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Robert Day
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Dear Mr. Day:

Re: OSC Notice 11-774 - Statement of Priorities Draft For Comment 2016 –2017

I write on my own behalf and on behalf of McBride Bond Christian LLP's Financial Loss Advisory Group. Our firm routinely represents investors who seek redress from retail financial services firms, both investments and insurance. We also represent advisors in regulatory matters and contract disputes.

The Ontario Securities Commission's ("OSC") Notice 11-774 – Statement of Priorities ("SOP") reports on the significant progress by the OSC during the last few years as well as proposing a full agenda for the coming financial year.

The OSC has earned high regard for its investigation, consideration, and adoption of steps toward a fair, honest and good faith, service level for financial participants when dealing with retail investors. Two examples of these successes are the recent introduction of a viable Whistle-Blowing Program and the empirical studies of Embedded Commissions. Both of these key investor protection initiatives were undertaken in the face of advisers and dealers opposition. Industry's denial of conflict of interest with respect to such Embedded Commissions and their lack of transparency is a major challenge to fair, honest and good faith dealings by industry with Ontario's investors.

OSC and Continued Investor Protection

As advocates for investors, we are encouraged by OSC's rebalancing of its two primary mandates of market efficacy and investor protection initiatives. Historically, investor advocates have had few voices and even less engagement with the OSC's staff, commissioners, vice-chairs and chairs and the OSC has favoured market efficacy over

investor protection. This is changing. The OSC's Investor Advisory Panel (IAP) and the Office of the Investor (OI) are now encouraged to share the investor's voice with the OSC. This, in itself, is a significant improvement.

We urge the OSC to continue to engage with the IAP and investors, and to support changes to the OI for continued progress towards the integration of investors' voices throughout the OSC's work. We urge that these best practices be shared with the fortress like entities of the Canadian Securities Administrators and the SROs (the MFDA and the IIROC) that still stonewall the voices of the investors.

SROs should be required in their mandates to have quasi-independent IAPs and OIs. At this time, the stonewalling is seen by investor advocates as getting worse; this suggests an embedded conflict of interest whereby both the MFDA and the IIROC unintentionally are biased towards industry. The OSC's lead and success are a beacon for investors in an otherwise barren landscape.

This continued engagement and sharing of the best practices are in keeping with the OSC's efforts to empower investors and their representatives, by enabling it to communicate both the observed failures and the challenges faced by Ontario's investors. We congratulate the OSC and its Staff for the progress during the fiscal year of 2015-2016 and for their thoughtful engagement of all interested parties in the development of the 2016-2017 Statement of Priorities.

We appreciate that industry's repeated claim to speak in the interest of Ontario's investors is now commonly recognized by the OSC to be analogous to the story of the emperor who has no clothes - while occasionally industry's comments may be in keeping with the interest of investors, more commonly these words are simply ways of packaging industry's own interests in a more politically correct way. We hope that this recognition will be shared with industry sided SROs, namely the MFDA and the IIROC.

We thank Chairperson Weston for his years of service. We also welcome the new chairperson, Maureen Jenson. Chair Jenson is well known to investor advocates and her appointment as chairperson is welcome news as we view this as the Government of Ontario's recognition of both her excellent work and the need for greater balance at the OSC and Canadian Securities Administrators (and their SROs the MFDA and the IIROC) of Ontario investors' rights and concerns.

The OSC's vision is much needed. Without diminishing the role of the many good people and business involved in the sale of investment products and strategies to Ontario investors, there is much to be done. Unfortunately, Ontario's investors are not currently being served by a culture of integrity or a culture of fair, honest and good faith compliance.

At this time, investor confidence is ebbing in their advisers, in the dealers who sponsor these advisers, and even in the SROs who are charged with keeping a watchful eye.

The major reason for this shift in perception is the dissemination of the many, many failures of these industry players.

The self-interest of industry players at the cost of Ontario's investors is better known now than it was in the opaque past. The public is better informed of the many breaches of standards, ethics, and blatant conflicts of interests of industry players and this despite the often lack of enforcement records held by SROs. This dissemination of facts is what is degrading Ontarian's faith in industry, not as may be suggested a change by industry in their practices.

Our comments are not intended to minimize the work done by some industry players; it is a recognition that the culture of the investment industry routinely favours its own interests and is therefore in conflict with the best interests of investors. Integrity and compliance fail when this conflict is denied and allowed to perpetuate.

Greater issues facing Ontario investors

The OSC, and through delegated powers, the SROs, are good at punishing those few who commit fraud, once they are caught. Unfortunately, these individuals are generally caught not due to robust compliance, but more often than not, due to tragic losses suffered by Ontario's investors. The OSC has a good record of enforcement with fraud and technical breaches; such as insider trading and market timing. Fraud and technical breaches only represent a small portion of the alleged wrongs to Ontario investors and should therefore not be the focus of the OSC's investor protections. It is how we deal with those who have been wronged by industry that distinguishes a fair investor protection system from a system that defends the interests of industry who profited from these wrongs.

At the stage of investor treatment, the system continues to fail Ontario victims in the majority of circumstances (i.e. not fraud and technical breaches). Most of the tragic harm to Ontario's investors is caused by:

- Negligence,
- Conflicts of interests,
- Dealer's failure to warn investors of potential (and often likely) harm.

Dealers responding to complaints directly to the dealer and then to their ombudspersons without upholding their duty to act honestly, fairly and in good faith. Most complaints are dealt with by blanket denials and litigation like tactics to dissuade investors. These are serious misdeeds by dealers and should attract punitive action by the OSC and, through the OSC's delegated authority, by SROs.

When Ontario's investors are harmed by the financial industry, it is the investor that bears the brunt of the wrongdoing and is often re-victimized by the SROs and industry. For example, the compensation of fraud victims is Byzantine and often filled with misleading representations by the fraudster's investment dealers and E & O insurers. Let alone systemic wrongdoings – rarely do investor's advocates find a single

wrongdoing by an industry participant, usually the wrongdoing is common through an adviser's book, the branch managers and the dealer's compliance department. Rarely are the branch managers and dealer's compliance department sanctioned for their failures and systemic tactics. The obligation to deal fairly, honestly and in good faith with Ontario investors must be enforced to have meaning.

The greater issues facing Ontario's investors is the harm done by non-fraudulent, conflicted, and negligent advice provided and the lack of fair, honest and good faith supervision/compliance/reporting to COMSET, SROs and the OSC Compliance and Registrant Regulation and by dealers. These issues are reflected in three of the five regulatory goals listed by the OSC in its SOP namely: 1) investor protection; 2) responsive regulation; and 3) effective compliance, supervision and enforcement.

The duty of industry to act fairly, honestly and in good faith is all but absent when dealing with industry participant's wrongdoing which should trigger the common law duty to warn those harmed and potentially harmed. To state the obvious, the wronged investor should be quickly notified of the potential wrong (by their dealers) and efficiently compensated for harm, if any, objectively suffered. The investor is instead met with a conspiracy of silence by regulators, dealers, and advisers.

In this regard, the dealer and E & O insurers' response to wrongdoings should include plain language notification to each potentially wronged investor and assistance in seeking review and, if appropriate, redress. This would require a major shift in market participants' behaviours towards the goal of integrity and fair, honest and good faith compliance.

Concrete steps to rehabilitate the compliance, enforcement, compensation triumvirate of investor protection are urgently required. We urge this rehabilitation be specifically recognized and address by the OSC in its SOP and in its actions.

Comments on the SOP

Our following comments are directly related to parts of the SOP and, in particular, the stated goal of delivering strong investor protection.

i. Advisor/client relationship. The OSC should continue to pursue a Best Interest Standard ("BIS"). The vast majority of advisers promise their clients that their advice and actions will be in keeping with the client's best interest.

It is our understanding that IIROC claims to require a BIS as asserted in Notice 16-0068. We would support such a position, if that is really what was stated by this notice. That being said, the notice is so poorly worded that even investor's advocates do not see a BIS being recognized by IIROC in this notice. If that was IIROC's intent, then the OSC in its oversight role should require clarification. Furthermore, dealers and lawyers for advisers deny that these notices have a legal significance in regulatory and civil

proceedings – if a BIS is intended, then it should be stated as a rule and enforced. To our knowledge IIROC has never alleged in allegations any breaches of a BIS.

Understandably dealers and their organizations (IFIC, IIAC, submissions by Dealer's law firms) are opposed to a BIS – it is not in Dealer's business interest to put their client's interest as top priority. Dealers often state that their primary duty is to their shareholders – that is incompatible with a BIS. A BIS would fundamentally change the culture of Dealers and their lawyers and, by extension, the culture of E & O providers. A BIS would cost industry as it would lead to more frequent and fuller compensation of victims of the investment industry for the wrongs done by the participants of that industry. This is not an issue of market efficacy, it is a matter of fundamental fairness.

However, it is a BIS that is promised by advisers to Ontario's investors. Studies show that investors believe they are receiving none conflicted advice in keeping with a BIS when communicating with their advisers. A BIS is the minimum reasonable standard given, as noted in the SOP, the complexity of financial issues and information with which retail investors are met. In all but a few exceptions, the investor lacks the training, experience and education to learn and keep current with the barrage of issues and information – <u>that is why advisers and dealers are compensated for advice and the "protections" of supervision and compliance</u>. Thus, it follows that the OSC should require a BIS whether or not other provinces are willing to take this basic step to foster a culture of integrity and of compliance.

ii. To this end, NI 31-103 needs updating and the explicit inclusion of adviser and dealer obligations to foster cultures of integrity and compliance need to be added. The investor's input in updating NI 31-103 will be crucial. Industry and regulators (and those formerly of either group) do not speak for the investor. Industry protects its shareholders at the expense of investors and Ontario's capital markets.

iii. While we support, the OSC considering the inclusion of commissions as a mode of fee payment, we are opposed to the continuation of the opaque and often misleading disclosures by advisers and dealers of present embedded commissions. Specifically, CRM2 fails to break down all costs to the investor and thus fails to sufficiently inform the investor of costs. Nothing is gained for Ontario's investors by hiding the industry's compensation. Transparency is crucial.

Advisor and dealer fees are a conflict of interest. The conflict will exist regardless of the adoption of either extreme, fee for service or commission models.

Plain language and meaningful disclosure (to the financial literacy level of the specific individual) is necessary to expose the conflict of interest between the investor and the industry. If advice is a value proposition, then the advisor and her dealer should compete honestly. If advice is not a value proposition, then industry should admit this. But the core of the problem is not the model, it is the lack of professionalism amongst advisers and the failure of dealers to act fairly, honestly and in good faith.

iv. There is little to be gained in the short term from investor education. The reach of such efforts is miniscule and the target is the majority of Ontarians. While information is useful to those who know to search in the right places (and the Investor's Office of the OSC is an excellent source), this is a drop in the ocean. Training of students in high school is a wonderful goal, but the results may be decades away. Investor education is a laudable goal for the future, but is of little value to today's investor.

v. Targeted research has become, in recent years, a valuable tool for the OSC. The recent compensation studies and blind-shopper study are excellent examples of how truth can be put to the bold assertions made by advocates. These studies armed the OSC to consider the interests of Ontario investors and laid bare the unreliable or conflicted nature of industries' submissions on these issues.

When confronted with the deep pocketed lobbying of industry and their law firms, empirical research provides the necessary insight to help the OSC balance the scales toward a culture of integrity and compliance.

A simple example is surveys showing that advisers predominately promise a best interest standard. In breach of this promise, when appearing in regulatory matters and civil claims, these same advisers and their dealers deny that clients should rely on such a promise.

It is time to bring the investor's belief and the adviser's promises in line. Regulation should mandate that all conflicts of interest must be resolved in the favour of the client.

vi. With respect to the OSC OI, the OSC has made great strides by re-invigorating this important initiative. While early in the OI's reboot under the capable lead of Tyler Fleming, its work a significant step forward.

The OIs proposals, and in particular the use of behavioural finance/nudging are opportunities that may bear fruit in the short terms while assisting the OSC's other branches to better understand the investor who they are mandated to protect. Roundtables and targeted research bring fresh understanding and perspectives to the OSC and are highly endorsed priorities.

Additional Comments

The compliance/enforcement lens used by the OSC lacks sufficient attention to investor's issues. An effective compliance regime starts with compliance and enforcement, but also requires notice to investors of potential harm and effective compensation. The compliance/enforcement teams routinely meets with the many representatives of industry's but is, in our opinion, disconnected from Ontario's investors.

The COMSET reporting required of dealers is not robust nor are failures to report harshly sanctioned. The wrongdoings uncovered in civil litigation are often not reported

by dealers to the OSC or to their SROs. Without full and timely reporting of all potential and actual wrongs, COMSET cannot work as an effective investor protection tool. That is why dealer failures to fully and timely report requires harsh sanctions. An audit of dealers for failure to report is necessary.

Trends in supervision and compliance breaches are rarely noted let alone acted upon. This is the Achilles heel of investor protection by the OSC and its SROs.

Systemic problems are rampant and undermine investor confidence, let alone the industries' efficacy. Investors routinely receive reduced (bargained) compensation, if any at all. This is a crisis that requires a new strategy. The SOP fails to recognize the extent of risk and harm to Ontario's investors. Action is urgently required.

Conclusion

The OSC's efforts in fiscal 2015-2016 were significant. The coming year holds great promise. The OSC's focus on rebalancing the regulatory scales towards fair, honest and good faith dealing by market participants requires redoubled effort. A lesser focus fraud and other technical breaches, and an important shift toward focusing on where most Ontario investors suffer harm is necessary. Stronger compliance, enforcement, and compensation for negligent harm caused to investors, and, in particular, vulnerable investors are what is very urgently needed.

Yours truly,

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