



THE INVESTMENT
FUNDS INSTITUTE
OF CANADA

L'INSTITUT DES FONDS
D'INVESTISSEMENT
DU CANADA

IFIC Submission

Re: *CSA Staff Notice and Request
for Comment 25-304 Application for
Recognition of New Self-Regulatory
Organization*

June 27, 2022





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Delivered By Email: consultation-en-cours@lautorite.qc.ca, comments@osc.gov.on.ca

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Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission of New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
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Dear Sirs and Mesdames:

RE: CSA Staff Notice and Request for Comment 25-304 *Application for Recognition of New Self-Regulatory Organization*

The Investment Funds Institute of Canada (IFIC) appreciates the opportunity to comment on CSA Staff Notice and Request for Comment 25-304 *Application for Recognition of New Self-Regulatory Organization* (the New SRO Consultation).

IFIC is the voice of Canada's investment funds industry. IFIC brings together approximately 150 organizations, including fund managers, distributors and industry service organizations to foster a strong, stable investment sector where investors can realize their financial goals. IFIC operates on a governance framework that gathers member input through working committees. The recommendations of the working committees are submitted to the IFIC Board or board-level committees for direction and approval. This process results in a submission that reflects the input and direction of a broad range of IFIC members.

IFIC appreciates the expeditious, hard work that the Canadian Securities Administrators (CSA), the Investment Industry Regulatory Organization of Canada (IIROC) and the Mutual Fund Dealers Association of Canada (MFDA) (MFDA and IIROC, together the SROs) have devoted to developing the framework for the new self-regulatory organization (New SRO) set out in the New SRO Consultation. Consolidating IIROC and the MFDA into the New SRO is an important and very worthwhile undertaking that will be advantageous to investors, the industry, securities regulators and other stakeholders.

We believe that the New SRO framework should continue to ensure Canadian investors access to meaningful investment advice and services, and enable dealers to provide a broad range of service offerings.

Summary

IFIC is pleased to provide the following comments in connection with the New SRO Consultation. Our feedback is focused on the following key points:

- individuals offering the same products and services to investors should have the same proficiency requirements, regardless of their firms' registration category - specifically, the existing proficiency requirements for MFDA mutual fund dealer representatives should apply to mutual fund only representatives of mutual fund dealers and dual-registered dealers under the New SRO rules;
- the New SRO Investment Dealer and Partially Consolidated Rules should be amended to allow, within jurisdictions that permit commission direction, directed commissions by registered representatives dealing in mutual funds only;
- current references in firms' documents to IIROC, MFDA, CIPF and MFDA IPC should remain as is, pending finalization of both the names of the New SRO and new investor protection fund (New IPF);
- the new account documentation requirements within the interim rules should be clarified; and
- the circumstances in which the New SRO Mutual Fund Dealer Rules apply to dual-registered dealers should be clarified.

Proficiency Requirements

The New SRO draft interim rules (Draft Interim Rules) have been proposed with a view to the New SRO achieving a successful launch and the CSA achieving its major policy objectives for the SROs, including facilitating conducting mutual fund dealer business and investment dealer business within the same legal entity. More specifically, the New Draft SRO Rules – Frequently Asked Questions (FAQ) provides that “*to ensure minimum disruption to members and their employees and Approved Persons each set of IIROC and MFDA rules will be adopted by the New SRO and will continue to apply with some key rules changes proposed in the interim to address structural impediments to the industry [emphasis added]*”. As explained below, IFIC does not consider proficiency requirements to be a key structural impediment that necessitates an interim change to the proficiency status quo for those individuals who are/will be registered in the category of dealing representative, mutual fund dealer within dual-registered firms.

The FAQ also provides that at a mutual fund dealer, individuals registered as “dealing representative, mutual fund dealer” will not need to complete the Conduct Practices Handbook Course (CPH) or any other new proficiency requirements under the Draft Interim Rules. In contrast, “mutual funds only” dealing representatives at a dual-registered dealer must complete the CPH, a new proficiency requirement, within 270 days of the firm becoming a dual-registered firm (unless the representative previously completed the CPH).

It is IFIC's view that individuals offering the same products and services, regardless of the technical category of their firm's registration, should be required to complete the same proficiency requirements. In other words, the substance of the products and services offered by the representative should govern the proficiency requirements, not the form of their firm's registration. Accordingly, IFIC believes that it is inappropriate to require an individual registered in the category of dealing representative, mutual fund dealer within a dual-registered firm to complete the CPH, absent a compelling policy rationale. IFIC is not aware of any such rationale. The existing proficiency requirements for MFDA mutual fund dealer representatives should apply to mutual fund only representatives of mutual fund dealers and dual-registered dealers under the New SRO rules.

Moreover, it would be very expensive for dual-registered firms to fund significant numbers of representatives taking the CPH. For large firms, the 270-day limit is inadequate time for all of their representatives to complete the CPH. Unjustified differences in proficiency requirements should not serve as an incentive for individuals to move from dual-registered firms to mutual fund dealers (regulatory arbitrage).

Most importantly, IFIC considers this proficiency proposal to be a major impediment to MFDA member firms becoming dual-registered firms. This impediment could prohibit the successful launch of the New SRO and result in certain major regulatory objectives failing to be met, including (i) eliminating the need for clients to move accounts to IIROC member firms from MFDA member firms to obtain different types of products and services (ii) permitting clients' advisors the flexibility to transition with their clients to facilitate holistic, one-stop-shopping business models for the benefit of investors, (iii) reducing duplication and investors' administrative difficulties and confusion when acquiring new products and services, (iv) reducing regulatory complexity, (v) facilitating the successful implementation and operation of dual registered firms, and (vi) enhancing confidence in securities regulation.

The CPH is designed for IIROC Approved Persons and not those registered in the category of dealing representative, mutual fund dealer within a dual-registered firm. IFSE's Canadian Investment Funds Course is well fit for purpose for a dealing representative, mutual fund dealer within a dual-registered firm. That course addresses registrants' ethical responsibilities, conflicts of interest, the Canadian regulatory bodies, legislation and regulations, compliance, know your client, suitability, know your product and registration requirements and dealing with vulnerable and older investors, which has served mutual fund investors and registrants well.

If necessary, as an alternative to the CPH, a new course specifically tailored to those registered in the category of dealing representative, mutual fund dealer, within dual platform firms could be developed and eligible for continuing education credits. Any additional proficiency requirement should allow one year for completion commencing from the time the firm becomes a dual-registered firm.

Directed Commissions

The FAQ provides that an individual registered as a dealing representative, mutual fund dealer will continue to be allowed to direct commissions within jurisdictions that permit commission direction and in accordance with Mutual Fund Dealer Rule 2.4.1(b). The FAQ addresses whether an individual that becomes affiliated with a dual-registered firm and transitions into the category of registered representative dealing in mutual funds only, may start or continue to direct commissions. The New SRO Mutual Fund Dealer Rules only apply to a dual-registered firm *where there is no corresponding requirement in the New SRO Investment Dealer and Partially Consolidated Rules* [emphasis added]. Mutual Fund Dealer Rule 2.4.1(b) does not impose a "requirement". It is permissive in nature. Hence, the New SRO Investment Dealer and Partially Consolidated Rules should be amended to allow directed commissions, by registered representative dealing in mutual funds only, within jurisdictions that permit commission direction. If this amendment is not made and registered representatives dealing in mutual funds only can not direct commissions within jurisdictions that permit commission direction, IFIC would consider this outcome to be a major impediment to MFDA member firms becoming dual-registered firms. This outcome would be inconsistent with the policy rationales supporting dual-registration (see "Proficiency Requirements" above).

IFIC appreciates the opportunity to have met with the CSA Directed Commissions Working Group and looks forward to continuing to work with it to harmonize directed commissions in the short and long term, potentially by adopting an incorporated salesperson regime as a long-term solution.

Documentation

References to IIROC, MFDA, the Canadian Investor Protection Fund (CIPF) and MFDA Investor Protection Corporation (MFDA IPC) appear in a very large number of documents within many investment dealers and mutual fund dealers and a large number of documents across all investment dealers and mutual fund dealers. It would be unduly complex and expensive for dealers to change references to these organizations to the names of the New SRO and New IPF as each new name is finalized i.e. potentially, more than once. A series of name change references would be unduly expensive and time consuming and create operational, regulatory and client-experience risk for dealers, while being confusing to clients. These outcomes would not be in keeping with the regulatory objectives of simplifying regulation and enhancing investor confidence in securities regulation. Accordingly, IFIC recommends that a mechanism be put in place to permit current references in documents to IIROC, MFDA, CIPF and MFDA IPC to remain as is, pending finalization of both the names of the New SRO and New IPF, after which a reasonable transition

period, such as 18 months, would permit documentation amendments to reflect these new names. For example, a new rule could explicitly permit registrants to continue to use such names in their documents and deem and interpret such references to be to the New SRO and New IPF, as applicable, pending finalization of both names of the New SRO and New IPF, after which a transition period of 18 months would apply for a registrant to amend its documents accordingly. As a related matter, rules pertaining to the required use of SRO logos should be amended, as necessary, to coincide with the use of the names of the New SRO and New IPF.

The FAQ provides that exemptive relief from “*the new account documentation requirements within the interim rules*” [emphasis added] will be generally available where the products and services to be offered to the client and the know your client information and assessment process at the dual-registered firm are materially the same as at the mutual fund dealer affiliate.

Where the existing mutual fund dealer account agreement has an acceptable assignment clause and the products and services to be offered and the know your client information and assessment processes are materially the same, the dual-registered firm may be exempted from the “*requirement to execute the normal account agreements and documentation*” [emphasis added].

In other circumstances, dual-registered firms will not be exempted from the “*requirement to execute the normal new account agreements and documentation*” [emphasis added] but may be given more time to do so.

Given the phraseology relating to documentation differs between scenarios - “new account documentation requirements within the interim rules”, “normal account agreements and documentation” and “normal new account agreements and documentation” – it would be helpful for a revised FAQ to specifically address each of account agreements and their related schedules, know your client documentation, relationship disclosure documentation and conflicts of interest statements, which we assume are all contemplated by the above document-related phrases.

Rules That Apply to Dual-registered Firms and Their Employees and Approved Persons

The FAQ provides that dual-registered firms and their employees and Approved Persons will be required to comply with (i) the New SRO Investment Dealer and Partially Consolidated Rules, and (ii) the New SRO Mutual Fund Dealer Rules, where there is *no corresponding requirement* [emphasis added] in the New SRO Investment Dealer and Partially Consolidated Rules. The phrase “no corresponding requirement” could be interpreted to mean no corresponding requirement whatsoever dealing with the same subject matter or a substantively different requirement pertaining to the same subject matter. It is very important that this ambiguity be clarified in an amended FAQ or otherwise.

New SRO Fees

IFIC understands that the development of the New SRO’s fee model will be a complex exercise that will require expert professional advice and consultation with members and other stakeholders through a public comment process.

IFIC endorses the enumerated principles to be applied in the fee model adopted by the New SRO.

IFIC also supports the New SRO, on an interim basis, utilizing the existing fee structures and models of IIROC (with respect to current IIROC Members) and the MFDA (with respect to current MFDA Members), but questions what “necessary modifications” are contemplated.

New Rule Development

The New SRO should clearly identify a material regulatory objective when developing new rules. A clear material regulatory objective that describes the issue to be solved should be articulated at an early stage;

this would focus the New SRO, the industry and other stakeholders on the need to implement a solution to the specific issue.

IFIC favours a proportionate regulatory approach based on the scale, extent, complexity and risk of the particular issue in order to achieve an optimal outcome. A significant element of determining proportionality should include a pre- and post-implementation cost/benefit and impact analysis for significant rule proposals. Meaningful consultation and input from all types of registrants, including smaller and independent firms, should be sought to develop risk-based regulation, which is also proportionate to different types and sizes of registrants and business models.

The industry should be provided with a meaningful comment period on proposed New SRO rules. The New SRO should ensure that the industry will have a sufficient implementation transition period for each new rule which, if necessary, is phased/staggered.

IFIC favours plain language rules that articulate a clear regulatory outcome. These rules can be both principles based and prescriptive, as appropriate. For example, business conduct rules lend themselves to a more flexible approach due to the variety of different business models and fact scenarios, however, a more detailed approach is appropriate for financial compliance standards.

IFIC believes that adherence to the foregoing principles would reduce the costs of rule development, implementation and ongoing regulatory oversight, while achieving appropriate regulatory outcomes and compliance. Given that dealers have recently implemented substantive rule changes, including the Client Focused Reforms and rules dealing with vulnerable clients, and continuous education, the New SRO should ensure that the new consolidated rules are substantially harmonized with these newly implemented requirements.

IFIC notes that the MFDA and IIROC continue to issue rule proposals, and we welcome ongoing rule amendments that help address industry concerns/investor protection. That said, as dealers require various project, technology, and advisor training resources in order to implement multiple substantive rule changes, we urge that there be a coordination between the regulators (MFDA/IIROC/New SRO) on the ongoing rule changes to ensure that the resulting applicable New SRO rules are harmonized.

New Draft SRO Rules – Frequently Asked Questions

IFIC appreciates the SROs' publication of the FAQ, which anticipates and answers many questions in connection with the New SRO. IFIC recommends that the FAQ be updated and re-published from time to time to address any New SRO rule issues that arise. IFIC suggests that ongoing consultation with industry, perhaps through the CSA Implementation Working Group, should occur to address matters to be covered by updated and re-republished FAQs. A similar approach was adopted by the CSA in connection with implementing the Client Focus Reforms and this was well received and helpful to both the industry and securities regulators.

Oversight of the New SRO

The Memorandum of Understanding among CSA members regarding oversight of the New SRO outlines the oversight program that the CSA members will implement to oversee the New SRO's performance of its functions. The CSA members will establish an oversight committee as a forum for the discussion of issues, concerns and proposals related to the oversight of the New SRO. Two CSA members will be initially designated as coordinators (Coordinators). Coordinators will be tasked with the roles of coordinating, communicating and scheduling activities of the oversight program among all CSA members, and between the CSA members and the New SRO.

Each Coordinator will serve for four years on a staggered rotation basis, except that one of the first two Coordinators will be replaced after two years to facilitate the staggered rotation. The overall result will be one new Coordinator being designated for a four-year term every two years. IFIC respectfully asks that each Coordinator be qualified and that the Coordinators provide clear, harmonized direction when carrying out their roles.

The “Self” in Self-Regulation

As set out in our previous submissions, IFIC strongly supports the value of keeping the “self” in self-regulation. IFIC does not agree with the CSA’s revised governance and oversight approaches that curtail members’ voices – particularly in the matters over which the CSA will have a veto, including business plans and exemptions from the New SRO rules. In addition, the role of current IIROC District Councils is proposed to be changed to an advisory role to provide regional perspectives on national matters. This would also result in a substantial diminution of the industry’s self-regulatory role because it would remove the powers of these councils to, among other things, approve New SRO members and members’ acquisitions of dealers, impose terms and conditions on Approved Persons, suspend or revoke approval of Approved Persons, and grant proficiency exemptions.

Overall, while we agree with many of the governance proposals to strengthen accountability, we believe that the foregoing reductions of self-regulatory authority do not achieve the right proportion of industry self-regulatory authority.

The FAQ provides that the Regional Councils will have an advisory role and make policy recommendations to staff of the New SRO and that the National Council will act as a forum for cooperation and consultation among the Regional Councils and provide recommendations on policy matters. It is unclear whether both the Regional Councils and National Council will make recommendations to the CSA on the same topics and, if so, where there is a conflict, whether the National Council’s policy recommendations will over-ride those of the Regional Councils. It is important that this ambiguity be clarified in an amended FAQ or otherwise.

Regional Councils and the National Council should have diverse memberships that collectively reflect firms of different sizes, which are integrated and independent, operate in different regions, and have different business models. All dealer distribution channels should be represented, including order execution only dealers, full-service dealers (offering brokerage and/or managed accounts) and mutual fund dealers.

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IFIC appreciates this opportunity to provide our input to the CSA on this important initiative. Please feel free to contact me by email at pbourque@ific.ca or by phone at 416-309-2300. I would be pleased to provide further information or answer any questions you may have.

Yours sincerely,

THE INVESTMENT FUNDS INSTITUTE OF CANADA



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