

July 20, 2004

**Via E-Mail**

John Stevenson, Secretary  
Ontario Securities Commission  
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Dear Mr. Stevenson:

**Re: The Fair Dealing Model**

We are responding to the request for comments on the Fair Dealing Model (“FDM”) Concept Paper I (the “Concept Paper”) of the Ontario Securities Commission (“OSC”) on behalf of RBC Investments, the wealth management division of RBC Financial Group. RBC Investments includes RBC Dominion Securities Inc., RBC Action Direct Inc., RBC Asset Management Inc., Royal Mutual Funds Inc. and RBC Private Counsel Inc. We participated in the preparation of the comment letter submitted to you by the Investment Funds Institute of Canada and are generally supportive of its contents. This letter highlights issues that are of particular concern to us.

We recognize that the formal comment period has passed but thought that it timely to provide you with this feedback now that we have had an opportunity to participate in a number of the FDM working groups (the “Working Groups”).

We have divided our comment letter into two sections. The first outlines general comments on the development of the FDM proposal and the second provides specific comments on certain elements of the Concept Paper.

***General Comments***

***Lack of Demonstrable Improvements***

While we are supportive of initiatives to enhance investor protection, we do not believe that the Concept Paper has provided enough evidence to justify a complete revamping of the current regulatory structure. The current FDM has outlined a number of proposals

without providing the background as to what particular problems the changes will address. We do not believe that there has been sufficient investigation into existing practices or alternatives to warrant many of the changes being proposed. Such research might demonstrate that there are more efficient or cost-effective methods of providing substantially the same benefits to investors as contemplated under the FDM at potentially less disruption to both the industry and investors.

#### *Cost Benefit Analysis and Timing*

The Concept Proposal states that the OSC will undertake a cost-benefit analysis on the FDM through information gathered at the Working Groups. We have found it difficult to undertake a comprehensive assessment of the FDM proposal without this industry-wide cost-benefit analysis. Such an analysis would be helpful in determining whether there are alternatives to the FDM that could provide the benefits of enhanced transparency and more meaningful disclosure without the complete revamping of the current regulatory regime contemplated in the Concept Paper.

We understand that the second phase of the FDM is expected to be released at the end of the calendar year and will propose a “single service provider license based on a business reality test.” Again, it is difficult for us to provide comprehensive comments on the Concept Paper without knowing the full extent of the proposals to be released in the second phase as the outcome of the Concept Paper deliberations are somewhat dependent on the elements being proposed for the next concept paper.

#### *National Approach to Securities Regulation*

We strongly supported the key recommendations outlined by the Wise Persons Committee in its report entitled “It’s Time” published on December 13, 2003. These recommendations included the creation of a single, national securities regulator administering a single, uniform rulebook. We understand that the OSC has also been a strong supporter of these recommendations and are therefore disappointed that the OSC has introduced the FDM solely as an Ontario project at this time. The formulation of the FDM without the participation of the Canadian Securities Administrators (“CSA”) is inconsistent with the OSC’s support of harmonization of securities regulation among all the Canadian provinces. Should the FDM proceed without the endorsement of the CSA and the other provincial regulators, we believe it will create a significantly worse environment than currently exists both with respect to investor understanding of applicable rules and the costs for investors and market participants.

We are also concerned that an “Ontario only” approach would cause significant problems for market participants that operate nationally. They would, under the model as proposed, be forced to alter their businesses to meet two sets of requirements – one in Ontario and one for the rest of the country – at significant unnecessary cost to their operations and ultimately to investors.

We understand that the OSC is promoting the implementation of the FDM on a national level and is currently making presentations to the various provincial securities regulatory authorities in that regard. While we are pleased that the OSC is seeking a national approach with respect to this initiative, we are unconvinced that endorsement from other

securities regulatory bodies of the current FDM will be forthcoming. We also believe that it would be more appropriate to seek national support on these types of regulatory initiatives at the outset.

#### *Consultative Process*

We are strongly encouraged that the OSC sought the input of industry participants in respect of the FDM proposal. However, we are concerned that the process of industry consultation is generally not being managed effectively.

The Working Groups were established by the OSC to “tackle implementation issues” of the FDM. However, as a comprehensive cost-benefit analysis is not available and alternatives to the proposal do not appear to be up for discussion, the Working Group participants can only advise as to whether they support the current FDM in theory. We suggest that the Working Groups be suspended until the further necessary research or analysis is complete. This analysis should, in our view, consider alternative means of achieving the stated regulatory objectives of the Concept Proposal.

More generally, we also think it is important to note that there is an understandable reluctance on the part of the industry to dedicate resources to new regulatory initiatives when the future of these initiatives remains uncertain. This confusion with respect to regulatory focus also makes it more difficult for industry participants to effectively engage in long-term strategic planning.

#### *Role of SROs*

We are concerned that the Concept Paper has not adequately considered the role of SROs in the marketplace. Both the Investment Dealers Association of Canada (“IDA”) and the Mutual Fund Dealers Association (“MFDA”) have mandates that include the promotion of investor protection. We strongly urge the OSC to work with the IDA and MFDA to determine if the goals of the FDM can be attained with greater reliance on the current regulatory model.

#### *Comments on the FDM*

##### *Regulation on the Basis of Relationships*

The FDM proposes to shift the regulatory framework from one that regulates on the basis of the particular products sold by dealers and their representatives, to one that regulates on the basis of the relationships formed between investors and their dealer or dealer representative. The Concept Paper states that the shift to a relationship-based regulatory model reflects modern business practices and that product-based regulation is no longer appropriate. We support the principle of a regulatory model that reflects business realities and is well understood by investors, but have the following concerns with respect to the current FDM proposal.

Discount, full-service and discretionary relationships do exist in the industry today. However, we are not convinced that the proposal around the creation of three distinct categories of advisory relationships combined with the requirement that the investor choose one of the three relationships for each account achieves the intended result at an

appropriate cost. More specific but simple guidelines around ongoing client communication and disclosure of dealer or advisor compensation may achieve the same result at a much lower cost.

Under the proposed model, in the event that a client wanted to execute a single transaction on the basis of an advisory relationship rather than a self-managed relationship that was already established under existing account documentation, it appears that separate account documentation would have to be created. This would have the result of creating inefficiencies and additional steps to carry out a transaction that an investor would more easily be able to undertake within the current regulatory regime and we submit at little perceived benefit to the investor.

More importantly, the assessment of the second category of relationship, the full-service or advisory relationship, as currently defined, is unclear. The Concept Proposal does not define advice and acknowledges that there is no intention on the part of the OSC to regulate advice. However, it appears that the model could create indeterminate liability for advisors as they would become responsible not just for trade-by-trade supervision, but for the ongoing suitability of a trade long after it has settled. This appears to be a significant departure from the current “business reality” of an advisory relationship. We believe that this apparent broadening of an advisor’s current responsibilities and liabilities is inappropriate and poses greater risk to full-service dealers who rely on their clients to make the ultimate determination as to whether or not they wish to accept an investment recommendation of their advisor. We question whether this was the intended effect given the stated goal of regulations that reflect the current business structures.

#### *Third-Party Compensation*

The Concept Paper outlined three alternatives to address concerns with respect to third party compensation. We understand that the OSC has decided not to pursue further the two options of banning embedded compensation or imposing point of sale liability on the fund company. We felt very strongly that these two options were inappropriate as well as contrary to the OSC’s stated objective of regulation that reflects current business structures. Therefore, we are encouraged with the response of the OSC and reiterate that the regulatory focus should remain on requiring transparent and understandable disclosure of compensation arrangements, rather than prohibiting or mandating certain types of arrangements.

#### *Education*

We believe that investor education is important and that both industry participants and regulators have a role to play in this area. While the intent of this portion of the current FDM proposal may have been to provide more consumer-friendly educational information, we are concerned that, as drafted, the result of the FDM is an obligation on the industry participant to educate the investor. We support the concept that educational information should be made available to all investors by both managers and dealers (perhaps in the form of baseline educational pieces); however, it must be left up to the individual investor to decide whether or not they want it. Investors who choose to transact without availing themselves of the educational materials provided may not be behaving intelligently but are being treated fairly.

We strongly urge the OSC to consider the comments made in this letter and by other industry participants before proceeding further with the FDM. We, as would other firms, would be appreciative of receiving feedback from the Commission addressing our concerns at this stage. We would like to thank the OSC for the opportunity to provide these comments on the FDM. Please feel free to contact me at 416-955-7826 if you have questions or would like to discuss further any of the matters raised in this letter.

Yours truly,

*“Reena S. Lalji”*

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