

OSC Investor Advisory Panel
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The Investor Advisory Panel (“IAP” or “Panel”) is an independent body formed by the Ontario Securities Commission in August 2010. It is charged with providing input on the Commission’s policy initiatives, including proposed rules and policies, the annual Statement of Priorities, concept papers and specific issues. Its mandate is to represent the views of investors and make recommendations to the Commission on matters affecting investors.

The Panel wishes to comment, although belatedly, on proposed amendments to Dealer Member Rule 43 and Dealer Member Rule 18.14. The amendments expand the conditions under which a Registered Representative (RR) or an Investment Representative (IR) can act as an Executor or Trustee (E/T) to administer the estate of a person who was not related to the RR/IR, provided the RR/IR who carries out the role of E/T does not also have control of the testator or settlor’s accounts with the Dealer Member (DM) in their capacity as an RR/IR.

The intended outcome of the proposed amendments, as the Panel understands it, is to balance the investor’s right to appoint the individual of their choice to manage their affairs while being protected from conflict of interest situations.

In the Panel’s analysis this proposal is seriously flawed and published commentary from others in the industry reflects a similar view.

For your consideration, we list our main concerns with the proposed amendments below.

Key concerns:

The nature of the relationship

The role of an Executor or Trustee (E/T) goes far beyond advising a client on investments: it is a fiduciary relationship governed by law pertaining to the administration of estates and trusts. In this role, the fiduciary relationship is paramount.

If under the proposed change, if an RR/IR were to accept the role of E/T, the existing client relationship is extended beyond the client as investor to the client as settlor or testator as well as to the client's beneficiaries. This fundamentally alters the nature of the relationship between the client and the IR/RR, which has not up to this point been of a fiduciary nature. If RR/IRs are permitted to act as an E/T on behalf of non-related investment clients, this change of relationship will need to be made explicit and transparent in the Rules.

The heightened duty of care will be a *personal* duty for the IR/RR. It is the Panel's understanding that the DM will not have increased responsibility and liability under trust/common law for any wrongdoing or errors in judgment of the E/T-RR/IR. This situation is anomalous under Ontario law for consumers. In the Panel's view, it is also unnecessarily risky.

The Panel is concerned that most clients and their beneficiaries will not understand that the responsibility and liability rests solely with the E/T, personally. How will this be effectively communicated and acknowledged? Will, for example, the E/T be prohibited from referencing the DM on letterhead or using their normal business title?

The proposed change requires the testator/settlor's assets to be moved to another RR/IR in order to manage conflicts of interest. However, at what point is the RR/IR-E/T required to address this key question with the client? What is in the client's best interest - to move the assets to the control of a different RR/IR, or to be advised to seek a different E/T?

Conflict of interest

The proposed change introduces a new and unmanageable conflict of interest situation that is contrary to public interest. The Panel notes the challenges IIROC currently faces in overseeing and managing existing conflicts of interest in the industry and questions whether investor protection would be enhanced by expanding the list.

Some argue that this change provides greater choice to consumers and therefore the risks associated with yet another conflict of interest are reasonable. We disagree. This change does not provide consumers/investors with greater choice amongst those who are recognized as *qualified* and *competent* to act as an E/T.

The RR/IR who takes on the role of E/T must act in the best interests of the estate, but the IR/RR who subsequently controls the accounts of the client does not have that duty at this time. While the E/T owes a fiduciary duty, including ensuring that the investments are made in the estate's best interests, this duty is not required of the RR/IR person managing the investments. The E/T-RR/IR has a fiduciary duty to the settlor/testator/estate and, at the same time, a duty of loyalty to the DM that is her/his employer. The DM will have almost nothing to do with the E/T relationship and no obligation to the client beyond the investing relationship.

How are such conflicts of interest to be managed? What safeguards would be in place to ensure the E/T is objective in overseeing the investment management of the trust or estate assets by the new RR/IR, and in advising the settlor, testator or beneficiaries?

For example, the E/T could decide that it is in the best interest of the estate to move the investment assets to another financial institution or that the appropriate investment strategy for the estate is one that is less profitable for the DM. The RR/IR who is overseeing the accounts earns less if the change is made; the DM's profits are less. This decision has a significant impact on the E/T's working relationships. How is it possible that the E/T will be and be seen to be fulfilling their fiduciary duty first and foremost?

The Panel argues that the risks resulting from the conflict are too pervasive to be mitigated by safeguards.

Related versus Non-related

The amendment to Rule 43, just recently implemented, allowed an RR/IR to act as an E/T for related persons as defined by the Income Tax Act or what a layperson would refer to as "family members". There is a huge difference between being allowed to act on behalf of family and providing services for members of the public at large. One interpretation of this could be that RR/IRs are being given license under securities law to act as E/T to members of the public without reference to necessary competencies, professionalism, or fiduciary duty. The Panel is concerned that the proposed change creates permission for unregulated activity that is contrary to the public interest.

Supervision and oversight

Under the proposed change, the DM will have notice of and acknowledge or approve the E/T role. Since the E/T-RR/IR is employed by the DM, clients and beneficiaries could easily and wrongly assume that the DM has some active role in oversight and monitoring the work carried out for the estate. The Panel is concerned that no amount of disclosure will correct misperceptions of this kind.

The proposed change is predicated upon the presumption that conflicts of interest can be tracked and monitored within a DM. However, that pertains only to the accounts of the testator or settlor that are held with the Dealer Member. What safeguards and oversight exist to prohibit the E/T from inappropriately transferring the assets elsewhere where they are managed in an "unregulated" environment?

The risk of a "halo" effect

If there is a good investment relationship, clients could assume an RR/IR has competencies that extend to matters of trusts and estates, where the RR/IR might have no expertise or experience - in other words, a halo effect may lead the client to ill-founded decisions. Competencies required to become a licensed representative under securities law have little bearing on the full scope of responsibilities and duties of an E/T as set out in law. The Panel views this as a particular concern for seniors and those who are vulnerable when preparing their wills (e.g. diagnosis of terminal cancer at the age of 50).

Challenges of disparate roles

Given the disparate nature of the roles (E/T versus RR/IR), is it reasonable to presume that the two can be carried out to the degree of excellence needed to serve all clients? As an E/T, for example, the RR/IR does not have systems and supports in place nor quality control oversight to ensure no mistakes are made. The E/T role creates an additional burden of time and could create a distraction from core investment responsibilities.

Leveling the playing field?

Several letters and articles published in recent years suggest that this proposed change has been motivated by a desire to remove a perceived advantage in cases where the DM is part of a bank group that also includes a trust company.

In the case of a trust company acting as a corporate E/T, there is government regulation and oversight of the E/T activities of the trust company and its trust officers. In terms of protection of the public interest, there can be no comparison between the proposed scenario and one where a client appoints a corporate trustee/executor while their investments are held with a DM. The securities law provides no protection to individuals other than in their role as investor.

If more and more clients were to appoint their RR/IR as their E/T at what point is the DM considered to be offering trust and estate services?

Reputational risk for the industry and its members

The proposed change creates unnecessary reputational risk for an entire industry and puts at risk investors' confidence in their relationships with advisors. The change intentionally permits IR/RRs to act as E/Ts for any client subject to them not having control over the client's investment accounts. Only one well-publicized failure of an E/T carrying out work under this clause would damage the reputation of many and create uncertainty about the industry's ability to both oversee the activities of its registrants and protect the interests of its investing clients from negligence and/or wrongdoing.

This proposed change can only be seen as self-serving.