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IIROC NOTICE

Rules Notice
Guidance Note
Dealer Member Rules

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Guidance on compliance and supervisory issues when dealing with senior clients

The number of Canadians over the age of 65 is on the rise and the average life expectancy of Canadians continues to increase.[1] In light of this aging client base, Dealer Members and their employees, representatives and agents (collectively, **representatives**) should be aware of, and adequately prepared to deal with, the issues that flow from this demographic trend.

This Notice provides guidance on how best to deal with the specific challenges that can arise when dealing with clients who are retired or about to retire (**senior clients**). IIROC recognizes that senior clients are not a homogeneous group and that issues that affect some, may not be relevant to all senior clients. However, we believe it is helpful to identify certain compliance and supervisory considerations that may be uniquely associated or more common with providing investment services to senior clients.

This guidance draws on a number of existing IIROC resources, including rules and guidance, as well as

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1 See Statistics Canada, *Life expectancy at birth, by sex, by province* (May 31, 2012) and *Population Projections: Canada, the Provinces and the Territories* (September 17, 2014).

industry best practices that may be particularly relevant to Dealer Members in dealing with senior clients. In addition, there are a number of resources provided by other regulators, governmental agencies and not-for-profit organizations that may be useful to Dealer Members and their representatives, which can be accessed through a dedicated senior client section on IIROC's web site.[2] IIROC has also produced a series of investor bulletins that Dealer Members and their representatives may find useful in their interactions with investors, particularly senior clients.[3]

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[2] Please see *Resources for Seniors* on IIROC's website.

[3] Please see *Investor Bulletins* on IIROC's website.

1. Key issues to consider when dealing with senior clients

In March 2014, the Investment Industry Association of Canada (**IIAC**) published a report (the **IIAC Report**)[4] that detailed practitioner-focused best practices relating to a number of senior client issues, including:

(a) powers of attorney (**POAs**) related issues

(b) effective communication

(c) policies and procedures

(d) product due diligence

(e) "know-your-client" (**KYC**), suitability and supervisory obligations and practices

(f) use of senior designations

(g) complaint handling process

(h) training on issues more common to senior clients, such as potential diminished capacity.

While IIROC is generally supportive of the best practices set out in the IIAC Report, below we provide regulatory guidance on some of these issues.

1.1 Powers of attorney

Industry participants expressed validity and supporting documentation concerns relating to the use of POAs by senior clients. While every client and situation is different, we encourage Dealer Members to adopt specific policies and procedures concerning POAs for all clients, including senior clients. In particular, Dealer Members may wish to implement policies and procedures that require their representatives to, among other things:

(a) ask senior clients about the existence and validity of any POAs at the time of account opening and periodically thereafter

(b) obtain copies of any POAs and verify the documentation supporting each POA

(c) refer to the applicable KYC information whenever there is a change to an existing POA to identify any potential inconsistencies.

Moreover, Dealer Members should remain attentive to any red flags that arise during the creation or modification of a POA, such as an apparent lack of connection between the client and the person being granted the POA.

1.2 Effective communication

Effective communication with senior clients should be a priority for Dealer Members. To enhance such communication, Dealer Members may find the following suggested practices to be helpful:

(a) increasing the frequency of contact with senior clients to remain informed about their

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4 IIAC Guidance, *Canada's Investment Industry: Protecting Senior Investors – Compliance, Supervisory and other Practices When Serving Seniors* (Mar. 18, 2014).

financial needs, employment status, health and other life events

(b) emphasizing the importance of accurate, complete and current KYC documentation, supplemented by consistent documentation, such as investment policy statements and financial plans

(c) reminding representatives about the importance of effectively documenting all material discussions with clients through correspondence, emails, documented notes and similar means and sending follow-up letters to clients after conversations to document and reiterate what was discussed

(d) educating clients about the benefits of POAs and when appropriate, encouraging clients who are in good health to share details of their financial affairs with trusted family members, estate lawyers or other professionals to help ensure that, if the client's health deteriorates, their financial affairs will be properly handled. This includes disclosure, and a balanced discussion, of the risks and considerations when granting such authority

(e) encouraging representatives to talk to clients about having an emergency or "trusted contact person" on file with the firm, such as a trusted family member or other trusted individual[5]

(f) using plain language (i.e., avoiding financial jargon) and having larger font versions of documents

(g) considering the firm's statutory obligations to accommodate client accessibility for disabled clients under legislation such as the *Accessibility for Ontarians with Disabilities Act* (Ontario).[6]

1.3 Policies and procedures

We encourage Dealer Members to consider the other suggested practices set forth in the IIAC Report for developing and improving their policies and procedures:

- training and educating of representatives on issues more common to senior clients (e.g., how to identify diminished capacity and financial exploitation)
- as discussed below[7], establishing an internal process for escalating issues and taking next steps
- encouraging clients of all ages to prepare for the future
- appropriate advertising and marketing to senior clients
- obtaining KYC information at account opening that identifies planned important life changes such as retirement
- ensuring suitability of investments

[5] Please refer to section 2.1 of this Guidance for a discussion concerning the "trusted contact person".

[6] For example, see IIAC Report at 9-10.

[7] Please refer to section 2.2 – *Escalation of issues* of this Guidance.

- conducting senior-focused supervision and compliance reviews.

As always, a Dealer Member must ensure that its policies and procedures are relevant to its business model and the clients it serves. Further, we expect Dealer Members to make reasonable efforts to remain current with evolving industry standards regarding senior clients and to update their policies and procedures, as appropriate.

1.4 Product due diligence, know-your-product and KYC

Dealer Members should keep in mind certain existing core investor-protection requirements when dealing with senior client issues. IIROC rules[8] and related guidance set out a number of these requirements, including the following product due diligence, know-your-product and KYC requirements.

(a) Dealer Members must have formal policies and procedures appropriate to their business to perform appropriate product due diligence before allowing any product to be offered to clients, including senior clients (e.g., thoroughly vetting any new product from a regulatory, risk management and business perspective).[9]

(b) Dealer Members must ensure their representatives satisfy the "know-your-product" requirements (e.g., taking reasonable steps to understand the structure, features and risks of each security that is available from the Dealer Member for recommendation to clients).[10]

(c) Dealer Members and their representatives must satisfy the KYC obligations (i.e., act as a "gatekeeper" by verifying the identity and essential circumstances of each client) and use due diligence to ensure that every recommendation and every order for each client is suitable.

These requirements apply to all Dealer Members dealing with any type of client. However, the application of these requirements would differ based on the Dealer Member's particular business model and the clients it serves. For example, the amount of product due diligence that a Dealer Member conducts for a new product intended only for institutional clients may differ from the amount required for full-service, retail clients.

Dealer Members and their representatives should be cognizant of circumstances and concerns that are unique to, and common amongst, senior clients. Being mindful of these circumstances and concerns will inform how the core investor-protection requirements described above should be applied to senior clients.

1.5 Suitability

Dealer Members are reminded that "compliance with the suitability requirements is fundamental to compliance with general business conduct standards and is essential to good business practice".[11]

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[8] For example, see Dealer Member Rule 1300.

[9] See Rules Notice 09-0087 – *Best practices for product due diligence*.

[10] See Rules Notice 12-0109 – *Know your client and suitability guidance* (**Notice 12-0109**).

While all retail clients should be treated individually, each with their own individual needs and circumstances, certain characteristics and issues are more frequently observed when dealing with senior clients.

1.5.1 Time horizon

One of the KYC information elements to be taken into consideration in assessing suitability is time horizon: the period of time within which the client wishes to reach his/her investment objective(s). While the presumption is that senior clients' time horizon is the duration of their retirement, senior clients may have differing time horizons for their accounts (e.g., where a senior client wishes to leave a legacy to a family member). Dealer Members should ensure that the rationale to support the time horizon used for each senior client account is appropriately documented.

1.5.2 Investment Objectives

Dealer Members and their representatives may encounter senior clients whose stated investment objectives are inconsistent. In such cases, the role of the Dealer Member is to identify the conflicts between the client's stated investment objectives and to assist the client in deciding which of the objectives is more important to the client, while informing the client of the risks associated with placing greater emphasis on achieving one or more of the stated objectives over others.

For example, senior clients often prioritize income generation and capital preservation over capital growth. This is because senior clients are more likely to rely on the income generated from, and proceeds realized on the sale of, their investments as a means to supplement or replace the cash flow generated during their working years. In some cases, the desire to generate investment income may result in senior clients becoming more vulnerable to assuming greater risks in the hopes of generating higher investment income. Dealer Members should remain vigilant to this risk.

To determine whether or not the investment objectives of income generation and capital preservation are both achievable, particularly in a low-interest-rate environment, the following KYC and client account investment information should be assessed:

- current financial situation
- investment time horizon
- current account investment portfolio composition
- current account investment portfolio risk, which should be consistent with the client's stated risk tolerance.

The Dealer Member's representative should communicate the results of this assessment to the client in a comprehensive and timely manner. When it is not reasonable to expect to achieve both objectives simultaneously, the Dealer Member should ensure that the client is made aware of this inconsistency and the reasons for it. In such circumstances, the Dealer Member should obtain clear instructions from the client as to which of the stated goals takes precedence.

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[11] See Notice 12-0109 at 1.

Since each client situation is unique, a lower-risk, capital-preservation-focused portfolio will not always be the most suitable for a senior client if the result is that the client cannot generate enough investment income to cover their living costs. Similarly, a higher-risk, income generation-focused portfolio will not always be the most suitable for a senior client, if the client is not comfortable with assuming the greater risk of suffering investment losses.

To ensure that a client makes a fully-informed and suitable investment decision that will enable him/her to achieve their highest-priority investment objectives, Dealer Members should:

- conduct a proper assessment of a senior client's unique KYC and account investment information
- communicate the assessment results to the client, and
- properly identify any alternatives available to the client.

1.5.3 Supervision

We expect Dealer Members to have effective and robust supervisory review processes in place that ensure investments made by senior clients are suitable. In this regard, Dealer Members may wish to conduct regular focus testing on senior client accounts.

Under the enhanced suitability assessment requirements adopted in connection with IIROC's Client Relationship Model initiative (**CRM**), Dealer Members must now consider an expanded set of KYC information, along with certain account investment information, in assessing whether the portfolio of investments held in the client's accounts is suitable. Suitability assessments must now be performed more frequently, including when certain important account events other than a proposed trade occur. In addition, certain account investment information must now be considered; namely, the current investment portfolio composition and risk level of the client's accounts that are subject to the suitability assessment.

2. Responding to potential financial exploitation and diminished capacity situations

Senior clients often rely on others for investment advice or ask others to make investment decisions on their behalf. Unfortunately, this has the potential to leave senior clients vulnerable to financial exploitation (e.g., where another person misuses or takes the assets or funds of the senior client through deception, intimidation or undue influence). In addition, industry particpants have also expressed concerns regarding the challenges associated with identifying senior clients who may suffer from potential diminished capacity.

Dealer Members and their representatives play an important role in reducing the likelihood that their clients are financially exploited and identifying signs that their clients are suffering from diminished capacity. Dealer Members should implement, maintain and carry out policies and procedures that are designed to detect and address potential financial exploitation and diminished capacity situations. We recommend that these policies and procedures:

(a) encourage clients to provide the name and contact information of an emergency or "trusted contact person" to assist the Dealer Member when issues arise

(b) enable the dealer to place a temporary hold on the client's account (e.g., to allow for verification of information or instructions) in instances where financial exploitation or diminished capacity is suspected.

2.1 Trusted contact person

Where policies and procedures are implemented dealing with a "trusted contact person", Dealer Members should require this person to be an individual who is not involved in making financial decisions with respect to the account.

Further, Dealer Members' policies and procedures should address the circumstances when the "trusted contact person" should be contacted. For example, when: (a) a representative has financial exploitation concerns, or (b) a client proposes to give authority of their account to a third-party for reasons that are not obvious. It is important that a Dealer Member reasonably believes the "trusted contact person" has had no involvement in the suspected exploitation or the proposal to reduce the client's investment decision making role.

Finally, Dealer Members' policies and procedures on this topic should also address circumstances where concerns arise that the Dealer Member's representative is involved in the suspected financial exploitation, or it is proposed that the representative take on a materially greater role in making investment decisions for a particular client. In such cases, an independent person at the Dealer Member should contact the "trusted contact person".

2.2 Escalation of issues

Dealer Members should establish internal processes, appropriate to their business, for the escalation of difficult issues involving senior clients. Such processes would require, among other things, representatives to contact the appropriate supervisor, compliance officer or legal counsel within their firm to obtain guidance on how to resolve difficult questions involving financial exploitation and other issues, such as POAs and diminished capacity.

3. Rules and guidance particularly relevant to dealing with senior clients

IIROC has various rules and guidance that, while applicable to all types of investors, are particularly relevant to Dealer Members dealing with senior clients. Listed below are number of such guidance notices that Dealer Members should review in the context of dealing with seniors.

(a) Rules Notice 09-0087 - *Best practices for product due diligence*. This notice identifies a number of new product considerations that would be relevant to senior clients, when discussing the possibility of purchasing a new product for their investment portfolio.

(b) Rules Notice 09-0363 - *Client complaint handling rule and guidance note.* This notice describes in detail the obligations of Dealer Members to address client complaints, including the Dealer Member's duty to assist clients in submitting a complaint, which may be of critical importance to some senior clients.

(c) Rules Notice 12-0107 - *Client Relationship Model – Implementation* and Rules Notice 12-0108 - *Client Relationship Model – Guidance.* These notices address the introduction of relationship disclosure requirements, general conflicts of interest management requirements and an enhanced suitability assessment obligation. The new rules:

- ensure clients receive additional, plain language information about their account(s) with the Dealer Member
- require the Dealer Member to disclose to clients how the firm has resolved conflicts in a manner that is consistent with the best interests of clients, and
- require registered representatives to assess the suitability of their client's account portfolio of investments more frequently, while using a more sophisticated assessment approach.

(d) Rules Notice 12-0109 – *Know your client and suitability guidance*. This notice focuses on the Dealer Members' KYC and suitability obligations. The notice includes a number of considerations that would be relevant to senior clients when discussing changes to a client's investment portfolio to better align with the client's stated risk tolerance and investment objectives.

(e) Rules Notice 14-0073 - *Use of business titles and financial designations.* In this guidance note, we remind Dealer Members of the need to be transparent and consistent with regard to the use of designations that suggest an expertise in relation to senior investors.[12] As set out in the guidance note, "[p]articular scrutiny should be given to the use of business titles that convey an expertise in seniors' issues or retirement planning to ensure any individual using such a business title is appropriately qualified and competent in that area."[13]

(f) Rules Notices 14-0133, 15-0013 and 15-0128 - *CRM Phase 2 – Performance Reporting and Fee / Charge Disclosure* and the CRM - *Frequently Asked Questions* publications.[14] These notices address the introduction of enhanced fee/charge disclosure requirements and new account performance reporting requirements. The new rules, once fully implemented, will ensure clients receive additional information about the fees/charges

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[12] The guidance note states, in the relevant part: "No IIROC Approved Person should hold his or herself out to the public in any manner, including without limitation, by the use of a business title or designation of qualifications or professional experience that deceives or misleads, or could reasonably be expected to deceive or mislead, a client or any other person as to their proficiency or qualifications. […] To mitigate against public confusion and increase public understanding of an individual's registration status, business titles should be coupled with public disclosure and plain language explanation of the individual's IIROC approval category, corresponding proficiencies, and the fact that IIROC is the licensing body. Depending on the firm's business model, firms should consider centralizing the review and approval process relating to the use of business titles and financial designations in general, *particularly those used in relation to senior investors and retirement planning*, to ensure consistency." IIROC Rules Notice 14-0073 at 2-3 (*emphasis added*).

[13] IIROC Rules Notice 14-0073 at 3.

[14] The third publication of CRM - *Frequently Asked Questions* was published on December 16, 2015 in Rules Notice 15-0288 (**CRM FAQ**).

they incur and about the performance of their account.

The CRM FAQ discusses how, under the new account portfolio-focused approach to assessing suitability, it is possible that one or a few higher-risk individual positions may be held within a client's account investment portfolio, without raising the overall portfolio risk to unacceptable levels. Conversely, it is also possible that a portfolio where the risk of each individual position appears to be acceptable may be unsuitable for a client. These considerations may be relevant to assessing suitability on senior clients' accounts.

(g) Rules Notice 13-0163 - *Disclosure and approval of outside business activities.* This guidance note addresses matters relating to outside business activities and provides that "[a]ny outside business activity that places an Approved Person in a position of influence over a client or potential client must be disclosed, whether or not it is a paid position."[15] Firms should be mindful of how outside business activities may place an Approved Person in a position of influence over senior clients.

(h) The "Opening Your Retail Account" brochure addresses in detail the type of information that a Dealer Member is required to collect from a client when he or she opens an account and why the information must be collected. This may be of particular interest to senior clients.

4. Conclusion

IIROC recognizes that senior clients are not a homogeneous group. Financial circumstances, time horizon, risk tolerance and financial literacy may vary considerably from client to client. However, there are a number of considerations that are generally associated with providing investment services to senior clients. While this Notice identifies many of these considerations and provides guidance on how best to deal with certain specific challenges that can arise when dealing with senior clients, it is not intended to be exhaustive. Dealer Members should ensure that how they deal with senior clients, including the content and nature of their policies and procedures, is adequate and sufficient based on their particular business model and the individual characteristics of the senior clients they serve.

15 IIROC Rules Notice 13-0163 at 5 and 7.