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*President and Chief Executive Officer*

June 9, 2000

Purdy Crawford, Q.C., Chair  
Securities Review Advisory Committee  
c/o Osler, Hoskins & Harcourt LLP  
Box 50  
1 First Canadian Place  
Toronto, Ontario  
M5X 1B8

Dear Mr. Crawford:

**Re: Five-Year Review of Securities Legislation in Ontario**

The Canadian Association of Insurance and Financial Advisors (CAIFA) is pleased to respond to your Committee's Request for Comments, published in the Ontario Securities Commission Bulletin on April 28, 2000.

Founded in 1906, CAIFA has for most of its history been the national professional association for sales intermediaries and advisors in the life insurance sector of financial services. CAIFA now comprises approximately 18,000 members, all of whom are voluntary. Our members participate in the activities of the Association through 51 local chapters.

Recent surveys indicate that approximately 63% of CAIFA's members nationwide are registered to act as salespersons for mutual funds or other securities. We estimate that 70% of CAIFA's 8,000 members in Ontario are securities registrants.

The Association's members advise their clients on the short-term and long-range financial needs of individuals, families and the owners of small and medium-sized businesses. CAIFA's membership reflects the convergence of life insurance with other financial sectors, notably securities.

Notwithstanding the diversity of their activities, the common activity of CAIFA's members may be described as: Providing financial advice to Canadians, using life and health insurance and other financial products to achieve financial objectives.

## **CAIFA's Interest in the Five-Year Review**

CAIFA first participated actively in policy consultations relating to securities approximately five years ago. The occasion was the release of the first Stromberg report on the mutual fund sector. In the intervening five years, the financial services industry has evolved rapidly and our members' activities have evolved with it. It is fair to say that securities issues now occupy at least as much of our time and effort at CAIFA as life insurance. We expect that the succeeding five years will bring accelerating change that follows trends that are now clearly discernible.

Anticipating such change, we have decided to take at face value your committee's invitation to re-examine the fundamental principles of securities legislation, as well as its operational rules. We are taking the opportunity to consider the regulation of securities registrants on a blank sheet as it were. At the same time, we appreciate that there will be impediments to change deeply engrained current norms.

The views which follow will, of necessity, be preliminary. We trust that we will have an opportunity to develop them further in dialogue with your committee, as we do now with the more focused cross-sectoral task forces on investment funds and financial planning in which CAIFA participates.

The overriding theme in the communication which follows is: securities legislation should provide a framework to accommodate responsible change, subject always to the public interest, and not constitute a barrier to change.

**Keynotes of Change.** CAIFA's principal concerns and insights relate to the regulation of its members, "registrants" in securities terminology. We identify the keynotes of predictable change as follows:

- Increasing convergence of financial products and delivery channels.
- Increasing consumer demand for advice, especially long- term and comprehensive advice for an aging population, by comparison with the execution of transactions.
- Increasing functional role of product transactions as a means to implement financial advice and diminishing role of transactions in isolation.
- Diminishing role of financial advisors as intermediaries required for the execution of transactions.
- Increasing fiduciary obligations of financial advisors in relation to their clients arising from the advisory role.

**Impediments to Change.** In CAIFA's view, the historically dominant concepts that have shaped the regulation of securities salespersons are transaction oriented and fail to acknowledge the signposts of change noted in the preceding paragraph. Recent attempts by securities regulators to reassert and extend those concepts are retrogressive and counterproductive.

In this regard, we refer to the following cornerstone concepts of securities regulation and recommend that they be re-examined in the light of emerging realities:

1. A definition of "salesperson" that is confined to "an individual who is employed by a dealer for the purpose of making trades in securities on behalf of the dealer". The definition devalues the role of registrants and, despite accelerating disintermediation driven by technology, inhibits the evolution of intermediaries from salespersons to advisors.
2. A narrow regulatory focus on "trades" and a definition of "trade" that reduces all prior and surrounding advisory functions to "activities in furtherance of a trade", notwithstanding that the reality may be that the trade is an activity in furtherance of advice.
3. Notwithstanding the rise to primacy of financial advice and the convergence of financial services, a full-time occupation requirement that regards participation in financial activities other than trading in securities as an exemption from the norm rather than the norm. Contrast the comparable requirement in the Agents regulation under the Ontario *Insurance Act* (R.R.O. 1990, Reg. 663, s. 5), which requires Level I life licensees "to have his or her sole business in the provision of financial services".
4. A regulatory scheme for the distribution of mutual funds—a wholly liquid, diversified, branded, commoditized, investment management product—that is founded on enforcement principles that originated in the need to suppress the sale of fraudulent stocks and the victimization of the vulnerable individuals who might buy them.
5. A regulatory scheme for the sale of mutual funds that, notwithstanding the absence of a secondary market, focuses excessively on compliance by a dealer and absolves issuers of the product from a duty to screen, monitor and report, where necessary, the intermediaries they employ to distribute their product. Contrast the Agents regulation under the Ontario *Insurance Act* (R.R.O. 1990, Reg. 663, s. 15.2), which imposes those obligations on the issuers of insurance contracts.

Before I address the issues expressly identified in your published discussion paper, permit me to bring to your attention related views that CAIFA has put on the public record. They originate in CAIFA's proposed model for the regulation of financial intermediaries and CAIFA's response to the Canadian Securities Administrators position on distribution structures in Notice 33-304 (August 1999).

## **CAIFA's Model for the Regulation of Financial Intermediaries**

**Origin.** In the mid to late 1990s, CAIFA responded to a multitude of discussion papers and draft legislation from provinces across Canada that proposed greater or lesser change in the regulation of financial services and life insurance in particular. We undertook to assess those proposals and develop our own model for the regulation of financial intermediaries. In April 1999, CAIFA's board of directors approved the resulting model, which is attached to this letter as Appendix A.

**Securities Influence.** For the most part, the model addresses the regulation of intermediaries in life insurance. You will see that it borrows some concepts from securities regulation, such as the recognition of distribution companies that are roughly analogous to dealers.

At present, outside of Quebec, only life insurance companies may qualify as sponsors for life insurance intermediaries, for a training period that can be as short as two years. Under CAIFA's model, distribution companies, along with life insurance companies, could qualify as sponsors of life intermediaries during the first five years of an intermediary's career. Thereafter, a qualifying intermediary could choose to work as a sponsored intermediary, an independent or an independent that qualifies to sponsor and supervise other intermediaries.

**From Harmonization to Integration.** The model also proposes an evolutionary scheme of regulation of financial intermediaries across financial sectors. Legislation would initially harmonize standards for entry into the occupation of financial intermediary within current regulatory boundaries. Legislation would subsequently proceed to integrate regulation governing entry into the occupation of financial intermediary without regard to current regulatory boundaries.

The key concept here is the need to satisfy a basic, common standard of proficiency in the knowledge of financial services before proceeding to qualify to sell any particular product categories that are now demarcated as securities or insurance. CAIFA continues to recommend such a development.

**Proposals for Securities.** When CAIFA developed its model in 1998 and 1999, we decided that we would concentrate on the sector we know best, life insurance, and defer for the time being to established norms in the regulation of securities.

We did, however, recommend two innovations on the securities side:

1. Mandatory continuing education for securities registrants. We understand that the Investment Dealers Association has adopted that obligation under its by-laws and that the Canadian Securities Administrators, with input from CAIFA, has

incorporated that requirement in its financial planners proficiency standard (Multilateral Instrument 33-107).

2. A "duty of care" on the part of securities issuers to screen, monitor and report, if necessary, the intermediaries they employ to distribute their securities. This innovation is adapted from the current duty of care that applies to life insurance companies under the Agent regulation of the Ontario *Insurance Act*. It would have its greatest practical impact in the distribution of mutual funds.

We continue to recommend those innovations.

**Corporate Governance and Duty of Care.** We note that the Joint Forum of Financial Regulators at its meeting in April 2000 adopted 15 recommendations for changes in the regulation of mutual funds and individual variable annuity contracts (segregated funds). Among these was a recommendation to enhance the governance of mutual fund companies, notably by requiring independent directors and otherwise ensuring that effective independent participants are responsible for oversight of the management of the product and for protecting the interests of consumers.

CAIFA considers that its recommendation that mutual fund companies (and issuers in general) be subject to a duty of care in the screening, monitoring and reporting of their market intermediaries is consistent with the decision of the Canadian Securities Administrators (through the Joint Forum) to enhance corporate governance of mutual fund companies.

There are strong similarities between the relationship of a soliciting agent for a life insurance company and a sales representative for products of a mutual fund company. A standard of corporate governance for mutual fund companies and a duty of care in relation to the distribution of its products, familiar concepts on the life insurance side, are potentially valuable supplementary consumer safeguards.

**Holding Out and Disclosure.** CAIFA's model places a high premium on the need for a financial intermediary to communicate unambiguously to a client critical information about the intermediary's competencies, business relationships, sources and methods of compensation and potential conflicts of interest.

The intermediary should communicate this information in writing before the start of a business relationship with the client and should update it thereafter as required. The objective is to clarify who is accountable for the conduct of the intermediary by line of product or activity: mutual fund dealer, life insurance sponsor or the intermediary in his or her own right, as the case may be.

Intuitively, the fact that an intermediary is licensed to sell life insurance or is registered to sell mutual funds should head the list of information to be disclosed to a

client. However, securities legislation specifically forbids a registrant to disclose the fact of his or registration: Ontario *Securities Act*, section 44.

CAIFA recommends that the prohibition against disclosure of registration be deleted from the *Securities Act*.

**Future Needs.** Our earlier comments under "Keynotes of Change" and "Impediments to Change" underlie CAIFA's view that the historical dealer-registrant model of regulation is deficient. It is inappropriate when measured against evolving expectations that a financial advisor engages in a professional relationship with his or her clients characterized by high levels of mutual trust, technical proficiency and fiduciary obligations. By contrast, the dealer-registrant model emphasizes the dealer's policing role over a salesperson who, absent policing by the dealer, may be expected to sell unsuitable products to vulnerable investors.

CAIFA has not yet formally adopted a recommendation for the reform of the dealer-registrant model in the regulation of financial intermediaries that distribute mutual funds or other securities. Nevertheless, CAIFA implicitly believes that applying the dealer-registrant model as a universal norm will frustrate the full development of a financial intermediary who works in a fiduciary relationship with his or her clients founded on mutual trust and the role of advice-giver and who provides the optimum choice of financial products to implement that advice.

CAIFA offers for your consideration the proposition that current trends suggest that, barring artificial barriers, such a financial practitioner will emerge before the next five-year review of securities legislation. At the very least, securities legislation should not prevent that development. Rather, securities legislation should adapt to allow that practitioner to qualify to work independently of a dealer, subject to the criteria of experience, proficiency, financial viability and liability insurance proposed in CAIFA's model for life insurance intermediaries.

### **CSA Distribution Structures Position (Notice 33-304)**

The Canadian Securities Administrators' position on distribution structures was released as a CSA "Notice" document in August 1999. The document observes that certain innovative structures in the relationship of dealer and salesperson often serve the wishes of securities registrants with a background in life insurance. Some of these dual-licensees own independent financial services businesses. The resulting position paper addresses regulatory concerns that innovative distribution structures threaten the effectiveness of dealer-centered supervision and accountability.

CAIFA commented on draft versions of the notice document as it was developed in 1998 and 1999. Attached as Appendix B is CAIFA's response (September 22, 1999) to the CSA on its distribution structures position as adopted. We have since then discussed our concerns with the CSA Distribution Structures Committee itself and

with senior executives of the Ontario Securities Committee. Those concerns continue to trouble CAIFA profoundly.

The CSA position includes three core elements:

1. **Relationship of "Independent Contractor" is Precluded.** CAIFA acknowledges that, under established principles of securities regulation, a registered salesperson cannot engage in the business of a financial intermediary in securities as an "independent contractor" in relation to his or her dealer and that the two parties cannot contract out of their joint and several liabilities to the investing public.
2. **"Introducing Dealer" Concept.** The CSA position document proposes the concept of an "introducing dealer" that will be registered in a relationship with a "carrying dealer". In effect, the introducing dealer would be a salesperson who is elevated to the status of a dealer with limited business powers. It is proposed that the salesperson, as a minimalist "dealer", will be able to exercise some of the prerogatives of an entrepreneurial financial services business that are commonly accepted by regulators of incorporated life insurance agencies. CAIFA has given its qualified recognition that the concept may have value as an interim compromise measure. We await the release of the rules and by-laws of the Mutual Fund Dealers Association that are expected to implement the concept.
3. **Dealer Control of "All Financial Services Activities [of a Registrant] Not Subject to Another Regulatory Regime".** Since we first became aware of this proposal in December 1998, CAIFA has vigorously objected to it as unilateral regulatory overreaching and an ill-considered sweeping extension of a dealer's mandate, without foundation in securities legislation. CAIFA's response to the CSA, reproduced as Appendix B, explains our views in detail. They are summarized in the following paragraphs.

**"Financial Services Activities Not Subject to Another Regulatory Regime" in Practice.** The sale of life insurance begins with a needs analysis of a prospective client's financial circumstances. The scope of that analysis exceeds the suitability tests contemplated under the securities rubric of "know your client". The needs identified by a life agent may extend over generations and involve the administration and successive ownership of personal estates and businesses.

An advisor with a background in life insurance may, depending on the market he or she serves, offer financial services personally or in collaboration with other providers. The services provided may encompass financial planning, tax preparation, estate planning, employee benefits consulting, financial records administration, charitable giving and many others. While a life agent must always satisfy personal suitability criteria to hold a licence, the financial services activities just enumerated are not

subject to the direct control of the insurance regulator, that is, they are "not subject to another regulatory regime".

Consider the following examples:

1. B.M is the proprietor of a financial services business established over a quarter of a century ago. As part of his comprehensive service to individual and business clients, B.M offers tax preparation. The service is carried out by a leading national accounting firm retained by B.M for the purpose. B.M.'s clients pay B.M.'s company a fee for this service.
2. J.D. specializes in financial planning for families who must care for disabled family members. The disabilities may be mental or physical. The needs that are addressed extend over the lifetime of the individual and may involve three or four generations of the concerned family. Funding may derive from private family resources and public agencies. J.D. has come to acquire extraordinary expertise in coordinating the specialized services of accountants, lawyers, trustees, health professionals and social agencies.

If the CSA distribution structures principles are implemented as proposed, a securities dealer would be required to supervise a national accounting firm when it provides the financial service of tax preparation on behalf of B.M. B.M.'s clients would have to pay the dealer for those services. A securities dealer would similarly be required to supervise the specialized financial planning provided by J.D., including trust arrangements and the requirements of social welfare legislation.

CAIFA doubts that the CSA intended those outcomes or that those outcomes can plausibly advance the public interest.

**CAIFA's Position.** A dually licensed salesperson is the agent of a dealer with respect to providing investment advice in securities or furthering a trade in securities. CAIFA believes with profound conviction that the public interest cannot be served by requiring a securities dealer, solely in its capacity as a securities dealer, to be liable for and control financial services activities provided by its registrant salesperson where the dealer has no experience, interest or competence in those activities. That requirement will not prevent inadvertent negligence or fraudulent conduct by a salesperson who is intent on defrauding the public.

However, the proposed requirement, if implemented in its present form, will be detrimental to the public interest by increasing the market dominance of larger dealers who are able to implement compliance systems for financial services outside of securities. The requirement will be more grievously detrimental to the public interest, in CAIFA's view, by depriving the public of specialized and innovative financial services that securities dealers refuse to supervise.

## Specific Responses to Issues List

### *Fundamental Principles*

3. *Does the [Securities] Act adequately account for the marketplace shift from trade execution towards "assets under management" and "advice giving"? Should these activities be regulated differently than they are now?*

CAIFA's entire response so far is predicated on the premise that, in the retail market, advice giving is replacing the execution of transactions as the core activity of a financial advisor who is registered as a salesperson under the *Securities Act*.

In CAIFA's view, securities legislation should be amended to respond to that shift of responsibilities by removing barriers to offering comprehensive advice and products in the traditional demarcated financial sectors and facilitating the ability of a salesperson to provide client service in the manner of a regulated professional advisor. The hallmarks of that status are direct accountability of the service provider to the client, with suitable economic backstops such as liability insurance, bonding or a compensation fund, and membership in a self-regulatory organization which is directed by peers of the service provider.

### *Focus and Scope of Legislation*

- 8(a). *Should securities regulation be amended to reflect the shift in the way financial markets are structured? For example, are the current exemptions from regulation of securities based on the issuer still appropriate?*

The exemptions with which CAIFA is most familiar derive from the safety and soundness of the issuer: government, banks, trust companies and life insurance companies. In the case of federally regulated financial institutions, notably life insurance companies, consumer protection is founded on a comprehensive and rigorous statutory regime for corporate governance that is intended to minimize self-dealing and conflicts of interest and to maximize solvency and prudential management.

That standard of consumer protection equals or exceeds comparable regimes for investor protection under securities legislation. CAIFA recommends that securities regulation maintain the current exemption from regulation where it is founded on the safety and soundness of the issuing institution maintained under another regulatory regime.

**8(b) *Should legislation include some formal requirement to facilitate the coordination between financial services regulators?***

CAIFA is pleased to observe that such coordination is progressing without an express legislated mandate. We note the work of the Joint Forum of Financial Regulators and collaborative projects across life insurance and securities sectors in relation to proficiency standards for financial planners and the harmonized regulation of investment funds.

Nevertheless, CAIFA believes that it would be advantageous to establish such collaborative efforts on a formal basis that would reduce reliance on *ad hoc* and personal initiatives. Any such requirement should address coordination among sectors within Ontario (a natural consequence of the announced merger of the Ontario Securities Commission and the Financial Services Commission of Ontario), among the provinces and territories and between federal and provincial levels of government.

***Regulation of Registrants***

The following recommendations originate with CAIFA and do not correspond to issues identified in the request for comments.

**Incorporation of Salespersons.** The observation is sometimes made that life insurance agents incorporate to reduce taxes. In fact, the rules under the *Income Tax Act* attach onerous restrictions to so-called incorporated employees. Incorporation may be sought not only to reduce tax liabilities but also to facilitate succession planning and the disposition of a business upon retirement. An incorporated salesperson whose securities income derives exclusively from a single dealer may possibly be denied tax-saving opportunities but could nevertheless wish to incorporate for legitimate business reasons.

The Ontario budget of May 2, 2000 announced that "this Government proposes that the right to incorporate be extended to all regulated professionals". The announcement explained that the incorporation of professionals would be subject to the full professional liability of the incorporated individual. The concept appears to follow established provisions in British Columbia and Alberta that allow professional corporations with unlimited liability.

CAIFA is committed to the proposition that, driven by technological disintermediation and rising consumer expectations in financial services, financial services intermediaries must evolve to assume the fiduciary and ethical obligations and standards of proficiency that are characteristic of the traditional learned professions. CAIFA believes that financial services professionals that are registered as salespersons should be able to avail themselves of the promised ability to incorporate.

CAIFA recommends that the definition of "salesperson" in section 1 of the Ontario *Securities Act* be amended to read "a *person* who is employed by a dealer..." instead of "an *individual* who is employed by a dealer...". "Person" includes a corporation. "Employed", in CAIFA's view, is not limited to the legal relationship of a master and servant but bears the dictionary meaning of "is engaged or utilized for a purpose".

CAIFA fully appreciates that the CSA has proposed to allow salespersons who wish to incorporate to qualify as an "introducing dealer". Nevertheless, that arrangement may not be suitable in many circumstances where incorporation is desired and is not contrary to the public interest. The concept of the "introducing dealer" remains untested in practice. CAIFA seeks legislative flexibility to allow incorporation, where appropriate, under future regulatory arrangements.

**Full-time Occupation.** Section 127 of the Ontario *Securities Regulation* requires full-time occupation as a securities salesperson, subject to certain exemptions. CAIFA recommends that the full-time occupation requirement under the Ontario *Securities Regulation* be amended to harmonize with the Agent regulation under the Ontario *Insurance Act*, which requires a life insurance agent who is subject to a full-time occupation requirement "to have his or her sole business in the provision of financial services".

**Holding Out as Registrant.** CAIFA recommends that the prohibition against disclosing in writing one's status as a registrant contained in section 44 of the Ontario *Securities Act* be deleted to enable multi-licensed financial intermediaries to disclose to potential clients material information about their competencies and the regulatory oversight to which they are subject.

### ***Mutual Funds***

27. *Since 1997, the CSA have been working with the Investment Dealers Association of Canada and the Investment Funds Institute of Canada to facilitate the establishment of a self-regulatory organization for distributors of mutual funds in Canada. Moreover, in May 1998 the CSA promulgated rules governing mutual fund sales practices. More recently, the CSA published a position paper which sets out acceptable ways in which securities firms will be expected to structure themselves for the purpose of distributing securities to the investing public. Are there additional reforms that are necessary or desirable in the area relating to the distribution of investment funds?*

**Mutual Fund Dealers Association.** CAIFA awaits the release for public comment of the rules and by-laws which will enable the MFDA to operate as a self-regulatory organization. We anticipate that, if those rules include an acceptable and practical

implementation of the "introducing dealer" concept, a substantial number of CAIFA's members may become members of the MFDA in addition to the 300 or so independent dealers that are now contemplated. Anticipating that development, CAIFA recommends legislation that will facilitate the evolution of the MFDA into an SRO that is directed by its own members rather than by a board that is controlled by representatives of external organizations.

In this regard, CAIFA would recommend its generally favorable experience with life insurance councils in the western provinces. CAIFA continues to recommend that form of self-regulation, subject to the proviso that a cross-sectoral basis of self-regulation may better address today's consumer needs and expectations than self-regulation that is based on a single regulated product, whether life insurance or mutual funds. CAIFA would welcome legislation that enables the formation of an SRO that reflects the reality of its dual and multi-licensed members.

Quebec has adopted a scheme of self-regulation under the auspices of its "Financial Services Bureau" that includes a "Financial Security Chamber", an SRO of integrated firms that provide both investment funds and life insurance products. CAIFA has supported that concept in Quebec and recommends that a similar concept be considered in Ontario.

In the fullness of time, CAIFA suggests that the public interest may be well served if the MFDA evolves into two SROs: an SRO of mutual fund dealers that operate as wholesale distributors of mutual funds and a professional SRO of professional financial advisors, who may carry on business in corporate form, and who serve the retail market as advisors who can provide mutual funds and life insurance products alike.

CAIFA recommends that securities legislation anticipate these and other future possibilities for self-regulation and sectoral consolidation in framework provisions that may be invoked when desired without undue delay.

**Mutual Fund Sales Practices Rule.** The rule (NI81-105) has been in force for two years. On the basis of its own direct experience with section 5.4 of the rule ("Industry Association Sponsored Events"), CAIFA believes that a review of the rule in practice with view to possible amendments would be timely. Such a review would be beneficial before the Canadian Council of Insurance Regulators implements its recent decision to consider a similar rule for the distribution of individual variable insurance contracts (segregated funds).

**CSA Distribution Structures Position.** CAIFA's views on CSA Notice 33-304 appear above and in our letter to the CSA, attached as Appendix B.

### ***Impact of Regulatory Harmonization and Globalization Trends***

32.     a.     ***Is the mutual reliance review system an effective means of achieving inter-provincial cooperation and harmonization?***
- b.     ***Are there other areas of securities regulation where it would be beneficial to have a more "seamless" form of regulation between provincial securities regulators?***
- c.     ***Should the Act explicitly recognize the ability of the Commission, in appropriate circumstances, to delegate functions to other securities regulators in Canada or elsewhere?***

CAIFA has participated in the mutual reliance system for exemptive relief from the prohibition contained in NI81-105 against mutual fund companies sponsoring the educational events of a trade association. While we have come to appreciate the ability of a lead regulator to coordinate a series of interprovincial applications, we believe that the potential of mutual reliance remains to be realized. For example, there can be little justification for the continuing need to file individual paper applications to each regulator and to pay fees for amounts that vary from \$0 to \$750 to each regulator when the lead or coordinating regulator charges \$450 and does the most work.

CAIFA recommends that the *Securities Act* be amended to facilitate the further development of a mutual reliance system

- that will enable a single filing with a lead regulator,
- that will be supported by a harmonized fee structure that reflects the differential obligations of a lead regulator and participating regulators and
- that will permit, wherever possible and appropriate, participating regulators to delegate to the lead regulator the decision making authority for all participants.

Delegation of decision-making authority could be provided as the norm for some routine functions, provided that a regulator could elect to reassert its jurisdiction. For other less routine functions, delegation could be an option that would require consent following notice and review of the initiating application.

### ***Mandate and Role of Commission***

#### ***39(a) Is the rule-making process an effective way of regulating?***

CAIFA has sought an amendment to the mutual fund sales practices rule (NI81-105) since December 1998. We are advised that our request is reasonable and unobjectionable. Nevertheless, we can discern no progress towards an amendment. It

would appear that one of the rationales for extending rule-making powers to securities regulators has yet to be fully realized, the potential for timely and expeditious amendments that address changing conditions and accumulating experience.

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We appreciate that many of the preceding comments are novel in the context of securities regulation as it is now understood. We would be happy to meet with your committee to discuss the views we have presented or any other aspect of the regulation of financial advisors. I am available at CAIFA's national office in Toronto. My e-mail address is: [thibs@caifa.com](mailto:thibs@caifa.com). In my absence, I may refer you to Ed Rothberg, CAIFA's Associate General Counsel, e-mail: [rothberg@caifa.com](mailto:rothberg@caifa.com).

Yours very truly,

A handwritten signature in cursive script, appearing to read "D. Thibaudeau".

David J. Thibaudeau, CLU, CFP, CH.F.C.

**CAIFA RESPONSE—APPENDIX "A"**  
**Regulating Financial Intermediaries:**  
**A Model**  
**Proposed by the**  
**Canadian Association Of Insurance And Financial Advisors**

Developed by CAIFA's Task Force on the Distribution of Financial Products and Services:

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Approved by CAIFA's board of directors: April 13, 1999

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**Regulating Financial Intermediaries:  
A Model  
Proposed by the  
Canadian Association Of Insurance And Financial Advisors**

**1.**

**APPLICATION OF THE MODEL**

**1.1 From Fragmented Regulation to Co-ordinated Regulation to Integrated Regulation**

CAIFA's model recognizes that "financial intermediary" at present refers to practitioners in fragmented financial sectors who are regulated by different regulators under separate regulatory schemes. Some of these practitioners work in more than one sector and are subject to more than one regulatory system. For example, most life agents have qualified to sell mutual funds. Many securities sales representatives have acquired a life licence.

CAIFA believes, along with other observers, that the regulation of financial intermediaries who work in the retail market, that is, serving individuals and households, should be harmonized and ultimately integrated. CAIFA's model therefore proposes that, when it is fully implemented, "financial intermediary" will mean an intermediary who qualifies under a common standard that is set for a financial intermediary before the individual proceeds to qualify to sell any particular category of product.

However, CAIFA's model does not wait for that outcome to occur. In the first instance, the model proposes changes that existing regulators can adopt separately. Those changes could then be adopted by a co-ordinating council for the financial services sectors similar to the Council of Financial Regulators proposed for Ontario in 1998. A co-ordinating council would include, as a minimum, the chief executive officers of insurance and securities regulators. CAIFA's model foresees that a co-ordinating council would evolve into a fully integrated financial services regulator, possibly a self-regulating organization.

**1.2 Definition of a "Financial Intermediary"**

CAIFA's model addresses face-to-face distribution by financial intermediaries. A "financial intermediary" is any individual who is authorized by regulation to sell financial products such as life insurance, including variable insurance contracts commonly known as segregated funds, health insurance, mutual funds and other securities. "Individual" is the critical element. The model does not at this time address the regulation of impersonal means of distribution such as direct mail, telemarketing or the Internet. Neither does it consider the regulation of the transaction and requirements such as prospectus or other product disclosure, replacement procedures or other anti-churning safeguards and statutory remedies.

Securities legislation creates ten or so categories of financial intermediaries, called "dealers", that are generally organized as corporations or partnerships. Depending on the category, a dealer may be authorized to sell all securities or specific types, such as scholarship plans or mutual funds. Dealers in turn engage registered salespersons as a kind of subintermediary. "Financial intermediary" in CAIFA's model, in respect of securities, refers to a registered salesperson of a securities dealer and not the dealer.

### **1.3 Note on Fee-Only Financial Planners**

By definition, a "financial intermediary" as described above does not include a fee-only financial advisor or planner. CAIFA's model does not address that activity. To a large extent, the regulation of financial planning is required to protect the public from sellers of product who hold themselves out as financial planners without qualifications. The holding out requirement described below addresses that problem: see section 5.2 ("Financial Planners"). Fee-only planners may be addressed at another time, if necessary. The relatively small number of self-described financial planners who do not sell financial products are unlikely to attract or remain in business if they cannot deliver the expertise that they promise. They require a different regulatory model, if any.

At present, only Quebec maintains legislation that governs financial planners who do not sell a regulated financial product or work for a regulated financial institution. CAIFA believes that a body which upholds uniform standards of proficiency and ethical conduct, such as the Financial Planning Standards Council, should govern fee-only financial planners.

### **1.4 Note on Estate Planners**

Estate planning is a distinctive activity which overlaps with elements of financial planning, the law of trusts and the applications of life insurance. Estate planning in the past has often been utilized by individuals with substantial estates who engaged a relatively small number of specialists in the area, often associated with trust companies and law firms. The requirements of an aging population have increased awareness of and demand for the services of specialists in estate planning. Financial intermediaries are responding to meet this demand. CAIFA anticipates that its model will in future address estate planning as a distinct activity.

## OVERVIEW

CAIFA's model is based on the following principles:

### 2.1 Requirements For Becoming A Financial Intermediary

2.1.1 Educational background: require a minimum general educational standard

2.1.2 Sponsorship:

- a) establish criteria for individuals or entities that will supervise a financial intermediary
- b) recognize that suitable sponsors or supervisors may take many forms
- c) recognize that practitioners in some financial sectors (notably, life and health insurance) should be able to work independently following a period of initial supervision and satisfactory demonstration of prescribed qualifications

2.1.3 Examinations:

- a) require demonstration of basic financial knowledge before proceeding to qualify to sell any particular product category
- b) require demonstration of proficiency to sell any desired particular product category
- c) optional: subsequently, demonstrate proficiency to sell independently in sectors (such as life and health insurance) that recognize independent financial intermediaries
- d) optional: subsequently, demonstrate proficiency to supervise financial intermediaries who do not qualify or do not wish to practice independently.

### 2.2 Overview: Product Sales Licensing Differentiated By Industry Regulators

	<b>Life and Health Insurance</b> (Including Segregated Funds) <i>Suggested Model</i>	<b>Mutual Funds</b> (see Appendix A for current regulation) <i>Suggested Model</i>	<b>Securities Generally</b> (see Appendix A for current regulation) <i>Suggested Model</i>
1. Examination	Expand proficiency requirement to test for basic financial knowledge as prerequisite to licence to sell insurance (or other financial product)	Same as for insurance: See Appendix A	Same as for insurance: See Appendix A
2. Supervision/ Accountability	Sponsor responsible for licensed individual while contracted until individual obtains independent status – require sponsor to satisfy proficiency requirement re Compliance/supervision	No change: See Appendix A	No change: See Appendix A
3. Duty of Care of Product Issuer	Issuing insurance company has statutory duty of care to screen, monitor and report (if unsuitable) its intermediaries (Ont. Reg. 663)	Issuing mutual fund company has statutory duty of care to screen, monitor and report (if unsuitable) its intermediaries	Securities issuer has statutory duty of care to screen, monitor and report (if unsuitable) its intermediaries

4. E&O Insurance (with fraud insurance)	Support concept of mandatory E&O insurance coverage including fraud and extended tail coverage	Same as for insurance: See Appendix A	Same as for insurance: See Appendix A
5. Obtaining Independent Status	Achieve independent status if: <ul style="list-style-type: none"> <li>• Min. 5 years experience and meets advanced licensing requirement</li> <li>• Financially viable; evidenced by initial capital adequacy and annual reports or bonding</li> <li>• No actions against or claims paid for fraud</li> </ul>	No change: See Appendix A	No change: See Appendix A
6. Full time Occupation	Insurance and related financial services be the sole occupation for new entrants into life insurance	Same as for insurance: See Appendix A	Same as for insurance: See Appendix A
7. Continuing Education	Support on going CE requirements for all licensees and actively pursue goal of harmonized CE requirement –minimum of 30 hours every 2 years	Same as for insurance	Same as for insurance
8. Public Database	Company and public access to information re misconduct and licence status for all licensed financial service providers	Same as for insurance	Same as for insurance
9. Complaints Register	Compliance/supervision obligations include maintaining a register of complaints	Same as for insurance	Same as for insurance
10. Compensation Sharing	Compensation be paid only to insurance agent licensed for class of insurance required for activity in respect of which payment made	Same as for insurance; otherwise, no change: See Appendix A	Same as for insurance; otherwise, no change: See Appendix A
11. Referral Fees	Referring agent to obtain prior consent of client; selling agent to disclose to client where payment made for referral	Same as for insurance	Same as for insurance
12. Financial Planning Certification	Financial service regulators recognize Financial Planners Standards Council as certification body for those who hold out as financial planners	Same as for insurance	Same as for insurance

### 2.3 Holding Out Regulations For All Financial Intermediaries

The key principle of the model is that effective disclosure to a potential client of relevant information about the financial intermediary before the client enters into a transaction will go far to prevent consumer complaints afterwards. Relevant information can include: business relationships, method of compensation, certification required to hold out as financial planner or financial advisor. The important element of the model is that rules governing holding out should be harmonized.

### 3.

## THE REGULATORY MODEL IN DETAIL

### 3.1 Requirements For Becoming A Financial Intermediary

#### 3.1.1 Educational Background

High school graduation or matriculation should be the minimum standard. Applicants should be able to demonstrate equivalent achievement where circumstances precluded formal education, for example, where war or civil unrest disrupted formal education in a foreign country.

#### 3.1.2 Sponsorship

- a) All entrants should enter into a contractual relationship with a recognized organization in the financial services industry which will be responsible for overseeing the development of the candidate.
- b) Suitable sponsor supervisors may take many forms provided that they meet established criteria. Criteria would include financial viability; experience; and resources to administer a program of training, supervision and compliance, including the appointment of personnel who have demonstrated personal competence in a supervisory role. An examination similar to the Partners, Directors and Senior Officers Qualifying Examination or the Branch Managers Examination under securities legislation would be desirable for this purpose if modified for individuals who supervise financial intermediaries in other sectors.
- c) Where a financial intermediary works in the securities area, qualifying sponsors could include the existing concept of a dealer under securities legislation. In life and health insurance, potential sponsors could be a life company, managing general agency, corporate agency which houses a qualified designated supervisor or an independent agent who meets the qualification of a supervisor.
- d) CAIFA's regulatory model recognizes that practitioners in some financial sectors (notably, life and health insurance) should be able to work independently following a period of initial supervision and satisfactory demonstration of prescribed qualifications. The rationale for this differential treatment of practitioners in different financial sectors is based on the differing methods of distribution in those sectors and the different roles in those sectors of a financial intermediary in relation to the purchasing client and the producer of the financial product in question. For example, purchasers of life insurance products ordinarily pay premiums directly to a life insurance company and not to an agent or incorporated agency. Life insurance policies are not issued or held in nominee form. By contrast, payments for a security will be paid directly to the intermediary dealer, which may hold the security in its own name. The need for close supervision of intermediaries is markedly less for intermediaries in life insurance than in securities.
- e) CAIFA's regulatory model proposes that, where financial intermediaries engage in multiple lines of business, they may be supervised by a different sponsor in each line and satisfy criteria to work independently which may differ from sector to sector.

### 3.1.3 Examinations

- a) A financial intermediary must demonstrate mastery of basic financial knowledge before proceeding to qualify to sell any particular product category. The standard could, for example, be based on the knowledge necessary to read the financial press intelligently, including rudiments of the capital markets, business and personal finance, taxation, retirement and estate planning, and so on, and to understand basic accounting principles and simple balance sheets.
- b) When the model is fully implemented, an integrated financial services regulatory body, which could be a self-regulating organization (SRO), would set the standard for basic financial knowledge and administer an examination. We cannot wait for the formation of such a body. In the immediate future, CAIFA will ask individual regulators to establish an examination of basic financial knowledge as part of their licensing requirements. For example, the life insurance licensing requirement could include a preliminary exam on basic financial knowledge that all candidates must pass. Alternatively, the licensing exam could include a separate section on basic financial knowledge that all candidates must pass.
- c) In the medium term, CAIFA would encourage the separate regulators to co-operate and coordinate the development of common standards and examinations. Then, the final stage would be the development and implementation of a basic financial educational standard by a single body that has jurisdiction over all financial intermediaries.
- d) The model requires that any financial intermediary demonstrate proficiency to sell any particular product category, after demonstrating mastery of the basic financial standard described in a). The model does not at this time define what, or how broad or narrow, the product categories should be, for example, life insurance vs. accident and sickness or life vs. segregated funds.
- e) Following satisfactory completion of the basic financial examination and sector-specific examinations, a program of mandatory continuing education would ensure that the financial intermediary maintained required levels of proficiency.
- f) An optional subsequent examination could be required to demonstrate proficiency to sell independently in sectors (such as life and health insurance) that recognize independent financial intermediaries.
- g) A second optional subsequent examination (similar to the Partners', Directors' and Senior Officers' Qualifying Examination or Branch Manager's Examination under securities legislation) could be required to demonstrate proficiency to supervise financial intermediaries by individuals who wish to assume that role.

### 3.1.4 Financial Planning Certification

- a) See comments under "Financial Planners" at section 3.4.2 below. Before a financial intermediary may hold out that he or she is a financial planner or a financial advisor, he or she must satisfy requirements established by his or her regulator. A financial intermediary who is licensed to sell life insurance would satisfy the holding out requirements of the insurance regulator.
- b) CAIFA supports a common proficiency standard for those who wish to hold out as financial planner. The Financial Planners Standards Council (FPSC) or some restructured version of the FPSC should administer the test and be recognized by financial service regulators as the certification body for those who hold out as financial planners.

## 3.2 Ongoing Requirements To Act As A Financial Intermediary

### 3.2.1 Continuing Education

- a) Every financial intermediary should complete a minimum of 30 hours of continuing education every two years in skills and subject matter that will directly enhance the financial intermediary's ability to advise and serve clients.
- b) The requirement should be coordinated to avoid unnecessary duplication of requirements and to recognize parallel continuing education requirements required by regulators in individual financial sectors and by recognized standard setting and designating granting organizations such as the FPSC and CAIFA.

### 3.2.2 Accountability

- a) Responsibility for supervision is inseparable from accountability.
- b) Where an individual or entity supervises a financial intermediary with respect to a line of business, the financial intermediary must hold out in the name of that responsible party in activities related to that business. A consolidated list of lines of business and entities that are responsible for each must be included in the personal information statement described in section 3.4.1. That requirement is needed to indicate to the affected consumer just who will be responsible for an improper transaction or advice. (As a practical matter, in most cases, mandatory errors and omissions (E&O) insurance will shift financial liability to the E&O carrier of the legally liable party.)
- c) Thus, where a problem relates to securities, the dealer who is responsible for the financial intermediary alleged to be at fault will be the point of redress.
- d) Similarly, where a problem relates to life or health insurance, the sponsoring supervisor of the financial intermediary alleged to be at fault—life insurance company, managing general agent (MGA), corporate agency or independent agent, as the case may be—will be the point of redress.
- e) Where a problem originates with an independent financial intermediary, the point of redress will be that independent agent.
- f) Each financial services distribution firm, including a sole proprietorship whose principal is authorized to work independently, must designate an individual who is responsible for training and supervision of financial intermediaries and responding to consumer complaints (cf. proposals in insurance regulation for "nominees" (B.C.) and "designated representatives" (Alberta)). The designated representative of a sole proprietorship shall be the sole proprietor. The designated representative of a partnership, corporation or branch will be required to pass an examination for supervisors described above in paragraph 3.1.3 g).
- g) In all cases, legal accountability will be backed up by liability insurance. This is especially critical to allow life agents to be independent and accountable.
- h) Because the consumer of life insurance always contracts directly with a life insurance company, the existing legal model of company liability for the acts of its representatives must remain. The legal principle of company liability may be modified to recognize the shared liability of a life company and its representative who is an independent financial intermediary or the supervising sponsor of a financial intermediary. In that case, the liability of the life company may flow from its duty of care to select and monitor the intermediaries with which it does business and report to the regulator any of its intermediaries

who it has reason to believe are unsuitable, as provided under legislation in Quebec, Ontario and Saskatchewan.

- i) CAIFA proposes that issuers of financial products other than life insurance, such as mutual fund companies and the securities issuers generally, should similarly be required to exercise a duty of care in selecting and monitoring their sales representatives. These will generally be mutual fund and securities dealers but will be individual representatives where an issuer distributes through a captive sales force. There should be an obligation to report any of its intermediaries—corporate or individual—which an issuing company has reason to consider are unsuitable.
- j) Distribution companies, i.e., including securities dealers, corporate insurance agencies, managing general agents, should similarly have a duty to screen, monitor and report (if unsuitable) financial intermediaries through whom they accept business.
- k) An effective producers' database covering multiple financial sectors (described below in section 3.3) will help issuing companies and distribution companies to carry out an obligation to screen, monitor and report (if unsuitable) their intermediaries.
- l) Distribution firms that are registered or licensed, including direct distributors of financial products and sole proprietorships, should be required to maintain a register of consumer complaints and to develop a procedure for monitoring and responding to complaints (as required in Quebec).
- m) Accountability has two aspects: (1) liability to compensate an injured party for the misconduct of the supervised financial intermediary and (2) exposure to regulatory sanctions, such as restrictions on the ability to supervise or other loss of privileges, for failure to carry out duty to train and supervise.
- n) Because no compliance system can prevent the misconduct of an individual who is intent on engaging in fraud or other criminal activity, the accountability of a diligent sponsor should not ordinarily extend to criminal misconduct of a supervised financial intermediary. However, a sponsor will be liable to a victim of fraud or other criminal activity to the extent that its failure to supervise diligently caused preventable harm to the victim.

### **3.3 Public Database**

- a) CAIFA supports the establishment of a database that is accessible to the public, which will inform the consumer who is authorized to act as a financial services representative and what that person is authorized to sell.
- b) Databases could initially be sponsored separately by individual regulators of the traditional sectors. Ultimately, an effective database would include all financial intermediaries who are authorized to sell a financial product anywhere in Canada so that users of the database would not have to cross-reference multiple databases to obtain information about any particular financial intermediary.
- c) The database should also provide restricted access to licensing authorities and compliance officers of mutual fund companies and other securities issuers, insurance companies and distribution companies (and ultimately to all parties with a need-to-know in any sector) to information that is not in the public record about a producer's market conduct history. Restricted information could include a history of complaints filed against the financial intermediary but not necessarily adjudicated or substantiated by a finding of guilt.

### **3.4. Holding Out Requirements For All Financial Intermediaries**

#### **3.4.1 Personal Information Statement**

- a) A financial intermediary should disclose to a potential client relevant information that may influence the potential client's decision to enter into or continue a business relationship with the financial intermediary. Relevant information would include: business relationship of the financial intermediary with other entities, source and method of compensation, qualifications and so on.
- b) The financial intermediary should provide to a customer, before giving advice on or selling financial products or services, information in writing about the financial intermediary's affiliations and qualifications, including:
  - (i) the licences held by the financial intermediary relevant to acting as a financial intermediary
  - (ii) the names of the financial institutions or distributors with which the financial intermediary does a substantial portion of his or her business
  - (iii) the fact that the financial intermediary receives financial compensation for selling financial products and the method and source of such compensation
- (c) The financial intermediary's personal information statement should disclose in writing to the customer any fee or compensation paid or payable to a third party for the referral prior to arranging a financial services transaction with the customer.
- (d) The financial intermediary's personal information statement should disclose to a prospective customer all conflicts of interest or potential conflicts of interest that may be associated with a transaction. The personal information statement should disclose:
  - all financial institutions that have an ownership interest in the distribution company with which the financial intermediary is affiliated and
  - the providers of financial products which are affiliated with the distribution company.
- (e) The financial intermediary's personal information statement should be amended as soon as practicable to reflect any material change in the information contained therein. The financial intermediary should distribute the personal information statement to all clients when it is amended and in all cases at least once every twelve months.

#### **3.4.2 Financial Planners**

- a) This is a particular holding out issue that appears to be on its way to a resolution. The key to the resolution is a coordinated effort by regulators of financial intermediaries to set proficiency requirements before a licensee or registrant may hold out as a financial planner.
- b) The British Columbia Securities Commission has adopted that approach. A BCSC registrant may not hold out as a financial planner or financial advisor unless the registrant qualifies to use the CFP designation or another listed designation that is acceptable to the Commission. Listed designations include the CLU, RFP and, as promised, the CH.F.C.
- c) Initiatives led by the Ontario Securities Commission may lead to the adoption of a proficiency examination as the basic standard for financial intermediaries who wish to hold out as financial planners.

CAIFA will recommend an examination and designation endorsed by the FPSC for this purpose but may be prepared to modify this stance to accommodate a restructured FPSC or successor organization.

## 4.

### PRODUCT SALES LICENSING – LIFE AND HEALTH INSURANCE

#### 4.1 Examination

- a) CAIFA has consistently supported minimum educational standards for entry into the life and health insurance business and an upgrading of the exam requirements.
- b) As agents progress from initial licensing to obtaining (if they desire) independent status, they will need to demonstrate a marked increase in their knowledge of the life insurance business. Basic life licensing could possibly be completed in two stages, similar to the process in Quebec:
  - (i) passing an examination similar to a current Level I examination would qualify the candidate to receive a provisional licence (comparable to a learner's permit);
  - (ii) following a period of close supervision not to exceed one year, the candidate would have to satisfy requirements similar to those for Level II (IFATC, MQE or similar) to obtain a permanent life licence.
- c) The knowledge base that is required to properly inform consumers about income investment and wealth protection has expanded. It would therefore be desirable for financial intermediaries selling life insurance, segregated funds, mutual funds and other securities to have a basic knowledge about all these financial products in order to be able to give their customers the best service. If CAIFA's recommendation for minimum requirements for becoming a financial intermediary, including an examination on the basics of financial knowledge, are not taken up, then at least there should be an expanded proficiency requirement of the Level I exam to test for basic financial knowledge.

#### 4.2 Supervision

- a) CAIFA supports the concept that the duty to supervise should move closer to the individuals who are supervised and that there be accountability for day-to-day supervision whether the supervisor be the immediate supervisor, MGA or insurance company. If the supervisor is to be able to properly supervise and ensure that the agent complies with licensing and distribution rules, then the supervisor should be required to satisfy proficiency standards regarding compliance/supervision. Those who obtain independent status would not require supervision.
- b) Whoever sponsors the licensed status of the life and health insurance agent should be responsible for the licensee while the contractual relationship exists and until the licensee obtains independent status. Responsibility should include liability to third parties for the errors and omissions of the supervised financial intermediary and the possibility of restrictions on distribution activities or other regulatory discipline for failing to supervise properly.
- c) Given the long-term nature of life insurance and the likelihood that an agent or supervisor will be long gone when a claim arises, the life insurance company concerned should continue to be liable, as a minimum, for all matters arising out of the contract and for failing to exercise a due duty of care over its distributors.

- The company's duty of care will include an obligation to screen and monitor the intermediaries it chooses to contract with and to report any intermediaries that it finds to be unsuitable, as now required in Ontario and Quebec.
- Similar requirements should extend to distribution companies, i.e., MGAs and agencies organized as corporations, partnerships or sole proprietorships.

### 4.3 Errors and Omissions Insurance

- a) CAIFA supports the concept of mandatory errors and omissions (E&O) insurance, including extended tail coverage and fraud coverage, as a fundamental consumer protection measure.
- b) An effective plan must provide extended liability or so-called tail coverage to cover E&O complaints discovered and launched after an agent has left the business or the jurisdiction. CAIFA sponsors an E&O insurance plan for its members that contains such a provision.
- c) CAIFA's plan also provides fraud coverage mandated in Ontario and Newfoundland. Quebec (and, as announced, Alberta) and most professions rely on a separate compensation fund to compensate victims of fraud. In CAIFA's view, it is difficult to see what gaps an indemnity/compensation fund would fill when properly designed E&O insurance coverage is in place. However, CAIFA has not so far opposed the creation of a compensation fund to compensate victims of fraud committed by a financial intermediary.
- d) A compensation fund, if any, should be financed by assessments of product manufacturers as well as distributors.

### 4.4 Obtaining Independent Status

#### 4.4.1 A life agent may achieve independent status if the individual meets the following requirements:

- a) minimum of five years experience (B.C. has proposed a minimum of five years experience to supervise other life agents; a similar experience requirement should allow an independent agent in effect to supervise him/herself)
- b) meets advanced license requirements established to demonstrate the required proficiency of an independent agent; the advanced proficiency requirement should give credit for qualifying to use the CLU or a similar designation
- c) demonstrates that he or she is financially sound by providing evidence of compliance with minimum initial and continuing capital requirements (to be determined), which may be satisfied by securing a performance/fidelity bond in the requisite amount
- d) has no recent or outstanding actions against them or recent claims paid under their fraud coverage
- e) produces a report to the regulator annually re solvency and capital adequacy, including renewal of the bonding option described in paragraph c)

#### 4.4.2 In addition, if the agent who has obtained independent status agrees to act as a supervisor, then he or she must meet supervisory/accountability qualifications set out above in paragraphs 3.1.2(b) and 3.1.3(g).

## **4.5 Full time Occupation**

**4.5.1** A financial intermediary should engage in full time employment in financial services (not necessarily life and health insurance only) in the formative years of the occupation. This period could be less than the five years needed to obtain independent status.

**4.5.2** CAIFA strongly supports full-time occupation (insurance and related financial services) for new entrants for two reasons:

- The need for a beginning agent to master a foundation of knowledge and skills
- The right of a consumer and his or her dependants to advice and service from a provider who is fully committed to satisfying the needs of clients at a career stage when outside activities would dilute the required level of service.

**4.5.3** CAIFA believes there should be established by regulation a list of prohibited occupations that are deemed to expose a client to the risk of undue influence so that practitioners of those occupations may not hold a licence to sell life insurance.

## **4.6 Compensation Sharing**

**4.6.1** An individual must have a life and health insurance license to share in a commission for acting to further the sale of these products. Otherwise, the door would be open to allowing unaccountable individuals lacking required skills or knowledge to secure directly or influence an insurance transaction for personal gain contrary to the interests of the consumer. For example, securities regulators would unlikely have the resources or mandate to discipline a stockbroker for improperly pre-selling an insurance product through a life insurance licensee who co-operates with that stockbroker.

**4.6.2** CAIFA supports sharing compensation for a sale only with an insurance agent authorized to act as an insurance agent for the class of insurance in respect of which the compensation was paid.

**4.6.3** A licensee may pay referral fees for information that leads to a sale. The payment must be for information only and not for any activity which would require a licence. The selling agent must disclose to the purchasing client the fact of the referral and that it was obtained for compensation (see B.C. Securities Commission Local Policy Statement 3-22, s. 3.3). A licensee who wishes to pass information obtained through a relationship with a client or prospective client must first obtain that individual's consent.

## **4.7 Continuing Education**

**4.7.1** A financial intermediary should complete a minimum of 30 hours of continuing education in financial services every two years.

- Given the increasing diversity and complexity of financial services, practitioners must be current in their knowledge and skills and must continually upgrade their knowledge and skills to remain current.
- The objective is to protect consumers by maintaining the skills and knowledge required by an agent to serve his or her clients.

**4.7.2** The continuing education requirement may be satisfied by completing parallel requirements need to maintain the right to use the CFP, CLU or other recognized designation.

5.

### **TRANSITIONAL MEASURES**

CAIFA considers the proposals contained within the foregoing model for the regulation of financial intermediaries to be necessary for consumer protection. CAIFA therefore proposes that the recommended measures be adopted without grandfathering following a reasonable period that would allow all financial intermediaries to adapt to their requirements.

## Appendix “A”—Current Licensing Rules By Securities Regulators<sup>1</sup>

	<b>Mutual Funds And Securities Generally</b>
1. Examination	For mutual funds, completion of Canadian Securities Course (CSC) or Canadian Investment Fund Course For Securities license: CSC course and Registered Representative's Exam. New entrant exam if previously registered in foreign jurisdiction.
2. Supervision/ Accountability	Individual must complete six-month period supervision in accordance with Registered/ Investment Representative Monthly Supervision Report. Securities representatives have same requirement as funds reps, but must in addition successfully complete the Canadian Securities Institute (CSI) sponsored Professional Financial Planning Course or Part I of the Canadian Investment Management Course within 30 months. Licence is restricted to mutual funds and contracts of insurance. Sponsoring dealer is responsible for supervision. Supervision of the rep is by the Branch Manager, who must be a registered rep, have experience and have taken the Branch Manager Exam administered by CSI or by compliance office. If Branch Manager's experience is less than two years, District Council of Investment Dealers Association (IDA) must approve. There follows a six month period when the representative is strictly supervised by the Branch Manager.
3. Duty of care of Product Issuer	No express requirement to screen, monitor and report (if unsuitable) intermediaries
4. E&O (and Fraud) Insurance	No individual rep is required to have E&O coverage. The companies (dealers) are required to have five classes of financial institution bonds. Any loss through a dishonest or fraudulent act of a sales rep is covered by a fidelity bond (Reg. 4000 IDA Rule Book)
5. Independent Status	NI (National Instrument) 81-105 includes in definition of a representative an “independent contractor” and reference is also made to a personal holding company of a registered rep. The independent contractor must, however, be registered as a salesperson or partner, officer or director.
6. Full Time Occupation	Ontario Securities Regulation: s.127(1) sets out full time rule for registration or renewal of salesperson; s. 127(2) sets out nine exceptions including small/ remote communities and holding of life license. Director of Securities Commission and employer can exercise discretion, i.e., if other activity will not interfere with rep's duties and responsibilities and there is no conflict of interest arising from the outside activity. Under Bylaw 18.5 of the IDA, other employment cannot be with another member of the IDA.
7. Continuing Education	No specific references to continuing education can be found in securities legislation or regulations. The IDA Rule Book will include a new bylaw effective July 1/99 which stock exchanges will adopt as well in respect of continuing education. Registered reps, among others, will be expected to complete two courses over a three-year cycle dealing with compliance (mandatory) and product knowledge or professional development. Course selection guidelines are to be issued which will indicate approved courses available from various educational providers. IDA will track, audit and report on each registrant's continuing education status. Bylaw provides fines and other sanctions if continuing education requirements are not met.
8. Public Database	Unknown whether Securities Commission or SROs maintain a <u>public</u> database. The CSA approved in principle at its January 1999 meeting in Vancouver the development of a Canadian registration database and formation of Steering Group to develop it. It will increase accessibility and information available to investors. Privacy and operational rules to be determined (see: OSC Bulletin, Volume 22, Issue 6, 12 February 1999).
9. Complaints Register	No specific requirement

10. Compensation Sharing	<p>Every dealer is required to have a policy on referral fees and commission splitting. Dealer should ensure disclosure of same and client acknowledgement in writing. BC mandates disclosure of referral fee and commission splitting. Alberta, Saskatchewan, Manitoba, New Brunswick, Nova Scotia and Yukon Securities Commissions prohibit commission splitting. Others permit commission splitting subject to certain conditions, but it is not permitted if it is used to compensate an individual or entity for activities that would require registration.</p> <p>In Quebec referral fees and commission splitting require 30 days notice to QSC. The arrangement may only proceed if QSC does not object. Quebec requires dealers to maintain a central registry of commission sharing.</p> <p>Referral fees are permitted in Ontario and Saskatchewan providing that the referring party only elicited a general interest in investing and not an interest in purchasing specific securities (ORSCN-3)<sup>ii</sup> and SSC Notice 1.2)<sup>iii</sup>.</p> <p>Referral fees received or paid must all be recorded on the books of the dealer. Payment cannot be made to the representative directly (IFIC Compliance Guide).</p>
11. Referral Fees	See "10. Compensation Sharing"
12. Financial Planning Certification	<p>The only specific references to financial planning under securities legislation are found in Quebec and British Columbia. Dealers in Quebec:</p> <p>A dealer that intends to hold itself out as a financial planner is required to obtain the permission of the QSC and may only carry out the financial planning activities through registered individuals (QLP Q-9, s.12).</p> <p>Registered Reps in Quebec: If a registered rep intends to use the description "financial planner":</p> <ul style="list-style-type: none"> <li>(a) His/her dealer must have QSC approval;</li> <li>(b) The rep must notify the QSC in writing, forwarding a copy of the authorization referred to in (a), a copy of the degree entitling him or her to use the designation of a financial planner (FP) and proof of payment of the membership fees provided for under s.29 of the Act Respecting Market Intermediaries;</li> <li>(c) The rep must use such designation only with the title of the dealer's representative; and</li> <li>(d) Each transaction undertaken pursuant to a financial plan must be approved by an officer of the dealer.</li> </ul> <p>British Columbia: Registrants holding out as financial planners must be qualified to use the CFP or other approved designation.</p>

<sup>i</sup> Material largely based on Ontario Securities Act. Regulations of securities can be by Securities Commissions and two Self-Regulating Organizations, i.e., the Stock Exchanges and the Investment Dealers Association of Canada.

<sup>ii</sup> ORSCN-3 refers to Registration Staff Clarification Notices of the OSC.

<sup>iii</sup> SSC Notice 1.2 refers to Notice of Saskatchewan Securities Commission.

**Robert J. Cowan, CFP, CLU, CH.F.C.**  
*Chair*

September 22, 1999

Douglas M. Hyndman, Chair  
Canadian Securities Administrators  
C/o British Columbia Securities Commission  
865 Hornby Street—Suite 200  
Vancouver, British Columbia  
V6Z 2H4

Dear Mr. Hyndman:

**Re: Canadian Securities Administrators (CSA) Notice 33-304—CSA  
Distribution Structures Committee Position Paper**

I am writing on behalf of the Canadian Association of Insurance and Financial Advisors (CAIFA) and its 18,000 voluntary members to convey CAIFA's views on the noted Position Paper published by the CSA on August 30, 1999 and to establish a basis for further discussion.

All of CAIFA's full members hold a licence to engage in the business of life insurance. At a conservative estimate, approximately sixty percent of those 18,000 members are also registered to act as salespersons in mutual funds or other securities.

Notwithstanding the diversity of their activities, the common activity of CAIFA's members may be described as: Providing financial advice to Canadians, using life and health insurance and other financial products to achieve financial objectives.

### **Overview**

CAIFA submitted comments on earlier versions of the Position Paper to members of the CSA Distribution Structures Committee in January and June 1999. We have taken and continue to hold the following positions:

- CAIFA rejects vigorously the proposition advanced in the Position Paper that a mutual fund or other securities dealer, with little or no relevant experience, should supervise and control all activities, revenues, trade marks and trade

names of intermediaries in financial planning solely because they have contracted with the dealer to provide certain products to their clients.

- More generally, CAIFA rejects the proposition that pervades the Position Paper that a securities dealer has the universal obligation or even the authority to supervise and control the activities of its salespersons in financial services described by the reiterated phrase "financial services, not subject to another regulatory regime", that is, that are not activities in furtherance of a trade in securities.
- Rather, CAIFA advocates that, in an era of rapidly changing financial services and consumer expectations and convergence of financial products and channels of distribution, consumer protection and the requisite standards of market conduct may be achieved effectively only through collaborative efforts that involve all participating financial sectors. CAIFA cites the current productive collaboration of the CSA's Financial Planning Committee with CAIFA and trade and educational associations in banking, mutual funds and securities to develop a proficiency standard for financial intermediaries who wish to hold out as financial planners.
- CAIFA regrets that the CSA Distribution Structures Committee, over a two-year period, consulted only with trade and regulatory organizations within the securities sector (identified in the Position Paper under "Committee Deliberations"). The Committee consequently developed positions that will be ineffective where activities fall outside of that sector or overlap with other sectors.

With regard to the last point, I may reiterate here the comments of CAIFA's President and Chief Executive Officer, David Thibaudeau, from CAIFA's response of January 29 to an earlier version of the Position Paper:

"Since an underlying reason for the Concept Paper [as it was then described] is the convergence of the distribution of life insurance and securities through multi-licensed intermediaries, it is regrettable that your committee consulted only with the securities side. I would not expect securities regulators and practitioners to be as knowledgeable about the practice and regulation of life insurance distribution as we are. It is therefore not surprising that your committee has recommended securities solutions where activities are unregulated or are subject to overlapping jurisdiction.

"Had CAIFA been consulted beforehand, I believe that your committee would have created a more balanced document that takes into account the perspective of practitioners on the life side. Looking to the future, I

would like to offer the cooperation of CAIFA, its members and staff to assist the work of your committee."

### **CAIFA's Response**

The remainder of this letter will record more explicitly CAIFA's objections to the main thrusts of the Position Paper insofar as, if implemented, they will impact on financial intermediaries who act as salespersons in the securities sector in the course of providing financial advice and products to their clients from many sectors.

While this letter will refer to "CAIFA's members" for convenience, the comments which follow apply to financial intermediaries generally who provide a spectrum of advice and products that include but are not restricted to securities.

It may be helpful if I first attempt to clarify here some fundamental points of conflict between the standpoints of the CSA Distribution Structures Committee, implicit in its Position Paper, and CAIFA.

**Dealer-centered vs. Agent-centered Regulation.** The securities model of regulation focuses heavily, if not exclusively, on the role of the dealer, who exercises close control over registered salespersons.

By contrast, a life agent is individually licensed and can qualify to operate autonomously, subject to consumer safeguards. Those safeguards include the vicarious liability of life insurance companies represented by the agent, progressive professional development through tiered licensing and mandatory continuous education, and individual professional liability insurance.

There is a long history of life agents forming their own financial services companies. Following recent business trends in life insurance towards greater multi-company representation and economic self-reliance of intermediaries, the autonomy of life agents has increased, as have regulatory requirements and consumer safeguards.

The values of autonomy and self-reliance on the life side extend from life agents as individuals to their history of collective action through institutions. Unlike their counterparts on the securities side, life agents have organized themselves in regional and national professional bodies for a century at least, most notably as CAIFA, and, more recently, have participated in self-regulatory life insurance councils in the western provinces and Quebec.

While the Position Paper concedes that isolated pockets of activity that are now regulated as insurance or banking (or, in Quebec, financial planning) may continue to be so regulated, the Position Paper takes as its underlying premise the belief that financial activity that is not regulated according to principles of

securities regulation presents an inherent risk of harm to the consumer. The Position Paper would therefore extend the mandate of securities regulators to all financial activities not subject to another regulatory regime and resort to the agency of their principal regulatory instrument, the securities dealer, for the purpose.

CAIFA's members, by contrast, consider themselves to be amply regulated, responsible, self-reliant and well-insured. (CAIFA's errors and omissions policy covers advice in mutual funds and financial planning generally and is available to non-members.)

**Relation of CAIFA's Members with Securities Dealers.** Glorianne Stromberg, among others, has observed that today's "consumer investor" (her useful phrase) primarily seeks guidance in his or her financial needs and objectives and regards a transaction in a particular financial product as only the means to implement those objectives.

Life insurance practitioners have long worked within a similar perspective. That is because life insurance inherently concerns long-term financial needs and the identification of future contingencies. In-depth fact finding and needs analysis are second nature to CAIFA's members and far exceed in rigour and depth the securities concept of "know your client" and its emphasis on identifying risk tolerance.

CAIFA does not question the Position Paper when it asserts that a securities dealer is accountable for the conduct of its salespersons, whether employees or agents of the dealer, in providing advice and furthering a trade in securities.

In their relation with a securities dealer, CAIFA's members regard the dealer as the supplier of one form of regulated financial product that they make available to their clients in the course of providing comprehensive financial advice and service. They understand the established regulatory arrangements that apply to dealers and their salespersons. They resist the intrusion of securities dealers into business areas that do not concern securities and regard such intrusion as paternalistic and annoying at best and potentially opportunistic and self-serving.

**"Financial Planning".** The Position Paper holds that "all financial services activities that are not subject to another regulatory regime", when conducted by dual-licensed life agents, must be subject to the supervision and control of the dealer.

As a practical matter, the activities "not subject to another regulatory regime" (outside of Quebec) that are pre-eminently relevant to CAIFA's members are the activities of consultation and advice, including but not limited to financial planning. Since definitive boundaries between financial advice in all its forms

and financial planning have yet to be drawn, this letter will, for convenience, refer generally to financial consultation as "financial planning".

**CAIFA's Objection to Dealer Control Outside of Securities.** In the Position Paper, the principle of dealer control and supervision is pervasive. It extends from financial planning and other undefined and unregulated financial activities *per se* to payment of compensation for those activities, sharing of compensation for those activities, books and records recording those activities, the business vehicle which provides those activities, and trade names and trade marks associated with those activities, among other ancillary matters.

As CAIFA's President, David Thibaudeau, mentioned in his January letter to the CSA Distribution Structures Committee, CAIFA deeply questions the wisdom of assigning to a securities dealer responsibility for activities in financial planning (and the control of related compensation, trade names and other holding out issues) when, for the most part, dealers have shown no discernible evidence of interest, experience or competence in that activity.

The Position Paper, at footnote 17, acknowledges the competence gap in assigning supervisory responsibilities in financial planning to securities dealers and suggests that dealers will obtain whatever expertise they require. CAIFA is skeptical. The duty to supervise should follow competence and experience. A proposal to reverse that relationship is artificial and lacks credibility. Mandatory dealer supervision of financial planning will be intrusive and redundant at best, and potentially incompetent and detrimental to the client.

Dealers and their employees who hold out as financial planners for the purpose of promoting transactions must be subject to rigorous standards of proficiency and market conduct in financial planning. CAIFA submits that the CSA also recognize that it is life agents that have for decades applied principles and methods of in-depth fact finding and long-term and comprehensive financial advice.

When dual-licensed, life agents bring those disciplines to the securities sector, not the reverse. CAIFA cannot accept the proposition that a securities dealer is the exclusive or even the appropriate agent of supervision and control in financial planning or other undefined "financial services not subject to another regulatory regime".

**Future Needs.** The Position Paper fails to address the difficult task of distinguishing between two distinct streams of financial providers: securities dealers and their employees who are extending their activities into unregulated areas such as financial planning, to the possible detriment of their clients, and life agents who have registered as salespersons of a dealer to augment their

advisory role by adding securities to the products that they can provide their clients.

CAIFA regrets that the CSA Distribution Structures Committee, composed solely of securities regulators, failed to appreciate the limitations of their knowledge and experience. When confronted with change in financial services and consumer expectations, the Committee in effect looked into a mirror and adopted a familiar solution in response: If there is any connection between a market participant and a securities dealer, bring everything that is not otherwise regulated under the control of that securities dealer. That response is short-sighted and inadequate.

If present trends continue, traditional lines of demarcation between financial sectors will continue to fade. In CAIFA's view, the proposals in the Position Paper, if implemented, will create an impediment to the effective integrated regulation of retail financial services in future through its one-sided reliance on the securities model.

**Points of Agreement.** The foregoing objections aside, there are fundamental points of agreement between CAIFA and the authors of the Position Paper:

1. **Goal of Uniform Regulation.** CAIFA agrees with the "ultimate objective" stated in the Position Paper under "Long Term Goals":

"The ultimate objective is to achieve uniform levels of investor protection through regulation of financial services, regardless of the regulatory regime through which the services are delivered. For example, uniform levels of regulation of financial planning would be required under both the insurance and securities regulatory regimes."

We would add that the truly ultimate objective is not uniform regulation across separate regimes but rather integrated regulation.

2. **Need for Clear Identity of Financial Providers.** CAIFA agrees that the identity of entities that provide financial products and services to a consumer or investor must be clearly disclosed and confusion as to their identities must be minimized. CAIFA believes that mandatory written disclosure by all financial intermediaries of the entities which the intermediary represents and the products and services which the entities provide, prior to any proposed transaction or delivery of service, can sufficiently mitigate the risk of consumer confusion. CAIFA rejects the position that a dealer must monopolize the delivery of financial services not subject to another regulatory regime in order to prevent consumer confusion as to the identity of the provider.

3. **Need for Clear Accountability of Financial Providers.** CAIFA agrees that not only should entities that provide financial products and services be clearly identified to the consumer or investor, the entities should also be accountable and be known to be accountable to the consumer and investor. The entity can be a financial intermediary or firm of intermediaries, if properly managed and financed in accordance with established norms and backed by mandatory liability insurance. Again, CAIFA rejects the position that only a securities dealer can be held to account to an aggrieved consumer or investor for all financial activities of the dealer's registrants outside of securities (excluding only insurance and banking).
4. **Need to Regulate Financial Planning.** The Position Paper explicitly addresses financial planning under "DISCUSSION AND POSITIONS—Financial Planning Activities by Registrants" (position #5). However, that activity is implicit throughout the paper wherever the phrase "financial services not subject to another regulatory regime" appears. CAIFA fully agrees that financial planning must be subject to common standards of proficiency and consumer redress, that is, regulation. CAIFA applauds the current and productive collaboration of the CSA Financial Planning Committee, CAIFA, the Investment Funds Institute of Canada, the Investment Dealers Association and the Canadian Bankers Association and their respective educational affiliates, with significant input from the Ontario Securities Commission, to develop a proficiency standard for holding out as a financial planner. CAIFA supports and has participated fully in this project. However, the implicit position of the Position Paper is that only one sector of a tripartite field—securities regulators and dealers—is destined to control financial planners and enforce standards in financial planning. That position is wholly at odds with the kind of collaborative process that alone may ensure consensus and effective regulation.
5. **Referral Arrangements and Commission Splitting.** CAIFA agrees with the Position Paper under "Referral Arrangements and Commission Splitting" (position #4) that disclosure must be made to a client setting out the circumstances of an arrangement to pay for a referral or to split commissions and that unauthorized individuals should not receive compensation for acting in furtherance of a trade in securities or for acting as an agent in insurance.

**CAIFA's Regulatory Model for Financial Intermediaries.** CAIFA has developed a regulatory model for financial intermediaries that amplifies the preceding observations. The model appears on CAIFA's Internet website, [WWW.CAIFA.COM](http://WWW.CAIFA.COM). CAIFA has distributed copies of its model to members of the CSA and other financial services regulators in all relevant sectors. CAIFA's

President, David Thibaudeau, has discussed the elements of CAIFA's model with several members of the CSA.

The objective of the model is to safeguard consumer protection and establish high standards of market conduct by financial intermediaries in a staged response to converging financial products and distribution channels. The model encourages regulatory movement from harmonized regulation to integrated regulation, while respecting the various norms of regulation that have evolved in the constituent sectors.

The model adopts dealer centered regulation in securities and preserves the option of responsible autonomy in life and health insurance. The model recommends specific, practical common measures that would apply to all participants: personal disclosure documents, a public database of financial intermediaries, mandatory errors and omissions insurance and tests of proficiency and economic viability, among others.

**CAIFA's Core Response to the Position Paper.** For the reasons stated above, CAIFA recommends that all positions and recommendations in the Position Paper be deleted where they are variants of the principle that "the dealer must be accountable for and control all financial services activities and incidents of carrying on business of its salespersons that are not subject to another regulatory regime".

The dealer's control and accountability should be confined to matters with respect to the securities in which the dealer is authorized to trade. Where salespersons of the dealer are engaged under a contract of employment, that is, as master and servant, the dealer can exercise control and accountability over its employees that extends to financial activities not otherwise regulated.

The relevant challenge to the CSA is to distinguish dealer-salesperson relationships and practices that deliberately or inadvertently frustrate the responsibilities of the dealer with respect to trades in securities and innovative relationships that arise from sectors outside of securities. The Position Paper disregards that distinction when it proposes to reduce all salespersons to the status of *de facto* employees of a dealer.

That position attempts to reverse trends toward integration of financial advice and delivery of financial products. That approach also undermines the rationale for multiple licences in financial services, which proceeds from the premise that an intermediary may hold more than one licence if he or she can maintain proficiency in the licensed disciplines and there is no conflict of interest between the licensed activities.

CAIFA appreciates that the preceding recommendation effectively asks the CSA to reject the core principle of the Position Paper that favours dealer control of financial services. In CAIFA's view, the "ultimate" objective of co-ordinated regulation identified in the Position Paper must be advanced to become a "short term goal" to accommodate existing consumer expectations and market realities. The proper "long term goal" is integrated regulation.

To paraphrase the concluding observation in the Position Paper, "CAIFA believes that its concerns are well founded, and its positions flow from those concerns".

### **Specific Responses**

CAIFA particularly regards the following specific items in the Position Paper, for the most part, as intrusive, unwarranted and unacceptable and therefore must oppose them. CAIFA is, however, able to endorse several measures that are identified below.

The Position Paper as published on the Internet lacks page numbers. This letter will therefore refer only to headings and subheadings in the Position Paper to identify items for comment.

### **"PRINCIPLES FOR DISTRIBUTION OF SECURITIES"**

**"(a) Legal Responsibility"**: CAIFA cannot agree that, as a universal principle, a securities dealer should be accountable "for all financial service activities of its salespersons [such as financial planning] that are not subject to another regulatory regime".

CAIFA can agree with remaining principles (b) to (h).

**"Short Term Goals"**: For reasons stated above, CAIFA must reject all three goals: (a) dealer control of all financial services activities of a salesperson that are not subject to another regulatory regime, (b) dealer liability for the same, and (c) unrestricted access by a dealer and securities regulator to books and records of a salesperson relating to those activities.

**"Long Term Goals"**: CAIFA must vigorously reject (b) dealer liability "for **all** [emphasis added] financial service activities between the dealer's salespersons and its clients".

### **"DISCUSSIONS AND POSITIONS"**

**Position #1 ("Dual Employment")**: CAIFA rejects mandatory dealer responsibility for all the financial services activities of salespersons not subject to another regulatory regime; dealer supervision of the same; dealer control of

revenues from the same; performance of such activities only through the dealer; dealer's prior approval of all financial services not otherwise regulated; disclosure of the dealer's name in all dealings with a client unrelated to securities; and dealer and regulator access to books and records unrelated to securities.

CAIFA recommends full disclosure of the salesperson's business affiliations, including the dealer and products and services offered through the dealer, in a uniform personal disclosure document that would be extended by all financial intermediaries before commencing a business relationship with a client or prospective client.

CAIFA shares concern (f) that "part-time salespersons [at least in their formative years] may not be able to maintain their proficiency at as high a level as is required to ensure the proper performance of their duties".

CAIFA fully endorses the CSA Distribution Structures Committee's support "of continuing education programs for all salespersons to ensure that their level of proficiency and competence is maintained".

**Position #2 ("Securities Sold Under Exemptions"):** Without specifically endorsing or rejecting the position, CAIFA questions a position that would allow a plasterer or hairdresser to sell an exempt security or an instrument which is deemed not to be a security while precluding salespersons who are registered with securities regulators, although restricted, from selling the same product. If the fault lies in too broad exemptions or exclusions from regulation under the Securities Act of a province or territory, the proper remedy should be to amend the statute.

**Position #3 ("Trade Names"):** These positions are particularly offensive: (a) business names and trade marks of CAIFA's members or other dual-licensed salespersons to be registered to a dealer; (b) dealer to give prior approval to such names and marks; (c) securities regulators to give prior approval for use of such names and marks; (d) use of trade name to be restricted to a single dealer; and (e) requirement that clients of a financial intermediary to enter into "all written agreements" in the dealer's name.

All the foregoing could constitute expropriation by the dealer of the intellectual property and goodwill of the business of a financial advisor. Any intended consumer benefit could be achieved just as effectively by mandatory disclosure of personal business affiliations and related product lines.

**Position #4 ("Referral Arrangements and Commission Splitting"):** CAIFA is pleased to see that the restriction that requires otherwise permitted payments to

be made only between a dealer and "acceptable entity" will be acceptable where the "acceptable entity" includes a duly licensed insurance agent.

CAIFA endorses the requirement that intermediaries disclose beforehand in writing to a client that they will pay a referral fee to, or share compensation with, another qualified intermediary.

**Position #5 ("Financial Planning Activities by Registrants"):** The Position Paper should stop after the second preliminary paragraph, which acknowledges "the work that is being done in this area by the [CSA] committee on the regulation of financial planning".

CAIFA observes that, with the assistance and consensus of a multi-sectoral working group of industry associations in life insurance, banking, mutual funds and securities, the CSA Financial Planning Committee has developed a proficiency rule that is limited to setting qualifications to hold out as a financial planner. The role of the dealer should be limited to confirming a salesperson's compliance with that rule, without presuming to supervise as a matter of regulation the salesperson's activities in financial planning.

CAIFA must oppose the position that "Salespersons who provide financial planning services must provide those services through the dealer that sponsors their securities registrations". CAIFA must further oppose proposal (d), that all fees earned from financial planning activities of the salesperson are to be paid to the dealer, and proposal (e), that the dealer must supervise the financial planning activities of the salesperson. Those positions are clearly objectionable, for the reasons set out earlier. The remaining recommendations are acceptable.

**Position #7 ("Dealer as Principal and Salesperson as Agent"):** Again, proposals (a) and (d), that a dealer must supervise all financial activities of all salespersons that are not subject to another regulatory regime and have unrestricted access to the books and records of the salesperson relating to those activities, are unacceptable.

CAIFA can endorse the established principle in (b) that a salesperson, in advising in securities or acting in furtherance of a trade in securities, is the agent of the dealer and that the liability of a dealer to clients for acts of the salesperson **with reference to securities** is the same as that which would apply in an employer and employee relationship.

**Position #9 ("Incorporation Without Registration"):** CAIFA vigorously rejects the proposition that dual-licensed intermediaries "will not be allowed to incorporate in order to conduct ... financial services activities that are not otherwise regulated". That proposal far exceeds the mandate of the Securities Acts.

**Position #11 ("Proposed Business Structures"—"(c) The introducing and carrying dealer model"):** The proposed dealer categories and relationships, in which a relatively lightly regulated "introducing dealer", with limited business powers, would place business through a more heavily regulated and capitalized "carrying dealer" may be of interest to some of CAIFA's members.

That could be the case where the intermediary wishes to hold out in his or her own business name (in conjunction with the name of the carrying dealer), has no interest in accepting client funds for his or her own account, is able to establish a satisfactory business arrangement with an acceptable dealer and is required to deposit an affordable sum of regulatory capital with the carrying dealer.

Where an intermediary is dual-licensed, to avoid an unreasonable and wasteful duplication of corporate structures, an incorporated insurance agency should be able to be registered as an introducing dealer.

### **Looking Ahead**

CAIFA and the CSA share similar objectives for consumer and investor welfare. Clearly, CAIFA and the CSA Distribution Structures Committee have different views on how to achieve those objectives. However, CAIFA's recent experience in working with the Ontario Securities Commission and the CSA Financial Planning Committee leads CAIFA to have every confidence that there is abundant good will within CAIFA and the securities regulators to work toward a satisfactory resolution of the differences identified in the Position Paper and this letter. The prerequisite is dialogue and consultation.

CAIFA continues to extend its offer to collaborate wherever possible in the work of the CSA, its committees and its constituent securities regulators.

Yours very truly,

Robert A. Cowan, CFP, CLU, CH.F.C.

Copies: All members of the CSA  
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