

March 25, 2024

Member Regulation Policy
Canadian Investment Regulatory Organization
(as of Monday February 12, 2024)
40 Temperance St,
Toronto, Ontario M5H 0B4
e-mail: memberpolicymailbox@ciro.ca

Market Regulation
Ontario Securities Commission
Suite 1903, Box 55
20 Queen Street West Toronto, Ontario M5H 3S8
e-mail: marketregulation@osc.gov.on.ca

Capital Markets Regulation
B.C. Securities Commission
P.O. Box 10142, Pacific Centre
701 West Georgia Street, Vancouver, British Columbia, V7Y 1L2
e-mail: CMRdistributionofSROdocuments@bcsc.bc.ca

RE: Position Paper – Policy options for leveling the advisor compensation playing field (“Position Paper”)

Established in 1996, the Federation of Independent Dealers (FID) serves as the premier collective voice for independent dealer firms in Canada. The Federation advocates on behalf of dealer firms overseeing assets under administration in excess of \$125 billion. These dealers represent a substantial network of over thirty thousand licensed registrants, offering a comprehensive range of financial services and planning to more than 3.8 million Canadians.

Our organization is deeply invested in matters that affect the interests of the independent dealer community and the professional advisors within it.

We thank CIRO for the opportunity to provide comments on the Position Paper.

General comments

We support the concept of leveling the advisor compensation options. Financial advisors on the investment dealer (ID) channel should enjoy the same business option that has been available on the mutual fund dealer (MFD) channel for over three decades.

The Position Paper provides a brief overview of this ongoing successful approach to commission redirection. It then posits generalized potential risks to build a case for changes to this business structure. This model has been in place without investor, dealer, or regulator harms for many years. We see no basis for change on the MFD side, nor for denying identical opportunities to ID registrants.

We would like CIRO to provide Option iii (a) for ID firms and Representatives as firms take advantage of the new dual-platform option to have both MFD and ID platforms in the same legal entity. Registrants should be able to continue operating as-is, move between platforms within the same dealer, or even transition their entire practice between ID and MFD firms without having to legally reconstruct it.

The proposed enhancements will increase oversight burden and costs. The position paper does not successfully make a case for changing, removing, restricting, or reducing the existing business model (the 'enhancements') for thousands of MFD registrants and their corporations across Canada. Footnote 15 states:

"A common concern/issue with all approaches (i.e., the current directed commission approach permitted under MFD Rule 2.4.1 and the three approaches analyzed within this position paper) is that securities legislation amendments would need to be enacted to allow Approved Persons to engage in and to be compensated for registerable activities within the corporation.

The difference between the existing commission redirection model and the proposed incorporated approved person model appears to be CIRO obtaining formal regulatory jurisdiction over the corporation, given that neither format currently permits registrable activities and would not be able to do so without legislative changes (as noted above, per footnote 15).

There may be business preference or specific provincial circumstances where this option could offer a benefit, and as it can be enabled via CIRO rulemaking, we would like it enabled as an additional option. Once legislative changes are pursued and eventually enacted to enable registrable activities under a corporation (similar to what exists today for insurance representatives), we would like to revisit this issue with a second consultation on specific implementation rules, timelines, and responsibilities.

CIRO will have to ensure the model doesn't create conflict between in-force Principal/Agent model advisory businesses and the CRAs view of small business corporations.

The CRA has launched a broad review of personal corporations to determine if they qualify as Personal Service Businesses (PSB). If a business is deemed to be a PSB, they could be subject to additional taxation. PSBs can face a tax rate of 44.5% versus 12.2% for corporations eligible for the small business rate.^{1 2}

"The tax hit on personal services business income could be as high as 66.3 per cent when paid as a dividend to an individual in Ontario's top tax bracket."³

¹ <https://www.theglobeandmail.com/investing/personal-finance/taxes/article-the-taxmans-project-on-incorporated-employees-is-in-full-swing/>

² https://www.dmcl.ca/between_sheets/be-aware-new-cra-campaign-focuses-in-on-personal-services-businesses/

³ <https://www.krp.ca/cra-is-scrutinizing-personal-services-businesses-heres-why>

Response to specific questions

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.*

We prefer the existing directed commission approach that is available to the MFD channel. The Position Paper does not provide evidence of any actual issues being caused by directed commissions and we are not aware of any either: the concerns are speculative, and we don't believe it is appropriate to create burdensome requirements that don't address or solve actual problems.

We believe that the concerns expressed in the position paper can be addressed with existing tools and substantial enhancements aren't needed at this time. A much simpler approach would be to slightly extend the current outside activities filings, firstly, by prescribing that any corporation to which a representative's commissions are paid constitutes an outside activity for that representative, and secondly, by requiring the outside activity filing on the National Registration Database ("NRD") to include a brief description of the corporation's business activities and its substantial shareholders. Dealers would review the information, as they currently do for all outside activities and will screen out corporations whose activities or shareholders raise concerns. Regulators, similarly, will know the corporations' activities and shareholders and can take appropriate action if concerns are raised.

We are very concerned that proposals which require legislative amendments are, in practice, not much more than aspirational and may create the impression of CIRO meeting its commitment to address the commissions issue without any prospect of being in place in any meaningful timeframe. The approach described in the preceding paragraph would address the practical regulatory concerns without requiring undue burdens on regulators, dealers, or registrants, without requiring legislative amendments, and without requiring any material changes to the NRD.

We've addressed the specific concerns with the existing directed commission approach below.

a. Risk one: Insufficient transparency

We are not aware of any risk that creates a need for additional disclosures or transparency and associated overhead for MFD member firms. We would expect the same track record to be established by ID member firms.

b. Risk two: Beneficial owners

We would like a better description of how disclosure of the beneficial owners of an advisor's corporation mitigates a tangible investor risk. The proposed solution to tackle this lack of transparency is to ban ownership by anyone who isn't a CIRO registrant. This appears to be a regulatory leap and will create issues with existing MFD businesses that have non-registrant owners. Transparency can be further addressed if necessary with enhancements to the Outside Business Activity rules.

c. Risk three: Activities undertaken

It isn't clear how the proposed requirements would prevent a corporation which is not permitted to engage in registrable activities from - illegally – engaging in registrable activities, or why redirecting the commissions of a registrant to the corporation increases that risk.

d. Risk four: CIRO jurisdiction over Approved Person, and limiting corporation activities to non-registrable activities.

Is this concern whether non-registered staff are performing the registrable work of registrants and licensees? The work within the corporation that would be considered registrable can only be performed by registrants under current legislation.

CIRO is seeking the authority to investigate books and records to detect whether licensing requirements are being breached. Dealers are currently required to oversee registrants' outside activities and the Position Paper doesn't provide evidence that the current regime is insufficient or has exposed clients to risk. We believe that an agreement, such as that included below in Appendix A (MSN-0072 Schedule A)⁴, would provide adequate authority for CIRO without creating the additional burden of a full registration or licensing regime for corporations that receive registrants commissions. MSN-0072 Schedule A, par. 3, shows clearly that regulators already have access to records of the corporation:

*"3. The Approved Person and Payee shall make available during normal business hours to the MFDA, the Member or any securities commission in Canada having jurisdiction over the Member, their authorized officers, employees and agents, free access to, and copies thereof, all books of account, bank accounts, correspondence and records of every description of, or maintained by or on behalf of, either of them"*⁵

Registrable activities are carried out on behalf of the dealer member, who oversees the registrable activities. Regulations enabling personal corporations can contain clauses preventing registrable activities by non-registrant staff, although those would merely be saying that illegal activities are illegal, which is redundant. These proposals appear to be an increase to CIROs scope of activity.

⁴ See Appendix A, MSN-0072-1, MFDA Staff Notice, Schedule "A"

⁵ <https://mfda.ca/wp-content/uploads/MSN-0072.pdf>

“CIRO sets and enforces rules for the business and financial conduct of Canadian investment and mutual fund firms and their representatives across Canada. All registered representatives are subject to high proficiency standards, training, and supervision by member firms.

The compliance teams examine firms for compliance with conduct, trading, prudential and operating rules, and work with firms to ensure they continually meet high standards while providing financial services to their clients.”⁶

The ‘enhanced directed commission’ approach could eventually be an ideal state for both CIRO and its ID/MFD members. We recommend enabling this option and rolling it out to ID members, and MFDs on an opt-in basis once the legislation has been passed. This will give participating dealers an opportunity to consider, adapt and implement needed policies and procedures. Then after a reasonable period, review the benefits and assess any needed changes.

There are a variety of implementations for MFD advisor corporations that are in place currently. Many of these will not want, and cannot implement without restructuring and cost, to eliminate their current corporations, redraft constating documents, divest ownership stakes, or create secondary corporations to reassemble their business models in response to CIROs aim of a ‘pure adoption of an Incorporated Approved Person approach’. We would like a detailed rationale on the impetus to change the existing MFD model, risks of offering this to ID firms, and the need to implement the noted additional jurisdiction for CIRO over private corporations.

As positioned, there will be no opportunities for estate freeze, trust, or estate transactions, on-boarding of new advisors or staff with minority ownership stakes, and no earn-out of retired advisors via share buyouts as these require non-registrant owners. We would like to see CIRO focusing on increasing opportunities for the growth of both large and niche businesses. This can be an opportunity to increase productivity and employment within advice distribution channel, which will in turn benefit all Canadians.

We would expect that such learned and respected bodies would not continue to permit this practice and then explicitly allow it if there was evidence that it posed risks to investors.

Different dealer business models will prefer different implementations of advisor incorporation/directed commissions. Larger businesses, or those operating on an employer/employee basis have reasons to prefer the Incorporated Approved Person model, option iii(b). The bulk of firms utilizing the principal/agent model will prefer the existing directed commissions model, as it suits their needs well.

The FID wants a successful implementation for ID member firms of the tried and true commission redirection practice that MFDs have used for more than 30 years without creating client, dealer, or regulatory issues (the Alberta Securities Commission referenced the practice in its ASC Policy 3.7 which was adopted in 1992). The CSA’s Distribution Structures Committee Position Paper,

⁶ CIRO <https://www.ciro.ca/about-ciro>

released in 1999, also discussed the practice since it had been well-established in most provinces at that point.

The proposed changes represent increased regulator and dealer oversight of private corporations that are not involved in registrable activity, in addition to the existing responsibility to oversee licensee activities. We don't support these changes, particularly without a fulsome need analysis and discussion of the specific costs CIRO expects to incur, the specific benefits to be gained, specific investor risks mitigated, and the metrics used to track them.

Respectfully,

Matthew T. Latimer

Executive Director,
Federation of Independent Dealers

Appendix A

Contact: Paige Ward
General Counsel and Vice-President, Policy
Phone: (416) 943-5838
Email: pward@mfda.ca

MSN-0072
March 29, 2010
(Replaces MSN-0002)

MFDA STAFF NOTICE

PAYMENT OF COMMISSIONS TO UNREGISTERED CORPORATION

MFDA Staff Notices are intended to assist Members and their Approved Persons in the interpretation, application of and compliance with requirements under MFDA By-laws and Rules. Notices make reference to these requirements and set out MFDA staff's interpretation of how to comply with these requirements. Notices may also include best practices or guidance.

This Notice replaces MFDA Staff Notice MSN-0002 *Payment of Commissions to Non-Registered Entities*, issued on May 15, 2001. The form of Agreement issued as Schedule "A" to that Notice has been revised in accordance with the terms of Rule 2.4.1 (Payment of Commissions to Unregistered Corporation), as amended, and will be replaced by the Agreement contained in this Notice.

Background

The securities regulatory authorities in British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, New Brunswick and Nova Scotia (the "Recognizing Regulators") have approved/not objected to proposed amendments to MFDA Rule 2.4.1. The Rule, as revised, is effective immediately.

Under Rule 2.4.1, as revised, where an Approved Person acts as an agent of the Member in compliance with MFDA Rule 1.1.5 (Agents), the Member may direct payments in respect of business conducted by the Approved Person on behalf of the Member to an unregistered corporation, subject to the conditions specified in subsection 2.4.1(b). Subsection 2.4.1(b) of the revised Rule does not apply in Alberta and, as a result, with respect to clients in Alberta, commissions must be paid directly to the registered salesperson.

Under subsection 2.4.1(b)(iii), the Member, Approved Person and unregistered corporation are required to enter into an Agreement in writing, in a form prescribed by and in favour of the MFDA. Schedule "A" to this Notice sets out the prescribed form of the Agreement to be executed for the purpose of complying with subsection 2.4.1(b)(iii).

Implementation of New Requirements

Members who are presently directing payments to unregistered corporations in respect of business conducted by Approved Persons on their behalf have until **March 26, 2011** to have the revised Agreement provided as Schedule "A" to this Notice executed by all required parties and

in place. Members who wish to start directing such payments to unregistered corporations on or after **March 31, 2010** must have the revised Agreement executed by all required parties and in place prior to any such payments being made.

DOCs 302596v3

SCHEDULE "A"

_____, 20 _____

MUTUAL FUND DEALERS ASSOCIATION OF CANADA / ASSOCIATION CANADIENNE DES COURTIERS DE FONDS MUTUELS ("MFDA")

AGREEMENT

BETWEEN:

_____ ("Member")

AND: _____ ("Approved Person")

AND: _____ ("Payee")

RE: **Agreement made pursuant to MFDA Rule 2.4.1 (Payment of Commissions to Unregistered Corporation)**

The undersigned Member, Approved Person and Payee, in accordance with the terms and conditions set out in MFDA Rule 2.4.1 that allow for payment of commissions to unregistered corporations, each hereby agree by and between themselves and with and for the benefit of the MFDA and any securities commission having jurisdiction over any of the foregoing parties as follows:

1. The Member and Approved Person shall comply with applicable MFDA By-laws and Rules and securities legislation and remain liable to third parties, including clients, irrespective of whether any remuneration, gratuity, benefit or any other consideration is paid to the Payee and no such payment shall, in and of itself, in any way limit or affect the duties, obligations or liability of the Member or the Approved Person under MFDA Rules and applicable securities legislation;
2. The Member shall engage in appropriate supervision with respect to the conduct of the Approved Person and the Payee to ensure such compliance as referred to in paragraph 1;
3. The Approved Person and Payee shall make available during normal business hours to the MFDA, the Member or any securities commission in Canada having jurisdiction over the Member, their authorized officers, employees and agents, free access to, and copies thereof, all books of account, bank accounts, correspondence and records of every description of, or maintained by or on behalf of, either of them;
4. A request made in accordance with paragraph 3 shall be for the purpose of determining compliance by the Member and/or each of the undersigned and its respective shareholders, directors, officers, employees and affiliates with the By-laws, Rules and Policies of the MFDA and applicable securities legislation, and each of the undersigned shall, and shall cause such shareholders, directors, officers and affiliates to, fully cooperate with any of the persons entitled to access to the records and other information referred to in paragraph 3 for such purpose. In addition, any such person so entitled to access to records and information is authorized to provide or disclose the same to any securities commission or similar regulatory authority, self-regulatory organization or law enforcement agency, subject to any applicable law restricting such disclosure;
5. The Member is receiving this agreement by each of the undersigned for itself and for the benefit of the MFDA and any applicable securities commission and the MFDA and any such securities commission shall be able to rely on this Agreement and enforce its terms without any duty or obligation to any other person, including the parties hereto;

6. The undersigned Approved Person shall take such steps and execute such documents including acting and voting as a director, officer, shareholder or employee of the Payee as may be necessary to cause the Payee to comply with this Agreement.

DATED this _____ day of _____, 20 _____

Approved Person: _____ Signed: _____
(Full legal name)

Payee: _____
(Full legal name)

(Authorized person) Signed: _____

Member: _____
(Full legal name)

(Authorized person) Signed: _____

Address where records maintained:

Telephone: _____

Fax: _____

E-mail: _____