmonized PCMA, represents an opportunity to finally, definitively, resolve this issue - so it is critical that its drafting seizes the opportunity of this fresh start. We are pleased that the PCMA begins laying the groundwork to achieve advisor incorporation, as in Section 2, the PCMA defines an 'adviser' as:

> a person engaging in, or holding himself, herself or **itself** out as engaging in, the business of advising others with respect to investing in, purchasing or selling securities or trading derivatives.
>
> [emphasis added]

Further, 'person' is defined as:

> an individual, **company**, partnership, unincorporated association, unincorporated syndicate, unincorporated organization, trust, trustee, executor, administrator or other legal representative.
>
> [emphasis added]

In our view, these definitions make it clear that the Cooperative System will permit advisors to act through a corporation: the Participating Jurisdictions have been careful to draft the PCMA using gender-neutral terms (through the use of the pronoun *itself*, or by stating *the person* rather than *he or she*), which contemplates entities other than natural persons being included. This is a positive first step towards completing the incorporation project. To maintain this momentum, the Participating Jurisdictions must also ensure that the regulations that complement the Draft Legislation are drafted as carefully, with the recognition that the concept of an advisor can include an incorporated entity.

It is also key that a professional corporation need not be registered where the advisor who is running his or her business through that corporation is already registered. We suggest that PCMA Section 22 dealing with registration be modified so that it states:

> **Unless a person or company is exempt under this Act from the requirement to comply with this section,** [a] person must not act as a dealer, adviser or investment fund manager unless the person is registered in accordance with the regulations and in the category prescribed for the purposes of the activity.

This modified section should be complemented by a statement in the regulations that makes clear that professional corporations which are established to collect fees or commissions from registered dealers are exempt from registration so long as their principal is duly registered.

In the past, some provinces have expressed a concern that if the professional corporation is not registered, there is a consumer protection concern regarding liability of the corporation versus that of the individual registrant. We have proposed that legislation strip away the corporate veil, but only against liability for market conduct related to the advisor's registered activity in the sale and distribution of securities.

For example, the acts of the corporation could be deemed to be the acts of the registered advisor, or the advisor could be jointly and severally liable with the corporation, in regards to the advisor performing registered activities through the corporation. A recent example of such drafting can be seen in Section 76.03 of Alberta's proposed *Securities Amendment Act, 2014*, which makes clear that the liability of the registered advisor to his or her client is unaffected, notwithstanding the advisor acting through a professional corporation.

Additional assurances that the registered advisor would not seek shelter behind the corporate veil could be achieved through a requirement that the advisor, his or her corporation and the dealer enter into a suitable contract with prescribed terms that address that concern. Those contracts would include undertakings and waivers that preserve the *status quo* of individual accountability and, in effect, reduce the corporation to a conduit for expenses and compensation, as has been the case for other professions and business groups.

The establishment of the Cooperative System represents an ideal opportunity to resolve the advisor incorporation matter; it is clearly the intent of individual provinces to do so, and resolving it through the Cooperative System would represent another tangible improvement over the existing regulatory framework. The advisor incorporation issue represents an opportunity for the Participating Jurisdictions to demonstrate how the Cooperative System can move a long-delayed effort forward, definitely and decisively, unlike the existing fractured system.

(vi) Checks and balances in the Draft Legislation

The Draft Legislation gives the Authority, through the Chief Regulator and the Tribunal, an extraordinary amount of regulatory power that is unlike anything that has been granted in the past. While these tools may prove useful, we believe that additional checks and balances must be added

in throughout the Draft Legislation so these powers are not used inappropriately, but rather with restraint and only after careful consideration.

In Section 44, the CMSA grants the Chief Regulator authority to issue a notice of violation (of the statute or regulations) and cause it to be served on a person. The notice may specify penalties up to $1 million for individuals and $15 million for non-individuals, and can be delivered without a hearing, but rather solely on the Chief Regulator's own reasonable belief that the person has committed a violation. It is only after the notice is delivered that the impugned person can make representations – but these representations are made to the Chief Regulator, the very entity issuing the notice, and the Chief Regulator then decides on the balance of probabilities whether the person committed the violation.

We believe that principles of natural justice may be violated by this structure, in regards to the respondent's ability to be heard, and the right to be heard by a neutral adjudicator. Further, given the life-changing quantum of administrative monetary penalties that are at stake, the standard of proof should be greater than the civil standard.

Additionally, while we strongly support full disclosure of substantiated claims of wrongdoing, we believe that notices of hearings should not be published in the public domain. In the public's mind, notices of a hearing about a particular violation are often equivalent to a conclusion that the named person is actually culpable of that violation – even if the person is later cleared, the claims retracted and a retraction published by the regulator. The reputational damage done by the notice is irreparable and the notices remain forever searchable on the internet. The appropriate time to publish is following a fair hearing, if an adjudicator finds the claim to be substantiated.

We find Section 85 of the CMSA concerning, which states that "the Authority may make regulations for carrying out the purposes and provisions of this Act..." Effectively, this section grants the Authority the ability to create its own laws, usurping the role of the legislature. To maintain accountability, the regulations must be promulgated from elected officials, and the Authority should not be in charge of creating the very rules it can enforce.

The PCMA also grants the Tribunal overly-broad powers; in Section 90, the Tribunal is empowered to "compensate or make restitution to one or more persons" where it determines that there is a violation of capital markets law. The granting of restitution is a function that is best suited for the courts, where there are evidentiary and procedural protections for all parties involved, rather than by an administrative tribunal, where such procedures (or even rules of evidence) can be arbitrary.

We believe that before the Cooperative System can move forward, the Participating Jurisdictions must take an earnest look at the checks and balances contained in the Draft Legislation. The Authority will be a forceful new entity that will enjoy the delegated powers of the federal and provincial governments; it is critical that these powers are carefully considered and strong accountability to elected officials is maintained.

Conclusion

We appreciate the enormity of the task faced by the Participating Jurisdictions in the development of the Cooperative System; Canada has tried to establish a national securities regulatory authority for decades, through countless iterations, to no avail. The Cooperative System represents the best chance that has ever come forward. That said, there are serious challenges ahead.

The intention behind our comments is to support your efforts and contribute positively in suggesting ways in which the Draft Legislation can be improved. We believe that taking a principles-based approach and leveraging the expertise of industry participants, such as Advocis, would result in legislation that is more efficient, effective and has greater industry buy-in. We believe that given their central role to the consumer's interface with the securities sector, advisors should be properly represented on the Board.

We believe that the distribution of segregated funds should remain outside the spectre of securities regulation, as the existing insurance-based regulation works well and respects stakeholders in each of the various sectors. And we believe that the Draft Legislation should settle the advisor incorporation matter once and for all, as a tangible improvement of the Cooperative System over the existing system.

Most importantly, the Cooperative System should seize this unique opportunity to fundamentally reconsider the role and regulation of financial advisors. For far too long, advisors have been considered mere agents of dealer-firms, which vastly understates their importance as providers of holistic financial advice to millions of Canadians. The Cooperative System, as proposed, does not change the *status quo*. By integrating our solution, *Raising the Professional Bar*, into the Cooperative System, the Participating Jurisdictions would signal their commitment to raising professional standards in the industry and elevating the advisor-client relationship that is ultimately at the core of the entire securities sector.

Finally, with a new, central regulatory authority comes a concentration of power. We believe that the Participating Jurisdictions must take significant care to ensure that the proper checks and balances are included in the Draft Legislation, including ensuring that ultimate accountability to elected officials is reinforced.

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

Sincerely,

Greg Pollock, M.Ed., LL.M., C.Dir., CFP
President and CEO

David Juvet, CFP, CLU, CH.F.C., CHS, FLMI, AMTC
Chair, National Board of Directors

Enclosure: *Raising the Professional Bar:*
Greater Consumer Protection Through Higher Professional Standards

Raising The Professional Bar

Greater Consumer Protection Through Higher Professional Standards.

A New Way Forward

Advocis®
The Financial Advisors Association of Canada

A Message from Ed Skwarek, Advocis Vice-President, Regulatory and Public Affairs

Dear colleague,

Financial advisors play a central role in helping millions of Canadians realize their goals and aspirations. Families and businesses across Canada rely on advisors to provide advice on and access to suitable financial products and services. Obviously, Canadians should be able to place their confidence in their advisors, trusting that he or she meets rigorous standards of professionalism, proficiency and accountability. Unfortunately, this is not always the case.

Let's justify Canadians' confidence in advisors
In a country which has professionalized everything from accountants to veterinarians, it is surprising that anyone can hold themselves out as a financial advisor, regardless of training, licensing or financial acumen. What's more, important consumer safeguards on those who sell financial products such as mandatory continuing education and minimum levels of errors and omissions insurance vary widely by both province and industry sector. All too often, our current patchwork of laws and regulations leaves consumers exposed to unnecessary risks, such as incompetence and even outright fraud.

Let's raise the professional bar for all financial advisors
Advocis has a straightforward, cost-effective and efficient solution to this patchwork problem: a requirement that anyone who holds himself out to the public as a financial advisor be required to maintain membership in a recognized professional association of financial advisors. The provincial government would accredit only those advisor associations which meet our proposal's strict professional criteria. Advisors would be free to choose which association they wish to join; and consumers could pick their advisor based on the reputation of the advisor, his employer, and his association.

This professional association model will significantly enhance consumer protection. Consumers will be able to easily verify their advisor's credentials and disciplinary history across industry sectors. Advisors will have to comply with rigorous proficiency requirements and obey professional and ethical standards of conduct. An effective complaints and disciplinary process will deal with "rogue" advisors. And regulators and distributors will realize a variety of efficiencies through ongoing improvements in the competencies of all advisors.

Let's complement existing regulation, not duplicate it
The existing regulatory framework primarily focuses on insurance and securities products. Rather than introduce yet another layer of regulation, Advocis' proposal simply closes off current regulatory gaps. The result will be a regulatory regime which will provide effective review of the comprehensive approach to financial advice that most Canadians receive.

Given the tremendous gains our model promises to deliver to regulators, product producers and distributors, advisors and, most critically, Canadian consumers, *now* is the time to raise the professional bar.

Yours truly,

Ed Skwarek, BA, LL.B., LL.M.
Vice President, Regulatory and Public Affairs
Advocis, The Financial Advisors Association of Canada
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I. Addressing The Need For Enhanced Advisor Professionalism

Problems with the Current Regulatory Framework

Financial advisors play a critically important role for millions of Canadians. Through the provision of financial planning and investment advice, retirement and estate planning, disability coverage, long-term care and critical illness insurance, advisors help the public prepare for life's events and secure their financial futures. This is ever more important in an economic climate where governments, facing their own fiscal challenges, are expecting Canadians to be increasingly self-reliant.

Given their critical role, Canadians should be able to trust that financial advisors are proficient, up-to-date in their knowledge and in compliance with the highest standards of conduct and ethics. While this aptly describes the majority of advisors, there are inevitably some who do not meet these standards, and due to gaps in the current regulatory framework, consumers are exposed.

Problem #1: Anyone can call themselves a financial advisor, which means consumers face significant – and unnecessary – risk exposure.

Anyone, regardless of their training, experience or education, can hold themselves out to the public as a financial advisor – which means that anyone can provide the public with what is purported to be "financial advice", even with little or no financial acumen. This regulatory gap is exploited by fraudsters such as Earl Jones, who represented himself as a financial advisor despite not being registered with securities authorities. This is an extreme example, but it highlights the significant harm consumers could suffer when they place their trust in a title that they believe is regulated, but which does not actually guarantee any expertise.

Problem #2: Existing regulation is focused on the sales of products, not the ongoing relationship of trust between financial advisors and their clients.

Financial advisors help clients develop comprehensive financial plans and provide advice on investments that can help achieve those plans. This is often a multi-year relationship built on the client's trust in the advisor's expertise. Advocis believes that all professionals in such positions of trust should subscribe to a code of conduct and ethics that establishes an overriding duty to their clients. They should also maintain errors and omissions insurance to protect clients in the event that the advisor fails to live up to that code.

But rather than focusing on this important relationship, existing regulation is based on the sales and distribution of financial products, and is further fragmented based on the type of product, whether it be life insurance, mutual funds or other securities. There is no industry-wide requirement that advisors subscribe to codes of conduct or maintain responsible levels of errors and omissions insurance. The result of this is that, depending on the type of product purchased, consumers could be receiving substandard levels of protection. Advocis believes that consumers should enjoy high

degrees of protection governing their entire advisory relationship, and this should not vary with the type of financial product that is needed to fulfill the consumer's financial plan.

Problem #3: There is no firm and clear requirement for advisors to keep their knowledge current.

Before obtaining their license to sell life insurance, mutual funds or other securities, financial advisors must demonstrate their initial proficiency in the product. Life insurance advisors are required to meet provincial licensing standards and to pass the Life License Qualification Program. The Mutual Fund Dealers Association of Canada (MFDA) designates as Approved Persons those individuals who meet the MFDA's registration standards and pass a designated mutual funds licensing exam. The Investment Industry Regulatory Organization of Canada (IIROC) designates as Registered Representatives those individuals who meet IIROC's registration standards and pass the Canadian Securities Course.

While these measures ensure the advisor's understanding of the product at the time of licensing, the industry is constantly evolving and static knowledge quickly becomes obsolete. But under the current framework, regulators' requirements for continuing education (CE) vary by product sector and even by province. In the life insurance sector, some provinces require advisors to complete several CE credit hours each year, some permit holders of educational designations to satisfy reduced requirements, and other provinces have no CE requirements whatsoever. For mutual funds, MFDA Rules speak only vaguely to CE, stating that it "should be provided". IIROC takes a clear stance and requires that advisors complete CE on both compliance and professional development matters.

Advocis believes that, regardless of product sector or province, advisors should be required to complete CE to maintain their license in good standing. Current regulations could allow advisors to become seriously deficient in their knowledge, posing a risk to consumers.

Problem #4: There is no effective, industry-wide disciplinary process.

Individual insurance or securities regulators are empowered to impose a variety of sanctions on advisors found guilty of misconduct, including stripping those advisors of their license or registration. However, a regulator's enforcement powers are limited to its respective sector – which does not reflect the business reality that the majority of advisors operate across sectors, and in assembling a client's financial plan, the advisor will likely recommend a combination of products that span those sectors.

This sectoral approach leaves consumers exposed. The types of serious misconduct that warrants an advisor's outright expulsion from one sector, such as fraud or gross negligence, speak to that advisor's conduct and ethics and are not sector-specific concerns. But currently, if an advisor is expelled from the mutual fund sector, for

example, that advisor can continue to sell segregated funds in the insurance sector. Advocis believes this type of "sector hopping" must be eliminated.

Also currently lacking is an easy mechanism for the public to verify their advisor's registration credentials. Regulators maintain their own individual websites where the public can verify their advisor's registration, but the information is valid just for that sector. Generally, the public does not understand the product-centred approach to regulation and the need to verify their advisor's status with each individual regulator. In the example above, if the advisor's client had only reviewed the advisor's standing with the provincial insurance regulator, the client would not have become aware of the serious sanction in the mutual funds sector.

The Solution: Require that Financial Advisors belong to an Accredited Professional Association

Fortunately, the solution to the problems identified above is simple, straightforward, and does not require significant government action or resources: anyone using the professional title of "financial advisor" should be required to maintain ongoing membership in an accredited professional association.

To be accredited, the professional association would be required to have the following characteristics:

- a code of conduct and ethics requiring, inter alia, the prioritization of the client's best interests;
- a requirement that members maintain errors and omissions insurance;
- elevated minimum initial proficiency standards, including addressing the proficiency standards of fee-only planners who do not sell financial products;
- continuing education requirements that address both substantive and professionalism matters;
- a best practices manual or practice handbook and information resources for members;
- a governance structure that includes representation from both financial advisors and the public;
- a complaints and disciplinary process that empowers the association to suspend or cancel the advisor's membership; and
- a public-facing database whereby clients can conduct a "one-stop" check of their advisor's credentials and disciplinary history.

Today, many financial advisors voluntarily choose to belong to professional associations such as Advocis that feature many of the characteristics listed above. These associations help advisors maintain high professional standards in serving their clients. This proposal seeks to codify that commitment to professionalism to encompass all advisors, and builds on the current sales-focused regulatory framework.

In essence, the proposed solution emphasizes proficiency, ethical standards, and accountability in the client–advisor relationship.

Membership in a professional association would mean that sellers of financial products and services put the interests of consumers first and provide them with proficient professional service. In particular, consumers would benefit through:

- the ability to review the credentials and disciplinary history across product sectors of a prospective financial advisor in an easily-accessible format;
- greater assurance that the financial advisor they select will meet a consistently high level of professionalism and accountability;
- greater protection from unqualified and unethical financial advisors, due to both higher licensing standards and the presence of errors and omissions insurance; and
- a responsive and robust complaints and disciplinary process that can remove unscrupulous actors from the industry and prevent further harm.

Regulating usage of "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, and in Alberta, the Alberta Boilers Safety Association, and the Petroleum Tank Management Association of Alberta is restricted to registrants of these associations.

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 Canadians' future financial needs onto individuals, now is the time to regulate the use of the professional title of "financial advisor."

II. Understanding The Professional Membership Association

This paper now turns to a more detailed look at the characteristics of proposed professional associations. (For an overview of the current regulatory framework, its shortcomings, and the virtues of the proposed professional association model, please see Appendix A, attached hereto.)

a. Who will belong?

Subject to several narrow and easily identifiable exceptions listed below, everyone who sells financial products to consumers, and everyone who offers financial advice and planning to the public, should be required to maintain membership in a recognized professional association. 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.

b. Who will be excluded?

It is important to note that the professional association requirement will not capture 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 (CAs, CGAs, and CMAs) 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.

c. Membership in a professional association as a condition of continued licensing

Individuals who hold themselves out as financial advisors would be required to belong to a professional association. Proof of membership would be a condition of the individual's registration or licensing (including license renewals) in the securities or insurance sectors. If an individual ceases to be a member of a professional association, his or her licensing or registration would also contemporaneously be in abeyance.

d. Regulators will designate associations

The relevant regulator would publicly designate as an approved professional association any membership association which it recognizes as fulfilling the necessary criteria (as described in Section 1 of this document). This would require regulators to draft the conditions of recognition necessary for accreditation as an approved professional association, to identify existing organizations as plausible candidates for recognition, and to invite candidate organizations to apply for recognition.

To be successful in their application for accreditation, candidate associations would have to agree to the following conditions:

- a commitment to meet specific criteria, which could include guidelines for the management and governance of all aspects of the operation of the association;
- execution of a memorandum of understanding with the regulatory body whereby the candidate association agrees to meet the aforementioned criteria while maintaining its accreditation;
- a commitment to pay for periodic audits, commencing with an audit within 12 to 18 months following recognition; and
- an acknowledgment that the regulatory body may revoke recognition of the candidate association.

It is likely that more than one association would be recognized by the regulator at the outset of implementing the proposed professional association model. Recognized associations would register financial advisors as members while building the systems and infrastructure required to meet their commitments to the regulator. If a professional association was found to have failed to meet its obligations and is unable to correct such deficiencies within a reasonable period, its recognition could be terminated. At that point, the defunct organization's members would be required to transfer to another professional association, and be directed to meet the new association's registration requirements within a specified period of time.

e. Proficiency standards for all financial advisors

All recognized professional associations would publish their proficiency standards. All financial advisors would be required to file an annual Certificate of Professional Standing issued by their association, as a condition of ongoing licensing or registration in the industry. In addition, all financial advisors would be required to meet a proficiency standard that encompasses the knowledge and competencies that their recognized professional association considers to be appropriate.

Initial proficiency standards for membership would be premised on the assumption that everyone who is licensed or registered to sell financial products meets the initial requirements for membership in a recognized professional association. However, all members would be required to fulfill ongoing continuing education requirements, which would have a structured component.

Accordingly, all recognized professional associations would accept, for the purposes of admitting individuals to membership, certain approved evidence of initial proficiency. For individuals who are life agents or securities representatives, sufficient evidence would lie in the fact that they currently meet the respective licensing or registration requirements for life agents or securities representatives. In the case of the individual who is a fee-only financial planner and receives no compensation directly or indirectly from the sale of financial products, the evidence of initial proficiency would lie in the fact that he or she currently holds a recognized financial planning designation. However, associations could, upon application, designate an individual as proficient, based on relevant education and industry experience.

The following designations would be granted initial proficiency recognition, provided that the fee-only advisor is in good standing with one of the designation-granting bodies:

- 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 (R.F.P.), sponsored by the Institute of Advanced Financial Planners;
- Chartered Financial Consultant (CHFC), sponsored by Advocis, the Financial Advisors Association of Canada;
- Certified Health Insurance Specialist (CHS™), sponsored by Advocis, the Financial Advisors Association of Canada;
- Chartered Life Underwriter (CLU®), 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.

f. Continuing education requirements

All financial advisors would be subject to ongoing continuing education requirements. These would include course requirements established by professional associations in consultation with industry regulators and firms. Individuals would be given credit by their association for mandatory continuing education taken in compliance with the requirements of regulators, but could be subject to additional requirements set by their professional association of choice. For example, all financial advisors could be required by their association to take courses on professional ethics and their association's code of conduct within a specified time after becoming members.

The main features of the proposed membership model with regard to continuing education include:

- all financial advisors would be required to fulfill competency-based continuing education requirements established by their association;
- professional associations would complement the proficiency standards and continuing education requirements of regulators and coordinate their continuing education programs with the requirements of regulators;
- professional associations would be required to credit their members for all continuing education completed in compliance with the requirements of a securities or insurance regulator or licensing body;
- professional associations would develop systems that facilitate the tracking of continuing education course requirements and course completions, with such systems being readily accessible to members and regulators; and
- professional associations would require all members to take continuing education courses related to professional ethics and to the association's professional standards and code of conduct, within a prescribed period of time after an individual becomes a member of the association.

g. A code of professional conduct

All financial advisors would be required to subscribe to their professional association's code of professional conduct, and abide by their association'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;
- 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 association and regulators.

h. 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.

i. A public registry of financial advisors

Professional associations would 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 and registration/licensing status and professional conduct as a financial advisor.

j. A best practices manual and information resources for members

Professional associations would be required to compile and make available online a best practices manual/practice handbook. They would also be required to prepare and circulate information materials, such as online and e-mail bulletins concerning regulatory requirements and developments, and membership disciplinary proceedings.

III. Implementing The Professional Membership Requirement

For reasons of Canadian constitutional law, the proposal for financial advisors to belong to a professional association would need to be implemented at the provincial level. Securities and insurance regulators would require individuals who are licensed to sell financial products, or who otherwise hold themselves out to the public as financial advisors, to belong to an association. Fee-only financial planners who do not sell financial products and are outside the scope of securities and insurance legislation would still be required to be members of an association.

a. Models of self-governance: self-regulatory organization vs. delegated administrative authority

The professional association must be recognized as an official regulatory body of financial advisors by provincial governments. This recognition can be accomplished in two primary ways: (i) as a full-fledged self-regulatory organization; or (ii) as a delegated administrative authority.

(i) self-regulatory organization

The self-regulatory organization model is the traditional approach to professional self-regulation. Examples of organizations constituted under this model include the Law Society of Upper Canada, the College of Physicians and Surgeons of Ontario, the Mutual Fund Dealers Association of Canada and the Investment Industry Regulatory Organization of Canada.

Regulatory power is vested in these organizations through provincial legislation (such as the Law Society Act) or official recognition by a government agency (such as a CSA recognition order of the MFDA). Obtaining this recognition is relatively challenging; the vetting process is rigorous, the standards to be met are high and the process can take several years.

Once approved, though, this model grants the organization a relatively large degree of autonomy – the organization is empowered to make rules governing a wide array of matters (including newly emerging areas) without having to go back to the province for approval. They are not subject to continuous government oversight; they are largely trusted to govern their own affairs, with only occasional reporting to, and reviews by, the government. To maintain the public's confidence as being a true professional regulator, they generally do not engage in any public-facing advocacy efforts that promote the profession or the organization's members.

(ii) delegated administrative authority

The delegated administrative authority (DAA) model is a relatively new way of obtaining recognition as a professional regulator. 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 reduce the government's footprint: the association's employees

are not public servants and they are self-financing, largely through fees paid by the association'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.

While the process of obtaining DAA recognition is less cumbersome than obtaining recognition as a self-regulatory organization, the powers granted to the DAA are more limited in scope. The province retains overall accountability and control of relevant enabling legislation; it monitors and remains accountable for the overall performance of each authority. DAAs have certain reporting obligations to the government, such as annual reports and audited financial statements, and they can be subject to operational reviews.

b. What organizations are likely to qualify for accreditation as a professional association?

The answer will largely depend on the accreditation standards that are set by the regulator. Also relevant will be the estimate, on the part of potential applicant organizations for accreditation, of the potential benefits and costs of meeting the accreditation standards and of operating as a professional association.

The requirement as outlined is not premised on onerous accreditation standards. It should be assumed that the standards would not be so burdensome that they would not be satisfied by a number of existing organizations, including associations that currently provide professional resources to financial advisors.

c. Requiring membership in a professional association in the securities sector

Most Securities Acts across the country allow that province's securities commission to prescribe rules, including criteria that an applicant must satisfy prior to registration: see, for example, sections 143 (1) and (2) of the Securities Act (Ontario) or 223 and 224 of the Securities Act (Alberta). Using this discretion, securities commissions could make membership in an association one of these criteria. Alternatively, National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations could be amended to require membership in an association as a condition of registration.

d. Requiring membership in a professional association in the insurance sector

Most Insurance Acts across the country do not provide the province's Superintendent of Insurance with the explicit authority to prescribe licensing conditions. However, most of these acts do provide broad latitude for the Superintendent to set the standards for determining whether a candidate is "suitable" for licensing.

Using this broad latitude, the Superintendent could deem that membership in a professional association speaks to the candidate's suitability to obtain and maintain

an insurance license in the province. In provinces where the Superintendent is not granted this discretion regarding suitability, the province's Insurance Act could be amended to either give the Superintendent such discretion, or the membership requirement could directly be prescribed in the Insurance Act.

e. Governance, discipline, and enforcement

(i) promoting the public interest

It is essential that any approved professional association represents the interests of consumers and the broader public interest, as well as the interests of its member financial advisors. Approved professional associations should be not-for-profit entities dedicated to financial advisor professionalism in the public interest. It is essential that professional associations be entirely independent from financial institutions, as well as product manufacturers and distributors.

The governance arrangements of all recognized professional associations, which would be set out in their charters, would include provisions for effective public representation. In particular:

- every recognized professional association would have public directors on its governing body, and also on any board committee responsible for professional conduct, discipline, advocacy, and policy and regulatory affairs; and
- public directors would be appointed in accordance with a suitable process that is appropriately independent in nature and designed to recruit qualified individuals.

(ii) governance issues

Initial membership application. With regard to applying for membership in a professional association, financial advisors would be permitted to apply for membership in an association of their choice. This would be the case even if they are already affiliated with a professional association at the time when they are required to apply to a recognized association for the purpose of membership. For example, the fact that an advisor holds a financial planning designation and is affiliated with the professional association that issued the designation will not make him or her a member of that association for the purposes of the professional association proposal.

Membership suspension or termination. An individual whose membership in a professional association is suspended or terminated as a consequence of his or her association's disciplinary proceedings, or whose membership is suspended as a consequence of the suspension of his or her license or registration by a regulator, would not be able to be employed in the industry as a financial advisor until he or she is again a member in good standing.

An individual who has had his or her license or registration suspended, cancelled or made subject to ongoing conditions, or who has had his or her membership in an association

suspended, cancelled or made subject to ongoing conditions, would be required to disclose his or her current status when applying for membership with a recognized association.

Show cause. An association would be entitled to require an individual who has had his or her license or registration suspended, cancelled or made subject to ongoing conditions, or who has had his or her membership in any association suspended, cancelled or made subject to ongoing conditions, to show cause why he or she is fit to be accepted as a member or to continue as a member.

Sharing of membership information. Professional associations and 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, or that the member is the subject of disciplinary proceedings, an association would take appropriate steps. Similarly, regulators would initiate a review of the licensing or registration of an individual upon being informed that his or her association membership has been suspended, revoked 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.

It would be necessary to carefully consider how to design a system where licensing and registration and association membership are inter-dependent, so that suspension or termination of any one (licensing, registration, association membership) could result in suspension or termination of the other(s). Fairness and due process implications would need to be studied, and a process would need to be designed to ensure fair treatment for the individual.

(iii) the complaints and disciplinary process

No duplication. Professional associations would complement but not duplicate the enforcement and disciplinary functions of regulators. In particular:

- a professional association's complaints and disciplinary process would enforce the association's rules and standards;
- a professional association's complaints and disciplinary process would not replace or supplant the disciplinary process of securities and insurance regulators;
- a professional association would have considerable discretion with regard to the investigation of complaints and the initiation of professional discipline, in order to ensure that association resources are used effectively to protect the public and complement the efforts of regulators; and
- a professional association, in considering whether to investigate complaints or initiate a disciplinary proceeding, would seek to conserve association resources and avoid duplicating the complaints and disciplinary processes of regulators.

Priority to public protection. As well, a professional association, in its complaints and disciplinary processes, would give priority to protecting the public by:

- ensuring that individuals who violate industry requirements in any one sector are not permitted to continue to be employed in the industry without further review; and
- exercising its authority to suspend or revoke an individual's membership in the association in specified circumstances that, while outside the scope of the regulatory jurisdiction of industry regulators, demonstrably indicates a lack of professional integrity or unsuitability to offer financial services to the public (i.e., convictions for criminal and regulatory offences, which indicate a lack of professional or personal integrity).

Initiation of proceedings. A professional association 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.

Power to delegate. Investigations and the prosecution of disciplinary proceedings could be delegated by a professional association to a third party accountable to the association, which could establish its own hearing panel. Alternatively, two or more professional associations could jointly establish a tribunal to hear and determine matters for any associations willing to participate in a joint fashion. The members of such a tribunal would be drawn from the participating associations.

(iv) advisor competence and incapacity

A professional association 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.

(v) administrative sanctions

A professional association 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.

(vi) cooperation with all industry regulators

Professional associations would cooperate with financial industry regulators with regard to complaints and disciplinary matters. Individual members would be required to consent to the sharing of information with financial industry regulators in regard to complaints and disciplinary matters. In general, a professional association would not proceed with any complaints or disciplinary proceedings in the event other

proceedings, initiated by a regulator and based on the same impugned conduct or circumstances, are already underway. As well, professional associations would cooperate with financial industry regulators with regard to continuing education programs and, when possible, participate in their policy development processes. Finally, the relevant regulators would establish a process for accrediting professional associations and monitoring their compliance with standards.

IV. How Enhanced Professional Standards Will Benefit Consumers, Advisors and Other Stakeholders

a. Promoting the interests of clients and consumers

The proposed membership model would promote the consumer interest in a number of areas.

(i) a mandated code of professional conduct and ethics

As noted above, all financial advisors would be required to comply with the code of professional conduct of their association of choice. Such a document would explicitly codify the following:

- recognition of the priority of the client's interests over those of the advisor;
- duties respecting conflicts of interest, including disclosure to the client of all real and apparent conflicts;
- the duty to provide competent service, performed with honesty and integrity;
- the duty to respect client confidentiality; and
- an accessible enforcement mechanism for disciplining and punishing members for misconduct, including criminal convictions and regulatory infractions.

(ii) proficiency standards and continuing education – the cornerstone of professionalism

Professional associations would establish initial proficiency standards for financial advisors, and would administer continuing education requirements designed to ensure that all financial advisors maintain a high standard of proficiency.

Such associations would be required to actively administer their codes of conduct, so the public is assured that member advisors understand and fulfill the ethical obligations they owe to their clients. Moreover, all financial advisors would be required to file an annual "Certificate of Professional Standing" issued by their association. This would be a condition for maintaining a provincial license or registration to sell financial products – and to ensure that the high standards to provide ongoing financial advice are met.

Individuals who want to hold themselves out as competent practitioners in areas of professional specialization, such as financial planning, would be required to hold in good standing the necessary recognized designations.

Professional associations' 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.

(iii) best practices and member information resources

Professional associations would publish information resources for members, such as a best practices manual, and periodic bulletins updating members on important regulatory requirements and developments, further ensuring client protection.

(iv) professional accountability — integrated across sectors

Professional associations 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.

An association's disciplinary action would have consequences for a member's ability to sell financial products as a provincial licensee or registrant. If a member of the association is expelled, that individual would be prevented from selling financial products. As well, if any regulator revoked or imposed conditions on a member's ability to sell financial products, that member's association would take appropriate action to suspend, revoke or impose conditions on his or her membership. Such measures would further buttress the actions of the particular regulator by imposing conditions on selling products or providing advice.

As noted above, a regulatory requirement that advisors must be in good standing with a professional association would prevent unscrupulous individuals from simply moving to a different financial sector and seeking licensing or registration.

The resulting regulatory umbrella created by professional associations 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.

Membership associations would have considerable discretion with regard to the investigation of complaints and the initiation of professional discipline, in order to ensure that association resources are used effectively to protect the public and complement the efforts of regulators. Associations would publish disciplinary proceedings and would follow a process of natural justice regarding procedural rights (hearing, tribunal, appeal process, etc.).

(v) ease of public access to information on financial advisors

Professional associations would be required to make information about their members conveniently accessible in a single public database. This would enable the public to easily determine if an individual is a member of a professional association and review his or her credentials.

b. Benefits to other key actors in the securities and insurance sectors

The proposed membership model would work to promote the interests of financial advisors, governments and regulators, and product providers and distributors.

(i) financial advisors would benefit from:

- enhanced public trust, status and confidence in advisors as professionals,
- access to resources that complement and facilitate standards and compliance with regulatory requirements, and
- a raised professional bar, through improved education and standards and the ready removal – in a public and effective manner – of unethical colleagues who tarnish the industry as a whole.

(ii) government and regulators would benefit from:

- the delivery of enhanced consumer protection and the "reining in" of unethical advisors who move from sector to sector;
- additional protection of the wider public from unqualified or unaccountable financial advisors;
- additional professional support for the government policy objective of increased individual financial responsibility for future financial needs;
- a reduced regulatory burden created by the various professional associations proactively complementing the current regulatory requirements and enforcement; and
- the combined expertise of the various professional associations, all of whom will contribute to the development of policy and implementation of effective regulation.

(iii) product providers and distributors would benefit from:

- the reliable professionalism of financial advisors representing their firms and products;
- the prevention of unethical advisors moving from one company to the next; and
- the development of a stronger platform to support the recruitment of new advisors into the industry through enhanced professional standing.

The following table indicates the limitations and drawbacks of the status quo and the benefits to consumers, advisors, and other stakeholders.

Advantages of professional membership over the status quo

Issue	Insurance	MFDA	IIROC	Proposed professional association membership
Who is covered?	Insurance agents	Mutual fund salespersons	Securities salespersons	**Everyone** who holds out as a financial advisor
Public represented in governance?	**Yes**	**Yes**	**Yes**	**Yes**
Financial advisors are "at the table" when regulators make policy?	Only to a limited extent.	Dealer members of the MFDA are the main stakeholder consulted.	Dealer members of IIROC are the main stakeholder consulted.	**All associations** will advocate with regulators on behalf of member financial advisors and consumers
Standards focus on consumer interest or on distributor / dealer interest?	Insurance focus	Mutual fund dealer focus	Securities dealer and consumer focus	**Consumer / client relationship focus**
Establishes proficiency requirements for all financial advisors to meet?	Licensing requirements focus on insurance	Registration requirements focus on mutual funds	Registration requirements focus on securities	**Builds on standards of insurance, MFDA and IIROC with structured continuing education requirements**
Mandatory competency-based Continuing Education?	No mandatory client-focused content	No specific continuing education requirement	No mandatory client-focused content, but focus on product knowledge to ensure proper service to investing public	**Yes.** Mandatory courses on ethics, conflicts of interest, duty to client, leveraging, regulatory / compliance developments
Use of a Code of Professional Conduct outlining duties and obligations to clients and public?	No enforceable dedicated Code of Professional Conduct articulating duty to clients, as such, but Insurance Councils in Western Canada have codified conduct rules in their by-laws	No dedicated Code of Professional Conduct articulating duty to clients, as such	**Yes** through the importation of CSI's Conduct and Practice Handbook	**Yes**

Advantages of professional membership over the status quo (continued)

Issue	Insurance	MFDA	IIROC	Proposed professional association membership
Participation in a public registry that covers all financial advisors?	No	No	No (IIROC Advisor Report is limited to advisors with IIROC members)	**Yes**
Can curtail ability of unethical or unregulated individuals to hold themselves out to the public as financial advisors?	No. Only able to suspend or cancel insurance license.	No. Only able to suspend or cancel status as MFDA advisor.	No. Only able to suspend of cancel status as IIROC advisor.	**Yes.** Including remedies against individuals who do not belong to an association (the "Earl Jones" problem)
Ability to prevent employment as a financial advisor of individuals who do not meet standards?	No. Loss of insurance license does not prevent employment as MFDA or IIROC advisor	No. Loss of MFDA status does not prevent employment as IIROC or insurance advisor	No. Loss of IIROC status does not prevent employment as MFDA or insurance advisor	**Yes.** While an individual's professional association membership is suspended or cancelled, they are barred from acting as an insurance, MFDA or IIROC advisor.
Ability to deal with misconduct relevant to integrity and suitability that is not within the regulator or SROs scope?	No	No	No	**Yes**

About Advocis

Advocis, The Financial Advisors Association of Canada, is the oldest and largest voluntary professional membership association of financial advisors in Canada. Advocis is the home and the voice of Canada's financial advisors. Through its predecessor associations, Advocis proudly continues a century of uninterrupted history of serving Canadian financial advisors, their clients, and the nation.

With over 11,000 members organized in 40 chapters across Canada, Advocis serves the financial interests of millions of Canadians.

As a voluntary organization, Advocis is committed to professionalism among financial advisors. Advocis members are professional financial advisors who adhere to an established professional Code of Conduct, uphold standards of best practice, participate in ongoing continuing education programs, maintain appropriate levels of professional liability insurance, and put their clients' interests first.

Across Canada, no organization has members who spend more time working one-on-one on financial matters with individual Canadians than us. Advocis advisors are committed to educating clients about financial issues that are directly relevant to them, their families and their future.

Questions?

If you have questions or comments, please contact:

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