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## **ADDRESSING THE NEEDS OF VULNERABLE INVESTORS: AUTONOMY AND PROPERTY RIGHTS**

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## I. EXECUTIVE SUMMARY

In Canada, demographic trends related to an aging population have brought into focus the challenges associated with providing financial services to clients who may be vulnerable to financial exploitation or incapable of making financial decisions.<sup>1</sup> For financial advisors and other registrants, there is a concern that financial exploitation and incapacity can impact a client's decision-making process and call into question whether a client has properly instructed the registrant to, for example, open an account or complete a transaction. More generally, financial exploitation and incapacity may impact upon a client's ability to make decisions that are in his or her best interests.

The regulatory response to these concerns has, by and large, focused on client protection. Securities regulators have noted that registered firms and individuals can be uniquely situated to observe signs of vulnerability, financial exploitation, and incapacity, as a result of their relationships to and interactions with clients.<sup>2</sup> However, regulators have also recognized that "vulnerability" is a complicated issue, and registrants are not qualified to make capacity determinations.<sup>3</sup> In an attempt to bridge this gap, regulators have issued guidance to registrants on how to identify signs of financial exploitation and incapacity and how registrants may respond to those concerns by contacting a trusted contact person or placing a temporary hold on a client transaction.

While protecting vulnerable clients is certainly an important policy objective, a balance must be struck between client protection, on the one hand, and respecting client autonomy and property rights, on the other. In order to achieve that balance, securities' regulators must emphasize the importance of client autonomy and property rights and should give serious consideration to providing registrants with a form of safe harbour defence or other statutory protections to rely on when servicing aging and vulnerable clients.

## II. VULNERABILITY, FINANCIAL EXPLOITATION AND MENTAL CAPACITY

The concept of client vulnerability is complex. Although often associated with elderly clients, securities regulators have recognized that vulnerability can affect clients of any age and can take many different forms. Several factors may cause or contribute to a client's vulnerability, including injury, illness, mental health issues, cognitive impairment, disability, and financial illiteracy. According to securities' regulators, client vulnerability concerns any limitation that puts a client at an increased risk of financial exploitation.<sup>4</sup>

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<sup>1</sup> Canadian Securities Administrators, [Notice of Amendments to National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations and to Companion Policy 31-103CP Registration Requirements, Exemptions and Ongoing Registrant Obligations to Enhance Protection of Older and Vulnerable Clients](#) (July 15, 2021) [the "CSA Notice of Amendments"] at p.2. Canadian Securities Administrators, [Staff Notice 31-354, Suggested Practices for Engaging with Older or Vulnerable Clients](#) (July 21, 2019) ["Staff Notice 31-354"], pp. 1 and 3; Canadian Foundation for Advancement of Investor Rights, [Report on Vulnerable Investors: Elder Abuse, Financial Exploitation, Undue Influence and Diminished Mental Capacity](#) (November 2017) ["FAIR Report"], pp. 15-18.

<sup>2</sup> CSA Notice of Amendments, *supra* at p. 2.

<sup>3</sup> "We do not expect registered firms and their representatives to be the final arbiter in matters of vulnerability, financial exploitation or mental capacity, but rather, believe that they may want to place temporary holds in these circumstances so that they can take steps to protect their clients." Ontario Securities Commission, [Companion Policy 31-103 CP, Registration Requirements, Exemptions and Ongoing Registration Obligations](#) ["CP 31-103"] at p. 29.

<sup>4</sup> *Ibid* at p. 152.

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The related concept of financial exploitation is premised on the fear that a family member, friend, caregiver, or other third-party may exercise undue influence over a vulnerable client and thereby subvert the client's decision-making process in favour of the third-party's interests. There are a myriad of relationships and family dynamics that may give rise to what may be perceived as undue influence. In some cases, a client may demonstrate overt signs of undue influence while, in other cases, undue influence may develop subtlety and slowly over time.<sup>5</sup>

In some cases, a client's vulnerability can be linked to broader concerns regarding mental capacity. Although not all vulnerable clients lack mental capacity, a client who lacks mental capacity may also be considered vulnerable. As with the concept of vulnerability, the causes and outward signs of mental incapacity are multifaceted. While some forms of cognitive impairment are progressive in nature, with the signs evolving over time,<sup>6</sup> other forms of impairment may fluctuate in severity or be of limited duration.<sup>7</sup> Ultimately, a client's capacity to make financial decisions will depend on the decision at issue, the time, and the context in which the decision is made.<sup>8</sup>

### III. DEMOGRAPHIC TRENDS

Although vulnerability and capacity concerns can impact clients of any age, demographic trends related to aging nonetheless suggest that registrants may face an increasing number of clients who demonstrate signs of vulnerability or incapacity in the coming years. Since 2000, the number of Canadians aged 65 and over has more than doubled from approximately 3.8 million to 7.8 million.<sup>9</sup> There are currently over 900,000 Canadians aged 85 and older<sup>10</sup> and, according to Statistics Canada, that number could reach more than 2.7 million by the year 2050.<sup>11</sup> Similar trends have been observed internationally.<sup>12</sup>

As Canada's population ages, it is expected the number of Canadians who suffer from dementia and other forms of cognitive impairments will increase. For example, as of January 1, 2024, there were an estimated 733,040 people in Canada living with dementia and that number is expected to increase in the coming years.<sup>13</sup> By 2030, the number of Canadians with dementia is estimated to increase to nearly 1 million and by 2050, an estimated 1.7 million people in Canada could have dementia.<sup>14</sup> These statistics further reinforce the expectation that registrants will be exposed to an increased number of clients who may be considered vulnerable.

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<sup>5</sup> FAIR Report, *supra* at pp. 22-23.

<sup>5</sup> CP 31-103, *supra* at pp.151-152.

<sup>6</sup> *Ibid* at p. 152.

<sup>7</sup> FAIR Report, *supra* at pp. 15-16. Staff Notice 31-354, *supra*, p. 3.

<sup>8</sup> *Palahnuk v Palahnuk Estate*, [2006 CanLII 44262](#) (ON SC) at para 67 and 75.

<sup>9</sup> Statistics Canada, [Population Estimates by Age and Gender](#) (last viewed September 25, 2024).

<sup>10</sup> *Ibid*.

<sup>11</sup> Statistics Canada, [A portrait of Canada's growing population aged 85 and older from the 2021 Census](#) (Release date: April 27, 2022).

<sup>12</sup> Organization for Economic Cooperation and Development, [Financial Consumer Protection and Aging Populations](#) (2020); International Organization of Securities Commissions, [Senior Investor Vulnerability](#) (March 2018), pp. 13-15.

<sup>13</sup> Alzheimer Society of Canada, [Dementia Numbers in Canada](#) (last viewed November 6, 2024).

<sup>14</sup> *Ibid*.



#### IV. THE REGULATORY RESPONSE

In Canada, the regulatory response to the challenges associated with providing financial services to vulnerable clients has focused primarily on client protection by providing registrants with tools to identify and respond to warning signs of financial exploitation and incapacity. For example, on May 31, 2016, IIROC released Guidance Note 16-0114, *Guidance on Compliance and Supervisory Issues when Dealing with Senior Clients* to provide registrants with guidance on, among other topics, responding to the potential financial exploitation of elderly clients.<sup>15</sup> Similarly, on June 21, 2019, the Canadian Securities Administrators (“CSA”) released Staff Notice 31-354, *Suggested Practices for Engaging with Older or Vulnerable Clients*, which included, among other things, a list of “red flags” or client exploitation and incapacity.<sup>16</sup>

Similar guidance has been provided by provincial securities regulators. For example, on March 20, 2018, the OSC released Staff Notice 11-779, which detailed the OSC’s action plan to respond to the needs of senior investors in Ontario.<sup>17</sup> The OSC’s action plan emphasized, among other things, the importance of enabling registrants to respond to situations where they suspect that financial exploitation or cognitive impairment may be affecting a client’s judgment.<sup>18</sup>

On July 15, 2021, the CSA expanded on the concept of client “vulnerability” through a series of amendments to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* and Companion Policy 31-103CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations*.<sup>19</sup> Those amendments built on earlier OSC and IIROC guidance notes with the goal of protecting vulnerable investors by introducing the concept of a “trusted contact person” into the client identification process, and clarifying the circumstances in which a registrant may place a temporary hold on a client transaction in response to concerns of financial exploitation or incapacity.<sup>20</sup>

##### a) Guiding Definitions

NI 31-103 defines “vulnerable client” as a client “who might have an illness, impairment, disability or aging-process limitation that places the client at risk of financial exploitation”.<sup>21</sup> This is a broad definition which, in contrast to comparable definitions in other jurisdictions, is not restricted to elderly clients and clients that lack mental capacity.<sup>22</sup> As a result, registrants are faced with the difficult task of being attuned to a wide array of client characteristics and circumstances which may

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<sup>15</sup> Canadian Investment Regulatory Organization, [Guidance on compliance and supervision issuers when dealing with senior clients](#) (May 31, 2016).

<sup>16</sup> Staff Notice 31-354, *supra* at pp. 3-4.

<sup>17</sup> Ontario Securities Commission, [Staff Notice 11-779, Seniors Strategy](#) (March 20, 2018) [“**Staff Notice 11-779**”].

<sup>18</sup> *Ibid.* See also: Ontario Securities Commission, [Staff Notice 11-790, Protecting Aging Investors through Behavioural Insights](#) (November 9, 2020).

<sup>19</sup> Amendments made effective on December 23, 2021. CSA Notice of Amendments, *supra*.

<sup>20</sup> *Ibid.*

<sup>21</sup> National Instrument 31-103, [Registration Requirements, Exemptions and Ongoing Registrant Obligations](#) [“**NI 31-103**”] at s. 1.1. See also: Canadian Investment Regulatory Organization, [Investment Deals and Partially Consolidated Rules](#) (September 28, 2024) [“**Dealer Rules**”], rule 3201(3).

<sup>22</sup> See: FINRA Rule 2165(a)(1), which defines “Specified Adult” as: (a) a natural person aged 65 and older; or (b) a natural person aged 18 and older who the member reasonably believes has a mental or physical impairment that renders the individual unable to protect his or her own interests.

or may not contribute to client vulnerability.

Similarly, NI 31-103 broadly defines “financial exploitation” to include “the use or control of, or deprivation of the use or control of, a financial asset of an individual by a person or company through undue influence, unlawful conduct or another wrongful act”.<sup>23</sup> Again, this is a broad definition, which recognizes that financial exploitation can be perpetrated against a client by any person and through different means. Based on this definition, financial exploitation can emerge from a spectrum of circumstances and relationships including family and other personal relationships. While there may be instances in which the financial exploitation of a client is observable to a registrant, there are likely to be cases in which the signs of financial exploitation remain latent.

Although NI 31-103 does not include a definition for mental “capacity”, the temporary hold provisions of NI 31-103 refer to incapacity as a lack of “mental capacity to make decisions involving financial matters”. This loose definition is consistent with the legal framework for mental capacity in Canada, which recognizes that capacity is decision specific. With reference to the Ontario *Health Care Consent Act*, the Supreme Court of Canada has held that incapacity refers to a lack of “ability to understand the information that is relevant to making a decision [...] and to appreciate the reasonably foreseeable consequences of that decision or lack of decision.”<sup>24</sup> Similar statutory and common law standards have been adopted for assessing capacity in the context of managing property<sup>25</sup>, making personal care decisions<sup>26</sup> and entering into contracts<sup>27</sup>. As a consequence, the issue of whether a client lacks mental capacity is highly dependent on the nature and complexity of the financial decision and that client’s capacity at the time that the decision is made.

In order to assist registrants with these complex issues, CP 31-103 includes a non-exhaustive and non-determinative list of warning signs of financial exploitation, vulnerability, and mental incapacity.<sup>28</sup> The OSC has also published resources to assist registrants in developing best practice for working with vulnerable investors including resources on identifying and responding to signs of financial exploitation.<sup>29</sup> However, the CSA has also acknowledged that the potential “warning signs” of diminished mental capacity and financial exploitation can be subjective in nature and no single warning sign is determinative.<sup>30</sup> Similarly, the Supreme Court of Canada has noted that capacity is an abstract concept and, although the primary means of assessing capacity is to observe what an

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<sup>23</sup> NI 31-103, *supra* at s. 1.1.

<sup>24</sup> *Starson v Swayze*, [2003 SCC 32](#) [“*Starson*”] at para 8, citing *Health Care Consent Act*, 1996, S.O. 1996, c. 2 Sched. A.

<sup>25</sup> “A person is incapable of managing property if the person is not able to understand information that is relevant to making a decision in the management of his or her property, or is not able to appreciate the reasonably foreseeable consequences of a decision or lack of decision”. *Substitute Decisions Act*, [1992, S.O. 1992, c. 30](#) [“*SDA*”] s. 6.

<sup>26</sup> “A person is incapable of managing property if the person is not able to understand information that is relevant to making a decision concerning his or her own health care, nutrition, shelter, clothing, hygiene or safety, or is not able to appreciate the reasonably foreseeable consequences of a decision or lack of decision.” *Ibid* at s. 45.

<sup>27</sup> Incapacity to contract refers to an individual’s inability to understand the terms of a contract and to form a rationale judgment on the effect of the contract on the individual’s interests. *Armstrong v Gula*, [2024 ABKB 358](#) at para 109.

*RMK v NK*, [2020 ABQB 328](#) at paras 131-133.

<sup>28</sup> CP 31-103, *supra* at pp. 151-153.

<sup>29</sup> See: OSC [Resources for working with older clients and vulnerable clients \(White Label Materials\)](#) (last viewed: November 11, 2024).

<sup>30</sup> Notice of Amendment, *supra*, Annex “A”, q. II(4).

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individual says or does, such observations are not determinative of whether an individual actually lacks capacity.<sup>31</sup> This underscores the difficulties associated with identifying signs of financial exploitation and incapacity.

#### **b) Trusted Contract Person**

Section 13.02.01 of NI-103 provides that, as part of each registrant's "know your client" obligations, registrants must take reasonable steps to obtain and keep current the name and contact information of a "trusted contact person" for each client.<sup>32</sup> Registrants are also required to take reasonable steps to obtain each client's consent to contact their trusted contact person regarding, among other matters, the registrant's concerns about possible financial exploitation of the client and/or the client's mental capacity to make decisions involving financial matters.<sup>33</sup>

According to CP-103, the "trusted contact person" is intended to be a resource for registrants to protect the client's financial interests when responding to concerns of potential financial exploitation or incapacity.<sup>34</sup>

#### **c) Temporary Holds**

Section 13.19(1) and (2) of N1 103-31 provides that registrants *must not* place a temporary hold on a client account unless the registrant "reasonably believes" that: (a) the client is vulnerable and financial exploitation of the client "has occurred, is occurring, has been attempted or will be attempted"; or (b) the client does not have the mental capacity "to make decisions involving financial matters".<sup>35</sup> Section 13.19(3) of N1 103-31 goes on to prescribe the steps that registrants must follow when placing a temporary hold on a client transaction including the requirements to provide notice to the client and to review the underlying facts.<sup>36</sup>

### **V. THE IMPORTANCE OF CLIENT AUTONOMY**

There is no doubt that protecting vulnerable clients from financial exploitation is an important policy objective. However, as the CSA has recognized, a balance must be struck between protecting investors and respecting client autonomy within a private contractual relationship.<sup>37</sup> This recognition is consistent with Ontario's legal framework for capacity, decision-making, and guardianship. As noted in the Law Commission of Ontario's *Final Report on Legal Capacity, Decision-Making and Guardianship*, for example, Ontario's legal framework is premised on several key policy choices, which include, among other things, a clear presumption of capacity and protection of self-determination and freedom from unwarranted intervention.<sup>38</sup>

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<sup>31</sup> *Starson, supra* at para 15.

<sup>32</sup> NI 31-103, *supra* at s. 13.2.01. See also: Dealer Rules, *supra*, rule 3202(4).

<sup>33</sup> *Ibid.*

<sup>34</sup> CP 31-103, *supra* at p. 153.

<sup>35</sup> NI 31-103, *supra* at s.13.02.01. See also: Dealer Rules, *supra*, rule 3222 (1).

<sup>36</sup> NI 31-103, *supra* at s.13.19(3). See also: Dealer Rules, *supra*, rule 3222(3).

<sup>37</sup> CSA Notice of Amendments, *supra* at Annex "A", q. V(1).

<sup>38</sup> Law Commission of Ontario, [Legal Capacity, Decision-making, and Guardianship](#) (March 2017), pp. 90-91.

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A client should not be denied autonomy simply because a registrant observes signs of what may be perceived as vulnerability or diminished capacity that falls short of an inability to make decisions involving financial matters. As the Supreme Court of Canada has noted, it is an error to equate the presence of a mental disability with incapacity.<sup>39</sup> Consistent with this proposition, the OSC has recognized that it is important to avoid the ageist tendency to regard all seniors as being “vulnerable” or unable to protect their own interests.<sup>40</sup>

Similarly, the outcome of a vulnerable client’s investment decisions should not be used to determine whether that client was subject to financial exploitation or incapable of making financial decisions. Put differently, it should not be assumed that a client was mentally incapable of making a decision or was a victim of financial exploitation just because the client may have shown signs of vulnerability and made poor financial decisions in hindsight. As noted by the Canadian Foundation for Advancement of Investor Rights:

“[...] At all times a client’s autonomy, self-determination and right to live at risk (including the risk of making poor financial decisions if they are mentally capable of understanding and appreciating the consequences of their decision) must be respected. Simply put, just because an older adult or a vulnerable investor makes a poor financial decision, or decides to invest unwisely in a way they have not previously done, or decides to unwisely invest in a family endeavour, this should not automatically trigger the thinking that this client may have mental capacity issues.”<sup>41</sup>

The risks associated with vulnerable clients making poor or unwise financial decisions are effectively mitigated by the extensive suitability obligations imposed on registrants by NI 31-103 and CISO’s Investment Dealer and Partially Consolidated Rules. As set out in s. 13.3(1) of NI 31-103, before a registrant opens an account for a client, purchases, sells, deposits, exchanges or transfers securities for a client’s account, takes any other investment action for a client, makes a recommendation to or exercises discretion to take any such action, the registrant must determine, on a reasonable basis, that the action satisfies the following criteria:

(a) the action is suitable for the client, based on the following factors:

- (i) the client’s information collected in accordance with section 13.2 [know your client];
- (ii) the registrant’s assessment or understanding of the security consistent with section 13.2.1 [know your product];
- (iii) the impact of the action on the client’s account, including the concentration of securities within the account and the liquidity of those securities;

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<sup>39</sup> *Starson, supra* at paras 10 and 77.

<sup>40</sup> Staff Notice 11-779, *supra* at pp. 3 and 11.

<sup>41</sup> Statement made in reference to placing temporary holds in response to incapacity. FAIR Report, *supra* at p. 64.



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(iv) the potential and actual impact of costs on the client's return on investment;

(v) a reasonable range of alternative actions available to the registrant through the registered firm, at the time the determination is made;

(b) the action puts the client's interest first.<sup>42</sup>

Section 13.3(2.1) of NI 31-103 goes on to provide that if a registrant receives instructions that do not satisfy the above conditions, the registrant cannot proceed with the investment action unless the registrant has informed the client, recommended alternative actions, and received confirmation to proceed from the client.<sup>43</sup> These regulatory obligations apply equally to clients demonstrating signs of vulnerability.

## VI. CONCLUSION

As it stands, registrants are in the difficult position of having to be aware of the various non-determinative and often subjective warning signs of possible client vulnerability, financial exploitation, and incapacity, which may not be apparent, while simultaneously respecting the fundamental concept of client autonomy in decision making. To promote a balance between client autonomy and property rights, on one hand, and client protection, on the other, regulators and policy makers should give serious consideration to providing registrants with a form of safe harbour defence or other statutory protections when servicing vulnerable clients.

As Canada's population ages, the autonomy and property rights of aging and vulnerable clients will become an increasingly important concern. Registrants must continue to respect their client's freedom to make financial decisions as a core expression of their autonomy and property rights. Similarly, financial regulators must continue to emphasize the importance of client autonomy and avoid inadvertently creating a second class of investor with weakened property rights.

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<sup>42</sup> NI 31-103, *supra* at s. 13.3 (1). See also: Dealer Rules, *supra*, rule 3402(1).

<sup>43</sup> NI 31-103, *supra* at s. 13.3 (2.1). See also: Dealer Rules, *supra*, rule 3402(5).