BCV Asset Management Inc.

October 19, 2018

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

comments@osc.gov.on.ca and consultation-en-cours@lautorite.qc.ca

Re: Canadian Securities Administrators Notice and Request for Comment: Proposed Amendments to National Instrument 31-103 – *Registration Requirements, Exemptions and Ongoing Registrant Obligations.* Reforms to Enhance the Client-Registrant Relationship

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The purpose of this letter is to provide commentary from BCV Asset Management Inc. to the Canadian Securities Administrators ("CSA") based on the CSA Notice and Request for Comment and Proposed Amendments to National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* and to Companion Policy 31-103CP *Registration Requirements, Exemptions and Ongoing Registrant Obligations* on Reforms to Enhance the Client-Registrant Relationship ("Client Focused Reforms") dated June 21, 2018.

BCV Asset Management Inc. ("BCV") is a Portfolio Manager located in Winnipeg, Manitoba. BCV was founded in 2007 and is an independent company wholly owned by its employees and key business partners. These owners include a team of well-mentored, experienced investment professionals, supported in the day-to-day operations by a team with extensive experience in the financial services industry. The ownership group is complemented by a number of external individuals who have considerable experience in the financial planning, legal, banking and information technology fields.

BCV is registered as a Portfolio Manager in British Columbia, Alberta, Saskatchewan, Manitoba, Ontario and Prince Edward Island. BCV's principal regulator is the Manitoba Securities Commission ("MSC").

BCV is a portfolio management firm dedicated to building and protecting client wealth, seeking to maximize long-term returns while minimizing risk. We offer an alternative to mass-market investment products, creating customized investment portfolios within Separately Managed Accounts. We provide a high level of personalized and professional service and ensure that clients have a direct relationship with the Portfolio Manager entrusted with managing their wealth. We are able to provide this discretionary portfolio management service to investors whose household meets our minimum investible asset threshold and are seeking alternatives to mutual funds or brokerage wrap accounts. BCV's current AUM is $1.6 billion with a large percentage of this being a result of client referrals from third party financial planners, both registered and unregistered.

While there are significant changes proposed to National Instrument 31-103 that will affect not only our business at BCV, but also that of our fellow portfolio managers; our primary concern and focus of this commentary letter surrounds the topic of "Referral Arrangements" under section 13.7 and 13.8.1 of the Instrument as it relates to Conflicts of Interest.

Our concerns with the proposed changes surrounding Referral Arrangements are as follows:

1. The misunderstanding in the definition of a "Referral Arrangement";
2. The broad definition of a "Referral Arrangement";
3. The prescriptive nature and limitations in the payment of Referral Fees under a "Referral Arrangement";
4. The unintended consequence of creating a very material Conflict of Interest while trying to reduce Conflict of Interest; and
5. The prohibition in paying referral fees to non-registrants.

The first area of concern is what appears to be a misunderstanding or mis-definition of the term "Referral Arrangement". Through industry discussions and a meeting with the MSC on July 18, 2018, the term "Referral Arrangement" was defined as a relationship between a Referral Party and a Portfolio Management firm whereby the Referral Party refers a client to the Portfolio Management firm and then has no further involvement with the client or Portfolio Management firm other than the collection of a referral fee. While this may be the case for some firms, the reality is that our referral arrangements (likewise with other Portfolio Management firms that we compete with) have an ongoing relationship and understanding of activities that are performed as we co-service the client with the Referral Party. In essence, our "Referral Arrangements" are more of a shared service arrangement than that of a pure referral-based arrangement where there is a hand-off and the end of the involvement of the referring party with the client. For example, the Referral Parties who we have relationships with and contracted "Referral Arrangements" typically perform estate, wealth, and tax planning for the referred client while BCV creates and manages the client investment portfolio based on the information obtained in our Know Your Client ("KYC") documentation, suitability assessment and resulting Investment Policy Statement ("IPS") signed by the client. There is a distinct delineation of duties in the arrangement whereby BCV performs all of the registerable activities as a registrant, while the Referring Party performs other planning activities (typically non-registerable activities – which is dependent upon whether the Referring Party is a registrant or not). In this relationship, the Referring Party receives a fixed percentage of the Management Fee that is collected by BCV out of the client accounts and paid to the Referral Party either directly or through their sponsoring entity for their portion of the work completed in servicing the client(s). However, while our "Referral Arrangements" are more "Shared Services Arrangements", the broad definition of a "Referral Arrangement" may still put BCV offside with respect to NI 31-103, which will be discussed in the next paragraph. Further to this point, given our business model and commercial relationship with our advisors, it is hard to understand how a conflict of interest exists given each parties role in servicing the client, other than the payment of fees in consideration of the referral, which is fully disclosed to the client, in advance. We view this shared service relationship between Referring Party and Portfolio Manager as one of mutual benefit to the client.

The second point of concern to highlight is the broad definition of "Referral Arrangement" as it currently stands. Effectively, this definition includes any sharing or splitting of commissions collected from the client by the party who received the referral. Therefore, even if the contracted relationship (as outlined in the paragraph above) is to the benefit of the client; the CSA may still view this relationship as a "Referral Arrangement" and BCV would be offside in accordance with the instrument. Without a more concise or specific definition, a "Referral Arrangement" could be subject to interpretation. This subjectivity by local, provincial regulators may result in inconsistencies in the application of the instrument, leading to further confusion by registrants. Furthermore, with the broad definition, it is not possible for registrants to structure their contracted relationships in a manner that would or could conform to the new proposed changes. Effectively, any shared service arrangement will be considered a "Referral Arrangement" leading to the restrictive payment requirements being put into place.

The third point of concern is the limitation of the amount and duration of the referral payment. The duration limit of 36-months and maximum of 25% of the total commissions collected from clients appears arbitrary even given the explanation received in the Companion Policy. It does not seem appropriate to put the 36-month and 25% limitations for payment to a Referring Party if that Referring Party is conducting regular and ongoing services to the end client. If a Referring Party is providing a client with an annual wealth management plan, would it make sense to stop paying that individual or capping the "value" they are providing to the client strictly on the broad definition of the arrangement? The prescriptive nature of these limitations as written effectively instructs registrants on how to conduct their business. It is our experience that regulators are not particularly fond in telling firms how to do their business (or impose commercial terms), but rather ensure that the business operations of the regulated firms fall within the parameters set out by the National Instruments and local regulations. Should a true referral arrangement exist, whereby a Referring Party simply refers a client and has no further involvement with the client, then we fully understand and accept the limitations of 36-months and maximum of 25%; however, without the proper definition of the "Referral Arrangement", shared service arrangements will be increasingly difficult to manage or maintain.

Should the CSA keep the amendment written as is, this will have a fundamental shift in the mindset of the asset management and investment industry. This is the basis for our fourth concern, which is the creation of a conflict of interest by the regulators between investment products. Because a commercial relationship will no longer be permissible, referring parties will direct clients to investment products that will secure a revenue stream which has been a constant for the referring party as it relates to any particular client.

The obvious example are products that pay a trailing commission (given these products are permitted to pay the commission in perpetuity). This will create a shift towards mutual fund products or other investment fund products that may not meet suitability standards and also create a conflict of interest amongst regulated firms and individuals by favoring a specific type of product over another (ie: having a client shift to a portfolio of Mutual Funds or Segregated Funds rather than a portfolio of individual securities held in a separately managed account that provided growth, value, and income opportunities). Furthermore, clients will generally experience higher management fees associated with these products as compared to other options such as a separately managed account with a Portfolio Management firm. While we believe that this conflict of interest created in favoring one registrant and their products over another (ie: MFDA firms and Mutual Funds, IIROC and fee-based or commission-based accounts as opposed to Portfolio Management firms and individual securities) is not intentional by the CSA, it will strongly benefit one group of registrants while being extremely damaging to others. Especially for those firms for which "Referral Arrangements" make a significant proportion of their business. In fact, since June 21, 2018; our referral-based business (for which the Referring Party also provides planning services) have effectively ceased due to the uncertainty and obscurity of these proposed amendments to NI 31-103. We and other firms have had to go on "damage control" to explain the process of the CSA's proposed changes, commentary periods, subsequent rulings, enactment, and transition periods to ensure that existing business and clients are not being moved out of BCV's management and into alternative products such as Mutual Funds. This announcement has effectively

"rattled" (for the better use of a term) Referring Parties, both regulated and non-regulated, into trying to find "safe" alternatives to preserve their own livelihoods. This will occur, and cases will be made by registrants and non-registrants to demonstrate that these products are better or more well suited for the client even though this may not be the case in reality. This is a very serious issue that the CSA has created, and we urge the CSA to take this proposal off of the table immediately in order to remedy the current effective freezing of referrals from registrant firms, which is harming Canadian investors.

The final point of concern is the prohibition of the payment of referral fees to non-registrants. While we understand that it is the view of the regulators that all client activity should be provided by a registered individual to ensure the consistent delivery of service and so that proficiency and oversight amongst registered individuals is maintained, there are individuals who are non-registered and provide considerable value to clients. Under our current structure with referring parties who are non-registered individuals, we outline that all registerable activities are to be performed by BCV and BCV only. All other non-registerable activities are able to be performed by the Referring Party. Regular communication between BCV and its Referring Parties occurs to reinforce this understanding. This arrangement is mutually beneficial to BCV, the Referring Party, and the client(s). BCV is registered as a Portfolio Manager and has expertise in the construction of investment portfolios, but does not have the capacity to perform estate, wealth, and tax planning for clients. The referring parties are not registered and do not have the expertise to construct investment portfolios but do have the capacity and expertise to provide estate, wealth, and tax planning for clients. The client benefits by having both parties excel in their areas of expertise while working harmoniously together and sharing in the fully transparent management fee revenues. If all referring parties are required to become registered, their options are to become a registrant as an Associate Advising Representative under a Portfolio Management firm (which has educational and experiential requirements, most of which will not have when these new amendments may be enacted), or seek sponsorship through an EMD, IIROC or MFDA firm. Given the significant differences in underlying requirements for registration amongst these various bodies, the Portfolio Manager route is likely the least attractive with gravitation towards EMD, IIROC, or MFDA firms. Again, this creates favoritism towards these firms and damages the Portfolio Management space. It also increases the power of dealer firms to restrict competition as we've seen with some former IIROC and MFDA registered firms who have narrowed their shelves to benefit higher profit, in-house products. Clients suffer in the restrictive nature of Mutual Funds in which their accounts will likely be invested and paying increased management fees where it would be more appropriate to explore a separately managed account given the size of the client's investment portfolio. Again, this is creating the conflict of interest towards specific registrants which goes against the objectives of NI 31-103, as outlined above.

Another point that we would like to highlight is that in the Client Focused Reforms, there is a word that is virtually nowhere to be seen; that is the "fiduciary duty". It appears that the CSA has shied away from focusing on different duties of care owed by various registrants but rather determined that every registrant under NI 31-103 should be subject to a sweeping set of Client Focused Reforms. Aside from a small mention in the Companion Policy to NI 31-103, the CSA does not acknowledge the fiduciary responsibility of Portfolio Managers at all in the Client Focused Reforms, but rather that "the amendments are designed to work together throughout the client-registrant relationship as an extension of the duty of registrants to deal fairly, honestly and in good faith with their clients". We believe that ignoring the continued existence and importance of the fiduciary duty does a disservice to the Canadian asset management industry and obscures for investors an important distinction in categories of registrants and of investor choice.

We pride ourselves in our fiduciary duty that we have to our clients as Portfolio Managers. We also believe that this sets us apart from the other registrant categories while providing clients with that additional layer of comfort that we are making decisions that have their, the client's, best interest in mind…always. In the broader industry sense, this is a competitive advantage we highlight in our marketing materials.

After outlining our concerns that we've highlighted above, let's consider how these relate to the 5 investor protection concerns as outlined in Annex E of the Client Focused Reforms.

The first investor protection concern is that "clients are not getting the value or returns they could reasonably expect from investing". First and foremost, the "reasonable expectation" is highly subjective and will vary from client to client and will ultimately depend on risk tolerance of the client as determined by the KYC and governed by the IPS in the selection of investment products to match risk tolerance and the fees they are paying. "Reasonable" to an uneducated investor is likely much different than that defined by an educated investor. Having our existing "Referral Arrangement" in place satisfies this concern in the fact that the referring party and BCV have the ability to have touch points and meetings with the client to manage their expectations with respect to value and performance of their investment accounts versus relevant benchmarks. BCV and our referring parties have constant communication through one-on-one conversations and market bulletins authored and sent by BCV to educate clients and manage performance expectations. And it is of course noted in the Client Focused Reforms that portfolio managers will have an ongoing annual suitability assessment obligation, which is the highest standard of ongoing client interaction, versus the per transaction standard for the balance of the industry.

The second investor protection concern is that there is an "expectations gap" between the client and the registrant, mainly surrounding the use of titles that may be misleading and the lack of variety or the use of proprietary products. With respect to the use of titles, we don't believe that this is an area of concern for Portfolio Management firms. First and foremost, an individual cannot be given the title of Portfolio Manager unless registered as an "Advising Representative" of a registered Portfolio Management firm without being able to prove proficiency through strict education and meeting relevant investment management experience requirements. The majority of Portfolio Managers hold the CFA (Chartered Financial Analyst) designation, which is World recognized as the pinnacle of proficiency in the investment industry. Second, clients are made aware of the type of service that are offered based on their risk tolerance. BCV's service is separately managed accounts whereby clients follow a strategy of owning blue chip, large cap companies that pay a dividend. The simplistic nature of the strategy which can be easily understood through past performance allows for clients to understand their investment portfolios. We feel that there is limited "expectation gap" in the current process of our business with our "Referral Arrangements".

Third, there is concern regarding "conflict of interest" in the sense that disclosure may be ineffective, and that the disclosure may further increase reliance on the advice that is or potentially conflicted. Due to the nature of our business and the services that are offered, there is a conflict of interest that comes into play for BCV in that a referring party receives compensation and where a referring party is also a shareholder of the company. In this situation, the referring party is not only compensated for the performance of their wealth planning role, but also through dividends and potential share price appreciation on BCV shares. In situation where this conflict is present, disclosure is made to the client outlining the conflict of interest that exists and how that conflict is managed. Given the nature of Portfolio Management firms and the products that are typically offered, the conflict of interest concern is reduced below that of an IIROC or MFDA firm.

The fourth investor protection concern surrounds that of "information asymmetry" and that the financial literacy of clients does not align with the underlying best interest of the client with respect to the advice or financial information they are receiving from registrants. As part of our KYC process, we as a registered Portfolio Management firm, solicit information from the client on their understanding of various investment products (ie: securities, bonds/fixed income, mutual funds, etc.). Based on this information, Portfolio Management firms customize the communication to clients to help clients understand the investment products that will make up their investment portfolios. Furthermore, while there is some onus on the client for their own financial literacy, the professional relationship between the Referring Party and BCV allows for the client to have increased resources in enhancing their own financial literacy. Our obligation as fiduciaries demands

that we have the best interest of clients first and foremost. We feel that there is a strong information symmetry given our roles as fiduciaries to act and inform in the best interest of the client.

The fifth and last concern identified by the CSA is that "clients are not getting the outcomes that the regulatory system is designed to give them". Portfolio Management firms are regulated to the highest standard of all registrants in the investment management industry due to our fiduciary duty owed to clients and discretionary management authority granted over separately managed accounts. We work to continuously enhance our regulatory compliance and communicate our compliance requirements to clients when appropriate. Categorizing Portfolio Management firms within the same group as SRO's, etc. may not be the best comparison for regulatory oversight and determination of client expected outcomes of that system. Furthermore, while the statistics that have been highlighted towards IIROC and MFDA with respect to percentage of securities owners, one should also note that within each IIROC or MFDA firm would be Portfolio Managers (who would be registered as such) overseeing the investable assets, or portfolio managers that are managing the monies through mutual funds. As a result, we respectfully submit that to say that Portfolio Management firms only account for 10% of overall security management is misleading in itself. We believe that Portfolio Management firms are the most appropriately aligned with investor expectations on outcomes that the regulatory system is designed to provide to them.

Overall, we at BCV are of the very strong opinion that our clients benefit from the current structure through which we conduct our business, which involves the use of "Referral Arrangements" (which should be viewed as shared service arrangements rather than simply a referral as there are additional and ongoing services provided to end clients) and the payment of a portion of the overall management fee to both registrants and non-registrants. We believe that the overall duty of care that a client receives through our fiduciary responsibilities as registered Portfolio Managers greatly outweighs that of SRO's such as IIROC, MFDA and EMD firms. We are able to provide clients with lower management fees than what are typically charged of mutual funds (MER's, DSC fees, and associate trailing commissions), we provide significant transparency with respect to reporting in terms of holdings, transactions, fees, and performance (time-weighted rates of return and money-weighted rates of return – as required by CRM2), and we have the ability to provide clients with a fully customizable investment portfolio that best suits their investment risk tolerances and objectives rather than potentially a shelf of limited investment products.

It is our opinion that Portfolio Management firms are the rated highest in terms of compliance under all categories regulated under the Canadian Securities Administrators. Portfolio Management firms are able to demonstrate high educational and experiential proficiency through registration requirements and professional designations. We have a fiduciary duty to our clients to act in their best interests. Portfolio Management firms also have an extremely low instance of litigation, client complaints or regulatory issues and as such as evidenced in the most recent OBSI report and which will be known to the CSA and OSC through the OSC's annual Risk Assessment Questionnaire. We should be able to exercise our professional judgement over client investment portfolios as we have been since the category of Portfolio Manager came to be. Enacting these new amendments to National Instrument 31-103 would be detrimental to all Portfolio Management firms who have these "Referral Arrangements", as they have been broadly defined, as the core of their business development model.

Furthermore, we feel that these prescriptive requirements for Portfolio Management firms have no place in our regulatory environment and there is no comparable to regulate the profession as such. We believe that we have outlined our rationale for this as noted in our 5 areas of concern. Focus should be on those firms designing and selling specific products as these firms are fundamentally conflicted in the very way they conduct their business, which is to put their business interests ahead of clients. The focus should not be on those who are professionals, bound by a code of ethics, who have the satisfactory education and experiential requirements which is the gateway to a true professional standard which is that of a fiduciary.

We believe that Portfolio Managers should be regulated in the same fashion of other professions, such as lawyers, accountants, doctors, etc. Here, there is a comparable for how a lawyer evaluates what is best for their client, how an accountant provides tax or business structuring advice, or how a doctor provides medical and treatment advice. This is what a professional does – provide advice that it in the best interest of the client, period. There will always be outliers in the professions where those who have stepped outside the boundaries will have to be dealt with. This will always occur; however, this needs to be done in a way that makes sense to the profession as a whole.

We are of the opinion that these proposed amendments are an insult to the professionals who assumed that the regulators respected of the educational and personal sacrifice and the legacy of professional advice provided to clients across Canada. BCV Asset Management Inc. believes that the CSA should revisit their proposed amendments to National Instrument 31-103 and focus on those concerns that truly impact the end client, remove their prescriptive nature, and focus on those individuals who truly pose a threat to the regulatory environment in Canada.

We thank you for the opportunity to provide commentary to the proposed amendments to National Instrument 31-103 and would like to offer our availability for future solicitation of comments or participation in consultation or focus groups as the CSA continues to navigate to a final set of amendments.

Should you need to contact us, please see our contact information below.

Sincerely yours,

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