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BY EMAIL

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Dear Sirs/Mesdames:

Re: Guidance on Order Execution Only Services and Activities (the “Proposed Amendments”)

The Canadian Advocacy Council¹ for Canadian CFA Institute² Societies (the CAC) appreciates the opportunity to comment on the Proposed Amendments.

We are generally supportive of the Proposed Amendments and agree that an update to the current member regulation notice respecting OEO services is necessary at this time and that recommendations of any kind should not be permitted. We also agree with IIROC’s assessment that some of the tools being offered by OEO firms are in fact implicit or explicit recommendations which should not be offered by such firms.

With respect to hyperlinks and similar references to third party websites, there should be an explicit requirement for OEO firms to make it extremely clear that the link is not an endorsement and that the viewer is leaving the firm’s website. Users might be required, for example, to “check the box” to confirm they understand they are not receiving a recommendation and are choosing to visit another site.

While we agree that in some cases the use of an automatic rebalancing tool would not amount to a prohibited recommendation, it may be difficult, particularly in unforeseen circumstances such as a market disruption event, for any alerts pushed out to clients not to constitute a recommendation. For example, the setting of an alert for percentage/dollar amount of change in a security in a portfolio may itself consist of an implicit investment recommendation to change holdings outside of the client’s automatic instructions.

¹The CAC represents more than 15,000 Canadian members of the CFA Institute and its 12 Member Societies across Canada. The CAC membership includes portfolio managers, analysts and other investment professionals in Canada who review regulatory, legislative, and standard setting developments affecting investors, investment professionals, and the capital markets in Canada. See the CAC’s website at <http://www.cfainstitute.org/cac>. Our Code of Ethics and Standards of Professional Conduct can be found at <http://www.cfainstitute.org/ethics/codes/ethics/Pages/index.aspx>.

² CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion for ethical behavior in investment markets and a respected source of knowledge in the global financial community. The end goal: to create an environment where investors’ interests come first, markets function at their best, and economies grow. CFA Institute has more than 135,000 members in 151 countries and territories, including 128,000 CFA charterholders, and 145 member societies. For more information, visit www.cfainstitute.org.

We respectfully disagree that research reports that are made available on OEO websites to be “pulled” by clients should generally not be considered to be recommendations. Although investors may be increasingly familiar with these types of reports (along with the potential conflicts of interest that exist if the issuer is a related or connected issuer of the analyst firm), in our experience the purpose of most research reports is to drive an investment decision (buy, hold or sell).

Studies have shown retail investors suffer from excessive trading. One study has shown that of 66,465 households with accounts at large discount brokers during the period 1991-1996, those that traded the most earned an annual return of 11.4%, while the market returned 17.9%, and that the average household turned over 75% of its portfolio annually.³ As a result, the existence of any kind of implied recommendation to purchase or sell a security is problematic to the extent it motivates an investor to conduct a trade if it would contribute to excessive trading.

The impact of asset allocation on portfolio performance cannot be overstated. It is either the largest driver or an important driver of performance, although there has been debate over the years as to whether it is in fact the largest driver. Taken together, market return and asset allocation policy return in excess of market return dominate active portfolio management.⁴

If an OEO firm makes a model portfolio or similar tool that suggests what the breakdown of an account should be for clients, that OEO firm is providing investment advice. We think there should be potential exemptive relief granted to allow OEO firms the use of limited model portfolios (the proposed “Permitted Model Portfolios”). Of the attributes listed, it is of particular importance that the model portfolios be “pulled” and not “pushed” to clients, and that specific securities or issuers not be named.

As a general comment, investor education of the limits of trade execution without advice should be mandatory.

Concluding Remarks

We thank you for the opportunity to provide these comments. We would be happy to address any questions you may have or to meet with you to discuss these and related issues in greater detail. We appreciate the time you are taking to consider our points of view. Please feel free to contact us at chair@cfaadvocacy.ca on this or any other issue in future.

(Signed) *Michael Thom*

Michael Thom, CFA
Chair, Canadian Advocacy Council

³ B. Barber and T. Odean, “Trading is Hazardous to Your Wealth: The Common Stock Investment Performance of Individual Investors”, (2000) Vol LV No.2 The Journal of Finance at 773.

⁴ Xiong et. al., “The Equal Importance of Asset Allocation and Active Management”, (2010) Vol 66 No.2 Financial Analysts Journal at 28.