



**Independent Financial Brokers of Canada**

740-30 Eglinton Avenue West, Mississauga, ON L5R 3E7

December 13, 2018

British Columbia Securities Commission  
Alberta Securities Commission  
Financial and Consumer Affairs Authority of Saskatchewan  
Manitoba Securities Commission  
Ontario Securities Commission  
Autorité des marchés financiers  
Financial and Consumer Services Commission of New Brunswick  
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island  
Nova Scotia Securities Commission  
Securities Commission of Newfoundland and Labrador  
Registrar of Securities Northwest Territories  
Registrar of Securities, Yukon Territory  
Superintendent of Securities, Nunavut

**Attention:**

The Secretary  
Ontario Securities Commission  
20 Queen Street West  
22<sup>nd</sup> Floor, Box 55  
Toronto ON M5H 3S8

Me Anne-Marie Beaudoin  
Corporate Secretary  
Autorité des marchés financiers  
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Submitted by email:

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Dear Sirs and Mesdames:

**Subject: CSA Proposed Amendments to National Instrument 81-105 *Mutual Fund Sales Practices***

Independent Financial Brokers of Canada (IFB) appreciates the opportunity to provide comments on the proposed reforms to National Instrument 81-105 *Mutual Fund Sales Practices*, on behalf of its approximately 3,500 members across Canada.

IFB is a voluntary, not-for-profit, professional association, federally incorporated for over 35 years. IFB members are licensed financial advisors who operate on a self-employed and independent basis. IFB



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does not represent employees of financial institutions, or career advisors of proprietary firms. Most IFB members operate small to medium sized financial practices in their local communities. They provide personalized advice, generally on a commission basis, and offer clients a reasonable cost-effective choice beyond their local bank branch. The majority are regulated by the MFDA or IIROC, as well as their respective provincial life insurance regulator. Many also provide clients, either through their own firm or through their referral networks, with complementary services such as financial planning, group benefits, estate planning, mortgages, exempt products, and deposit brokering, for example.

IFB has responded to, and actively participated in, the many previous consultations and roundtables held by the CSA, and some CSA members, on potential reforms to the client-registrant relationship. An important part of IFB's mandate is to advocate on behalf of its members by bringing forward issues that are specifically focused on potential impacts to the clients of the small businesses and firms IFB members operate. By doing so, IFB is able to provide regulators with a different perspective than that of large financial institutions and trade associations.

Below are our comments on the proposed amendments that are relevant to IFB members and their clients.

### **Repeal of Section 3.1 - Elimination of upfront commissions**

The CSA has proposed the elimination of all upfront commissions, which it expects will eliminate the DSC option.

It has been IFB's position that investors should have choice in how they pay for the advice and services they receive, and that DSCs can be a valid choice for some investors. Just like any investment choice, however, before purchasing, investors should be fully informed as to the details and costs of the investment and how it fits with that investor's goals. DSCs can be helpful in supporting a longer-term commitment to investing, while also offering a declining redemption charge over time, the opportunity to change investments within the same fund family, and to redeem 10% of their holdings annually. The upfront commission paid to an advisor often permits them to service smaller accounts where the time and cost to do so might otherwise be prohibitive.

IFB is cognizant, however, of the investor concerns expressed by the CSA in relation to DSCs. In consideration of these concerns, IFB has suggested in previous submissions that DSCs be allowed to continue, albeit in a modified way. For example, the length of time investors would hold the mutual fund before they could redeem it without penalty could be shortened to add flexibility, and in recognition that many investors do not want to tie up their investment for 6 or 7 years. Alongside this shorter time frame, upfront payouts to firms would be reduced.

IFB has also suggested tightening the suitability requirements so that any recommendation of a DSC takes into consideration both the investor's time horizon and investment objectives, such as is required under the current SRO rules. We note that the proposed higher conduct standards contained in the CSA's Client-focused reforms and, in particular, the expanded conflict of interest rules proposed in NI31-103, will impact all investment recommendations, including DSCs.



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Of further note, it remains to be seen what the policy position of the Ontario government will be now that it has indicated that it may not agree with the outright elimination of the DSC option. IFB will comment further as details on the government's position become available.

Should the CSA proceed with its proposal to ban DSCs, however, IFB supports permitting the current redemption schedules to expire.

If DSCs are determined to be unsuitable, it is unclear to us why the CSA would permit new sales of these products during the transition period, rather than discontinuing these sales effective on the decision date. Permitting new DSC sales during the one year transition period will only increase the potential risks for investors. As well, advisors who recommend such products during the transition will be subject to heightened scrutiny and potential enforcement from 'hindsight' suitability reviews. We see no value in this scenario.

### **Amendment of section 3.2 – Elimination of payment of trailing commissions**

IFB supports the proposal to eliminate the payment of trailing commissions to dealers where no suitability determination is required in connection with the client's purchase or ongoing ownership of mutual fund securities. This would affect order-execution-only dealers, and some permitted clients.

As the CSA notes, if investors are switched into a mutual fund with no trailing commissions, this will trigger delivery of the fund facts document unless the CSA provides an exemption. While we agree in principle with an exemption, if an exemption is used investors may not have the most current fund facts, i.e., the version with trailer information excluded.

### **Definition of "trailing commission"**

The CSA is proposing to include a definition of trailing commission which would more broadly include any payment for services provided to the client in connection with their ownership of the mutual fund.

We observe that the purpose of the proposal to disallow payment of trailer fees to order-execution-only (OEO) brokers, or in other instances when no suitability is provided to the client, is founded on the lack of advice provided to investors under these circumstances. The CSA's view is that investors should not be paying fees related to advice that they are not, in fact, getting. Broadening the definition to include any services provided to the client, not limited to advice, will require clear language so firms and advisors understand what "services" are (or are not) captured as a trailing commission.

### **Modernization of NI81-105**

#### Section 5.4 Industry Association Sponsored Events

The CSA has posed several questions regarding future modernization of NI81-105, which has remained largely unchanged since May 1998. While most of the instrument continues to be relevant to the regulation of the sales practices of mutual funds, Section 5.4 *Industry Association Sponsored Events*,



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which deals with restrictions on educational events is outdated, and the process unduly prescriptive. It specifically provides relief for education provided by IFIC and the (former) IDA. Other “trade or industry associations”, and industry participants must make application for exemptions from the provisions that do not fit with today’s educational marketplace.

As an example, IFB sponsors educational opportunities and events across Canada relevant to financial intermediaries and advisors, which are focused on market conduct, industry trends, compliance and regulatory issues. Pursuant to the restrictions in NI81-105, IFB applied for and received exemptive relief from Section 5.4 in February 2008. The decision states that it *will terminate in that Jurisdiction one year after the publication in final form of any legislation or rule of that Decision Maker which modifies the provisions of section 5.4 of NI 81-105 in a manner which makes the relief provided for in this decision unnecessary or provides similar relief on a different basis or subject to different conditions.*

While the current CSA proposals do not affect Section 5.4, IFB submits that this is an opportunity to revisit these restrictions and employ a modern approach that would move away from naming specific providers (i.e., IFIC and the IDA), and the cumbersome process of applying for exemptive relief.

#### Scope of NI81-105

IFB agrees that NI81-105 should apply more broadly to include other investment products, not just prospectus qualified mutual funds. New types of investment products have been developed since NI81-105 was adopted in 1998, and they should be subject to similar controls on sales practices and other arrangements if they are not captured elsewhere. As per our comments on Section 5.4, however, we believe this should be part of an overall review that would seek to modernize the instrument and reduce the burden of overly prescriptive requirements.

#### Renaming ‘trailing commissions’

The CSA has asked for input on changing the term “trailing commission” to a plain language term. The term ‘trailing commission’, or ‘trail commissions’ is commonly used in many international jurisdictions.

In recent years, regulators, industry and investor groups have dedicated a great deal of time and resources to helping investors access more plain language explanation of investment terms, with the goal of raising the level of financial literacy amongst Canadians. In our view, renaming trailing commissions to some other term may well be more confusing. We think a better approach is to provide an explanation alongside the term, and/or redirect investors to where more explicit information is available. The fund facts, for example, contain an explanation, as do some regulatory websites, like the OSC’s “get smarter about money” website. Investors who work with an advisor have the advisor as a resource for more information and to answer questions like these.

#### **Regulatory arbitrage**

We agree that there is the risk of regulatory arbitrage between investment products whenever there is regulatory inconsistency. Elimination of the DSC option may well increase this risk. IFB has been a proponent of alternatives to outright elimination of the DSC option, as discussed above, which would



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help to mitigate this risk. If the CSA decides to pursue the elimination of DSCs, it will need to do so for any securities products offering a DSC option, and engage with other financial regulators to ensure processes are in place to protect investors of other financial products.

### **Closing remarks**

In closing, IFB notes that NI81-105 has been in place since 1998. It was aimed at controlling conflicts of interest in mutual fund sales practices, including the payment of higher commissions to encourage the sale of in-house or proprietary products. IFB has often commented on the influence of these types of structural incentives, and their impact on investors and advisors. Unfortunately, this has been a long-standing conflict of interest that has been permitted to carry on unchecked until IIROC, the MFDA and provincial/territorial securities regulators undertook the *Targeted Review of Member Compensation and Incentive Programs* in 2016/17, which resulted in the investigation and fining of some large firms by both IIROC and the MFDA. In other words, the problem was not the instrument, it was in the lack of enforcement. We believe, and continue to believe, that regulators do not need to create many more regulatory tools – what is needed are better controls and enforcement of existing rules so that the industry can remain competitive and innovative, while not stifling access to independent advice for Canadians.

Please contact the undersigned, or Susan Allemang, Director Policy & Regulatory Affairs (email: [sallemang@ifbc.ca](mailto:sallemang@ifbc.ca)) should you wish to discuss our comments further.

Yours truly,

A handwritten signature in black ink that reads 'Nancy Allan'.

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