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Dear Sirs/Mesdames:

Re: PCMA Response to CIRO Position Paper - Policy Options for Leveling the Advisor Compensation Playing Field

The Private Capital Markets Association of Canada (the “PCMA”) is pleased to provide its comments to the position paper titled “Policy options for leveling the advisor compensation playing field” (the “Position Paper”) published by the Canadian Investment Regulatory Organization (“CIRO”).

About the PCMA

The PCMA is a not-for-profit association founded in 2002 as the national voice of the exempt market dealers (“EMDs”), issuers and industry professionals in the private capital markets across Canada.

The PCMA plays a critical role in the private capital markets by:

- assisting hundreds of dealers and issuer member firms and individual dealing representatives to understand and implement their regulatory responsibilities;
- providing high-quality and in-depth educational opportunities to the private capital markets professionals;
- encouraging the highest standards of business conduct amongst its membership across Canada;
- increasing public and industry awareness of private capital markets in Canada;
- being the voice of the private capital markets to securities regulators, government agencies and other industry associations and public capital markets;
- providing valuable services and cost-saving opportunities to its member firms and individual dealing representatives; and
- connecting its members across Canada for business and professional networking.

Additional information about the PCMA is available on our website at www.pcmacanada.com. The PCMA has also established an advocacy site called **Fair and Balanced Regulation** which includes articles and comment letters by the PCMA and others about various matters that impact the private capital markets. See our advocacy website at: www.fairandbalancedregs.com.

General

Many PCMA members include firms registered solely as EMDs which are not required to be members of CIRO or subject to its rules and by-laws. The PCMA is submitting a comment letter as it believes this consultation is of national importance to all registrants, including EMDs and other dealers. All dealing representatives seek the same fairness and benefits and advantages of a compensation approach adopted by CIRO and the Canadian Securities Administrators (the “CSA”) for investment dealer – dealing representatives under securities legislation and registered representatives and investment representatives under CIRO investment dealer registration categories for individuals. A consistent regulatory approach is important for harmonization and creating a level playing field for all registrants. The PCMA requests that the CSA will consider the changes to be made by CIRO, and approved by the CSA, and enact similar changes for the benefit of all registration categories.

The PCMA commends the CSA for having established a Directed Commissions Working Group as set out in CSA Position Paper 25-404 – *New Self-Regulatory Organization Framework*¹ as part of its then review of creating a new SRO. At such time, the PCMA understood that the CSA would also consider the compensation structures applicable to other registration categories including EMDs and their dealing representatives.

Since the coming into force of National Instrument 31-103 *Registration Requirements and Exemptions* (“NI 31-103”) and its related Companion Policy 31-103CP *Registration Requirements and Exemptions* in September 2009, EMDs and dealing representatives have sought to establish a compensation model that permits directed commissions or an alternative arrangement to allow their fees and commissions to be directed to, or earned by, a personal corporation (*i.e.*, those involving registerable and non-registerable activities).

Many EMDs have looked at the approach taken by the Mutual Fund Dealers Association as set out in MFDA Rule 2.4.1 when it was then in effect before the establishment of CIRO, as guidance toward structuring compensation arrangements with their dealing representatives.

However, the regulatory uncertainty regarding directed commissions prevented many such registrants from availing themselves of a directed commission or other arrangement such as corporate licensing. The PCMA believes all registrants require and deserve certainty and a uniform securities regulatory approach, including in the creation of permitted registrant compensation arrangements.

¹ <https://www.securities-administrators.ca/uploadedFiles/General/pdfs/CSA%20Position%20Paper%20on%20SRO%20Framework%20-%20Final%20with%20Appendices.pdf>

Guidance from Life Insurance Agent Licensing

Many dealing representatives are dually licensed as life insurance agents and have established a licensed corporation or partnership to receive commissions. Such individuals would seek to structure their compensation arrangements involving their securities business in a similar manner, preferably under the same entity.

The Position Paper suggests that a registered corporation approach would allow the entity to receive compensation for registerable and non-registerable activities. The PCMA recommends that CSA members and CIRO (collectively, the **Securities Regulators**) consider allowing a registered individual or Approved Person² to utilize a single licensed and registered corporation for both life insurance agent and dealing representative activities, if desired, to provide the registered individual or Approved Person with the flexibility to structure their business and affairs (the “**registered corporation approach**”). We note that legalizing a registered corporation would allow registered individuals or Approved Persons, to structure their compensation arrangements in a manner to minimize their tax liability to the full extent of the law as permitted by the long-standing Duke of Westminster principle affirmed by the Supreme Court of Canada.³

The PCMA recommends that Securities Regulators specifically contemplate the following in any regulatory and/or legislative amendments to facilitate the registered corporation approach:

- explicitly permit a corporation to register as a dealing representative sponsored by a registered dealer in accordance with securities law; and
- permit registered corporations to conduct "non-registerable" activities including life insurance, in the same manner as registered individuals under securities legislation.

The PCMA believes that dually licensed and registered corporation can provide appropriate flexibility to registered individuals without compromising investor protection. This situation is currently permitted for registered individuals.

Taxation Benefits

The PCMA understands that CIRO is not considering any tax benefits in the Position Paper, however, the PCMA notes that setting up a corporation to receive commissions has many benefits to a registered individual, which vary depending on the facts for each individual, including, but not limited to the following:

- *Lower overall tax rate* - The combined corporate and personal tax rates on income earned inside a corporation can be lower than personal tax rates on income earned directly by an individual registrant;

² See full definition in Corporation Investment Dealer and Partially Consolidated Rules in Rule 1200 s.1201(2) <https://www.ciro.ca/media/16/download?inline>. An Approved Person is an individual approved by CIRO to carry out functions for an investment dealer including an investment representative, portfolio manager, and a registered representative.

³ See article titled “*The Supreme Court of Canada confirms taxpayers are entitled to arrange their affairs to minimize tax payable*” at <https://www.fillmoreriley.com/publication/the-supreme-court-of-canada-confirms-taxpayers-are-entitled-to-arrange-their-affairs-to-minimize-tax-payable>

- *Income splitting* - Corporations provide more flexibility for dealing representatives to split income with family members through dividends;
- *Tax deferral* - Income retained and invested inside the corporation can benefit from tax deferral until withdrawn as dividends or salary to the registered individual;
- *Capital gains exemption* - Up to \$1,016,836 (for 2024) of capital gains realized on disposal of qualified small business corporation shares can be tax exempt for individuals;
- *Estate planning* - Shares of a corporation can be gradually passed to heirs in a tax efficient manner.

PCMA Responses to Specific Questions

Question #1

This paper discusses compensation approaches that could be made available for use to all CIRO Approved Persons. Which of the following rulemaking options do you prefer that CIRO pursue and why:

- pure adoption of an Incorporated Approved Person approach,
- pure adoption of a registered corporation approach, or
- interim allowed use of an enhanced directed commission approach while pursuing over the medium-term the adoption of either:
 - an Incorporated Approved Person approach, or
 - a registered corporation approach.

The PCMA strongly recommends the pure adoption of a registered corporation approach. The PCMA believes this is the optimal policy option to harmonize registrant compensation regulation nationally, provide individual registrants, including Approved Persons, flexibility in structuring their compensation arrangements while maintaining strong investor protection.

The PCMA believes the CSA could amend NI 31-103 to permit a registered corporation approach as it has done with many other proposed changes to securities law and publish a proposed rule with a comment period and implement such changes appropriately. Those CSA jurisdictions that require legislative amendments could be addressed and harmonized with those changes adopted by the CSA under changes to NI 31-103.

As stated in the Position Paper, “registered corporation” legislation was passed by the Saskatchewan legislature in 2012 and by the Alberta legislature in 2014, but has not been proclaimed in force. The PCMA believes it is important to have a national uniform approach led by the CSA and that legislation in the various jurisdictions be conformed as much as possible.

In further support of a CSA-led initiative on registrant compensation models, the PCMA notes that:

- the Incorporated Approved Person Approach only benefits CIRO members and not all other registrants, including EMDs and their dealing representatives, which is inconsistent with having a harmonized and fair approach for all registrants; and
- the Enhanced Directed Commission Approach arguably provides lesser protection since compliance oversight is left to the sponsoring dealer firm and not the applicable Securities

Regulator. In addition, this is an interim approach adding a step which could increase costs for registered firms as they may have to make changes to their compensation structures twice.

In addition to the foregoing, the PCMA's supports the pure adoption of the registered corporation approach for the following reasons:

- It provides direct regulatory oversight by the Securities Regulators of a registered corporation's activities and ownership, ensuring transparency and compliance oversight.
- It enables registered individuals to engage in both registerable (*e.g.*, those involving the business of advising and the business of trading) and non-registerable activities through their registered corporation and allows registered corporations to engage in outside activities in the same manner as registered individuals.
- It holds registered individuals directly accountable and liable to clients, Securities Regulators, and sponsoring dealers or advisers for all activities within the registered corporation, maintaining high standards. Under this model, poor supervision or compliance failures at the corporate level could potentially trigger direct regulatory disciplinary action against registered individuals personally, including potential suspension. This threat of direct sanctions creates very strong incentives to maintain discipline and integrity when conducting registerable activities through a registered corporation.
- The registered corporation offers clients statutory rights and additional investor protections under existing securities legislation. For example, having registered corporations would enable clients to file complaints with the Ombudsman for Investment and Banking Services regarding, among other things, misconduct by a registered corporation and its registered individuals. Securities Regulators could investigate and take potential enforcement actions against the registered corporation, as appropriate, based on existing investor protection rules.
- It allows limitations and restrictions on ownership and activities to be implemented through legislative provisions. For example, securities legislation could restrict ownership of registered corporations solely to registered individuals and their immediate family members. Ownership by other parties could be prohibited.
- Registered corporations establish a consistent national framework applied equally for all registrants in Canada. This legislative harmonization would eliminate current discrepancies and inconsistencies between different dealer categories (*e.g.* EMD vs. investment dealers vs. mutual fund dealers vs. scholarship plan dealers vs. restricted dealers) as well as across different jurisdictions.

Question #2

Are there other requirements not discussed in this paper that CIRO should include within any rule amendments it proposes relating to acceptable compensation approaches?

The PCMA believes CIRO should consider clarifying the following matters in connection with any rule amendment, which should equally apply to the CSA when considering implementing similar changes across all registration categories and in all jurisdictions:

- clearly state what specific corporate, shareholder, and compensation information must be disclosed to Securities Regulators and sponsoring registrant firms under the new compensation frameworks;
- clarify the specific books and records registered corporations would be required to maintain for review by Securities Regulators;
- clearly explain the role of a registered corporation and registered individuals in the relationship disclosure information documents provided to clients as required under NI 31-103; and
- require notice to Securities Regulators of material changes to the registered corporation.

The PCMA discussed other issues in the preamble to the responses to Questions.

* * *

In summary, while the PCMA strongly supports the pure adoption of the registered corporation approach it also encourages the CSA to lead this initiative to ensure changes to compensation arrangements benefit all registrants and not just CIRO members.

The PCMA welcomes further discussion on creating an optimal harmonized national framework for registrant compensation.

Yours truly,

PCMA Advocacy Committee

“Brian Koscak”

*Chair of Advocacy Committee
PCMA Vice-Chair*

“Nadine Milne”

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“David Gilkes”

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“Michael Edwards”, CA, CLU

PCMA Member

cc: PCMA Board of Directors

