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VIA E-MAIL: comments@osc.gov.on.ca; consultation-en-cours@lautorite.qc.ca
May 30, 2017

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, New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Yukon
Superintendent of Securities, Nunavut

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Re: Canadian Securities Administrators (CSA) Consultation Paper 81-408: Consultation on the Option of Discontinuing Embedded Commissions (Consultation Paper)

On behalf of Investment Planning Counsel Inc. (IPC), we thank the CSA for the opportunity to provide comments on the Consultation Paper.

Our company

IPC is a diversified financial services company, operating on a national platform with over $26 billion in assets under administration as at March 31, 2017on behalf of approximately 260,000 investors across all provinces. Its subsidiaries include IPC Investment Corporation (IPCIC), an MFDA member, IPC Securities Corporation (IPCSC), an IIROC dealer member and Counsel Portfolio Services Inc., (Counsel), a mutual fund manager. IPC is part of IGM Financial Inc., which is a member of the Power Financial Corporation (PFC) group of companies.

General Comments

IPC has a strong interest in the discussion set forth in the Consultation Paper. Founded in 1996, IPC has always adhered to the philosophy that clients are best served through the comprehensive services of an independent financial advisor.

We are supportive of the CSA's overall objectives to set out a more explicit framework for addressing conflict of interest matters and to clarify the nature of the client-registrant relationship for clients, which we believe have been largely met through the Fund Facts pre-sale delivery disclosure (Point of Sale or POS) and Client Relationship Model (CRM) projects, as well as the current proposals in CSA Consultation Paper 33-404 (the CSA CP 33-404).[1]In our view, however, the regulatory option to discontinue embedded commissions will have far-reaching, and we believe, unintended outcomes.

We already have, as the CSA acknowledges, a highly concentrated fund distribution industry in Canada with deposit-taker and insurance owned fund distributors dominating fund distribution. We anticipate that a full transition to direct-pay arrangements will significantly impair the ability of a number of independent dealers and representatives from continuing to service mass-market households and more modest clients, which will diminish both the degree of product and advice choices for investors, as well as, impact the affordability of financial advice. A potential regulatory outcome that leads to an even more concentrated fund distribution industry is not, in our view, optimal for retaining a competitive and innovative financial services industry, nor does it facilitate good investment outcomes for Canadians. We strongly urge the CSA to reconsider the proposals in the Consultation Paper in this context.

Our submissions are structured as follows:

- How the current regulatory reforms underway will address the key investor protection and market efficiency issues identified in the Consultation Paper;
- The market trends and forces underway that arealso driving changes aligned with the CSA's objectives;
- Alternative regulatory options for the CSA to consider instead of discontinuing embedded commissions;
- The impact discontinuing embedded commissions could have on independent dealers, their representatives and their clients, and specifically for IPC.

In addition to our specific comments, we also wish to emphasize the following three key objectives that we believe must guide the CSA's decision-making process for both the Consultation Paper and the current proposals in CSA CP 33-404, which we've been told previously by the CSA to consider together.[2]

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[1]CSA Consultation Paper 33-404 Proposals to Enhance the Obligations of Advisers, Dealers, and Representatives Toward their Clients (April 28, 2016).

[2]CSA Staff Notice 81-327 *Next Steps in the CSA's Examination of Mutual Fund Fees*, June 29, 2016.

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1. Preserving financial advice for Canadians

Personal savings is a key component to the accumulation of financial wealth and retirement readiness. Among other things, households who have and keep an advisor (i) are twice as likely to save for retirement at all ages; (ii) have significantly higher levels of investable assets at all ages; (iii) improve their regular saving for retirement at all income levels; (iv) rate themselves as more financially knowledgeable; and (v) are more confident in their ability to achieve a comfortable retirement.[3] We also know that investors' primary source of financial information comes from their advisors.[4]

Beyond active management ("Alpha") and asset allocation ("Beta"), better financial planning decisions ("Gamma") have a significant impact on an investor's retirement outcomes. In fact, "Gamma" can increase approximately 1.59% in arithmetic "Alpha" on a portfolio.[5] Therefore, as part of the CSA's deliberations, we urge the CSA to be mindful of not proceeding with any regulatory changes that may have the potential to diminish the level of advice provided to Canadians.

2. Not disadvantaging the sale of securities vs. other financial services and products

We share the views expressed by our sister companies within PFC on this topic, that the obligations owed by registrants to their clients should not be dependent on the legal nature of the product being sold or the license held by the registrant. The securities industry is only one part of the financial services sector in Canada. Insurance and deposit products are also significant segments of the capital markets. We found it particularly disconcerting that the CSA suggests in the Consultation Paper that the high level of horizontal integration at deposit-taker and insurance owned dealers somehow leads these firms to focus less on any one business line and more on "gathering assets across all business lines and on directing clients to the appropriate business line". We submit there is evidence to the contrary.[6]To truly enhance the level of advice provided to Canadians, we need consistent reforms across securities, insurance and banking sectors. As part of the CSA's consideration, it will therefore be critical to ensure that any regulatory action does not result in product and regulatory arbitrage with clients being directed towards products that may not best meet their investment needs and objectives.

We believe it is noteworthy that in each of the jurisdictions that has introduced a complete ban on embedded commissions, the ban has extended beyond investment funds. This is a very important

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[3] Sources: CIRANO, *Econometric Models on the Value of Advice of a Financial Advisor* (2012) and *The Gamma Factor and the Value of Financial Advice* (2016). All advised households, at all age levels, are found to save at approximately double the rate of non-advised households, with advised households having higher net worth than non-advised households across all ages and income levels (Source: IFIC *The Value of Advice*, 2011).

[4]Key Highlights CSA Investor Education Study 2016 prepared for the CSA by Innovative Research Group, Inc. (April 2016).

[5] Source: Morningstar, *Alpha, Beta and Now... Gamma,* 2012.

[6]See: CBC News reports by Erica Johnson, http://www.cbc.ca/news/canada/british-columbia/td-tellers-desperate-to-meet-increasing-sales-goals-1.4006743 (March 6, 2017), http://www.cbc.ca/news/business/td-bank-employees-admit-to-breaking-law-1.4016569 (March 10, 2017), http://www.cbc.ca/news/business/banks-upselling-go-public-1.4023575 (March 16, 2017) http://www.cbc.ca/news/canada/british-columbia/bank-s-deceptive-titles-put-investments-at-risk-1.4044702 (March 29, 2017) and http://www.cbc.ca/news/business/financial-investment-rules-client-interests-1.4069847 (April 17, 2017).

distinction to the proposal in the Consultation Paper. While we welcome the CSA's support for a harmonized regulatory approach for similar products, and we appreciate that the Canadian Council of Insurance Regulators (CCIR) has indicated it will review the CSA policy direction on embedded commissions and assess its appropriateness for segregated funds, the potential for regulatory arbitrage remains. The Consultation Paper also gives no indication of the timeline for the CCIR's review or a commitment for coordinated action with the CSA, nor is there any discussion in the Consultation Paper of whether a similar review is being considered by the Office of the Superintendent of Financial Institutions (OSFI) with respect to banking products, such as GICs and daily interest accounts (DIAs).

3. The need to ensure advice remains affordable and accessible for modest investors

Finally, we believe it is critical for the CSA to ensure that financial services and advice remain accessible and affordable to all Canadians going forward. Research shows that fewer choices of compensation models can limit access to advice and result in higher overall cost if only fee-based compensation is available, particularly for households with more modest investment levels.[7] We believe that the decisions by some global regulators to not proceed with a ban on embedded commissions, in part because of the recognition of the importance of retaining independent dealers and manufacturers to preserve greater choice for investors in their markets, should not be overlooked. We encourage the CSA to consider and provide a more detailed analysis as to why the approaches taken in countries such as Sweden, Hong Kong, Germany, New Zealand and Singapore, among others, would not be appropriate for the Canadian market and for Canadian investors before a regulatory decision is made to discontinue embedded commissions in Canada.[8]

Comments on the Consultation Paper

[7] In the United States, the average total cost of fee-based advice is comparable to the cost of advice in Canada (2.00% to 2.20%), however the cost is higher for modest investors with less than $100,000 of financial assets (2.40%) than for high net worth investors (1.70%) (Source: Investor Economics & Strategic Insight, *Monitoring Trends in Mutual Fund Cost of Ownership and Expense Ratios: A Canada-U.S. Perspective,* 2015). Where regulation has been changed to ban or limit commission, the absence of embedded compensation has been found to lower the cost of the product, but the cost of advice was seen to go up. It has also been found that in jurisdictions that have moved to fee-based compensation, those with less wealth or income found it more difficult to get advice than others. Ultimately, all forms of compensation affect advice and outcomes and there is not enough evidence indicating that fee-based compensation will lead to better long-term outcomes than commission-based compensation (Source: Mutual Fund Fee Research prepared for the Ontario Securities Commission on behalf of the Canadian Securities Administrators, written by Dr. Edwin Weinstein, PhD The Brondesbury Group (Spring, 2015) ("The Brondesbury Report")).

[8] Currently, only four countries have imposed a ban on embedded commissions: Australia, Netherlands, South Africa and the United Kingdom. In the Netherlands, the discontinuation of embedded commissions is a voluntary arrangement among the five large banks that dominate investment fund distribution. While under the MIFID II reforms, the imposed ban on embedded commissions only applies to independent financial advisors, which make up only 11% of the European market. Despite MIFID II, a number of jurisdictions have concluded not to impose a ban on embedded commissions, including: Belgium, Denmark, France, Germany, Ireland, Italy and Sweden. Additionally, we have seen a number of other jurisdictions decide not to proceed with the regulatory option to discontinue embedded commissions, among them: Brazil, Hong Kong, India, Israel, Japan, New Zealand, Singapore, South Korea and the United States.

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Current Regulatory Initiatives Address the Issues Identified

The CSA identified three key investor protection and market efficiency issues with embedded commissions. In our view, the POS and CRM projects, together with the CSA CP 33-404 proposals, once all reforms and/or guidance has been fully implemented, will substantially address each of these issues. To the extent there remains any gap, we submit market forces underway (which we discuss later in our submission) together with other possible regulatory actions (noted below) will achieve the CSA's desired objectives.

1. **Embedded commissions raise conflicts of interest that misalign the interests of investment fund managers, dealers and representatives with those of investors**

To suggest that investment fund managers who pay embedded commissions to dealers may be incentivized to rely more on those payments than on generating performance to attract and preserve assets under management is simply not our experience, nor do we believe it is an accurate portrayal of today's competitive market environment.

As we identify below in our discussion of market forces driving changes independent of regulation, our data indicates that the majority of embedded commissions offered by investment fund managers are substantially the same across asset classes and series and that manufacturer margins and costs (management expense ratios) are decreasing. We also note that the trend of dealers and advisors is to shorten the number of fund manufacturers with whom they are working, with the key drivers of dealers and advisors focused on overall performance of the company's products and consistent performance.[9] All of this means that investment fund managers are today aggressively competing on fund costs and performance.

The introduction of the proposals in CSA CP 33-404 will only further increase, in our view, the scrutiny by dealers and their representatives on investment fund costs and performance. The explicit requirements in the know-your-product (KYP) and suitability proposals will require registrants to take into account the impact on the performance of the product of all fees, costs and charges, <u>including any embedded commissions paid</u> as part of the suitability analysis. The reforms also propose that dealers and their representatives will have to assess whether any remuneration, <u>including trailing commissions</u>, could reasonably be expected to inappropriately influence how representatives deal with their clients. We strongly believe that with CSA CP 33-404, the CSA has effectively addressed any residual reliance there may still be today for fund managers to compete on embedded commissions to promote sales or retain assets.

The central purpose of the proposals in CSA CP 33-404 is "to better align the interests of registrants with the interests of their clients". As we've indicated, we believe that the proposals when implemented as rules and/or guidance will address the concerns expressed in the Consultation Paper that embedded commissions may encourage dealers and their representatives to recommend higher cost fund products, or promote a particular purchase option, that pays them a higher commission to the detriment of investor outcomes. In fact, we consider the breadth of the proposed conflicts of interest reform and accompanying guidance in CSA CP 33-404 on compensation arrangements and incentive practices to capture much more than simply any potential for influence caused by embedded commissions. The proposed reform requires dealers to assess whether <u>any remuneration</u> could reasonably be expected to inappropriately influence

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[9] Source: Environics Research, *2015 Adviser Perceptions in Canada: A focus on the Future & Consumers* (2015).

how representatives deal with their clients. This approach recognizes that conflicts of interest and the potential for misalignment of interest exists in any fee model, not just with embedded commissions.[10]

2. Embedded commissions limit investor awareness, understanding and control of dealer compensation costs

From the beginning, the POS project was intended to increase investors' awareness and understanding of embedded commission costs, as well as better equip investors to compare the costs of one mutual fund to another, and to understand the impact of such costs on their investment returns. Similarly, the CRM reforms introduced, in the first phase, new relationship disclosure to investors at account opening explaining the types of products and services provided by the dealer as well as more fulsome information on charges, including transaction charges, which they may expect to pay in connection with their investment.[11] Phase 2 of CRM (CRM2) next introduced new annual account level reporting on charges and other compensation of commissions and other amounts paid to dealers, including any embedded commissions in dollar amounts. Like the POS project, the CRM project was intended not only to increase investors' awareness and understanding of dealer compensation costs, but to also lead to better, more informed investor decision making when it comes to dealer compensation costs and the corresponding level of service that's being provided.

Investor knowledge, attitude and behaviour, registrant practices, fees and product offerings, have all been identified by the CSA as potential positive impacts of the POS and CRM2 projects.[12]Without the results of the CSA research project underway to measure the impacts of these projects, we do not believe it's appropriate for the CSA to conclude that discontinuing embedded commissions is necessary to create greater investor fee awareness, or opportunities to negotiate and have greater control over dealer compensation. This position also seems inconsistent with the continued regulatory focus by the Mutual Fund Dealers Association of Canada (MFDA) as well as the CSA to continue to enhance CRM2 disclosures to capture mutual fund management fees, as well as the non-cash incentives that may be paid to the dealer or advisor and its representatives.[13]

3. Embedded Commissions paid generally do not align with the services provided to investors

The concern raised by the CSA in the Consultation Paper of the need for advice and services to better align with the costs paid by investors (directly or indirectly through the trailing commission) is an important issue. However, in our view, this is an issue that may impact all forms of compensation (not just embedded commissions), and is not solved simply by discontinuing such payments. While the direct-pay option may be more transparent to the investor that fees are being paid, investors selecting this option may not be aware of the fees other investors are paying or the services they are receiving, nor will clients necessarily

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[10]All forms of compensation affect advice and outcomes (The Brondesbury Report,p 4).

[11]Including the initial sales charge and DSC options and any trailing commissions or other embedded commission paid.

[12]See press release: CSA to Measure Impact of Point of Sale Amendments and Phase 2 of the Client Relationship Model (August 22, 2016).

[13] MFDA Bulletin #0671-P – Report on Charges and Compensation – Consultation Regarding Cost Reporting for Investment Funds (December 18, 2015) and CSA Notice and Request for Comment on Proposed Amendments to National Instrument 31-103, Companion Policy 31-103CP and National Instrument 33-109 (July 7, 2016).

have any market strength to negotiate fees or to realize or to be able to calculate the impact those (now external) fees have on the returns of their portfolio.

In fact, recently we saw the Investment Industry Regulatory Organization of Canada (IIROC) in their review of compensation related conflicts indicate that fee-based accounts may not always be in the best interests of clients.[12]

As noted in the Brondesbury Report, no empirical studies have been done to document whether investors have greater after-fee investment returns with fee-based compensation instead of commission-based compensation.[13] There is no standard fee for service structure in the market place: there can be flat fixed fee, flat fee based on percentage of assets, tiering of fees based on percentage of assets or fees based upon asset classes. IIROC dealer members also have fee for service structures associated with managed accounts in respect of which those fees are for the provision of discretionary investment management services along with other services.

Within our business model, embedded commissions are not strictly limited to providing advisor compensation in exchange for investment advice, but rather support a broad range of services provided by the advisor and dealer. For example, fees are used towards: reporting, portfolio rebalancing, compliance, insurance, regulatory fees, IIROC and MFDA investor protection fees, infrastructure, back-office systems and investor education and may be used towards financial planning and estate and tax planning.

We believe the increased performance reporting and saliency of fund costs and dealer compensation created by the POS and CRM projects will in fact lead to better alignment of overall services and advice with dealer compensation paid. These initiatives, fully implemented, are expected to cause investors to question the overall level of services and advice they are receiving, whether embedded or not, which in turn is anticipated to cause representatives to better demonstrate their value proposition or, lead to investors switching to lower-cost alternatives. If the articulated aims for the POS and CRM projects are met, investors will be empowered to make more informed decisions on whether the fees orcommissions they're paying, embedded or not, are commensurate with their specific needs, expectations and preferences for service and advice.

We expect thiswill prompt greater price and service competition of dealers and their representatives to demonstrate their value proposition and to promote the level of services provided to investors in exchange for dealer compensation. In fact, through our complaint intake management, we have already seen clients questioning their advisors with respect to the services rendered in exchange for the fees they are paying. Our experience is that clients have become more engaged in the discussion of how much they compensate their advisor and dealer, what services are being provided in exchange for such fees, and the frequency and level of engagement they expect from their advisor.

4. Market Forces are Already Driving Changes Aligned to Regulatory Objectives

We strongly believe that competitive market forces, influenced in part by recent regulatory reforms, are already effecting the industry changes that the CSA expects to occur from a ban on embedded

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[12] See IIROC Notice 16-0297 Managing Conflicts in the Best Interest of the Client – Status Update (December 15, 2016) and IIROC Notice 17-0093 Managing Conflicts in the Best Interest of the Client – Compensation-related Conflicts Review (April 27, 2017).

[13] The Brondesbury Report, p 18.

commissions. In particular, we are seeing today the growth and availability of direct-pay options andreductions in fund fees, increased price competition, decreasing fund management costs and market innovations in product distribution and advice.

The CSA is correct to identify that the share of mutual fund assets held in fee-based purchase options (F series) is growing, and growing quickly. Competitive market pressures are driving the growth of F series for many fund manufacturers, with frequent changes to the F series offering or pricing. Fee-based program assets as a percentage of total assets is gaining ground in IIROC platforms, and in full-brokerage the shift in advisor compensation is inline with the shift to fee-based.[14]Our own experience at IPCSC is that fee for service mutual fund holdingshas increased, from 4% to 21% from December 2011 to December 2016.

Where we disagree with the CSA is the discussion in the Consultation Paper that direct-pay options today are not available to all investors in all channels. While it is correct that IIROC dealers generally do not offer fee-based programs to mass-market households, generally because of a lack of scale and the cost to implement, there are direct-pay options available to MFDA representatives today looking for fee-for-service for smaller investors where the dealer program may be restrictive to high minimum investments or fees for the reasons identified.At IPC, in February 2006,we launched a negotiable advisor fee series, Series D for our Counsel funds. This manufacturer sponsored solution allows for the negotiation of an advice and service fee directly between the investor and dealer, through the representative, pursuant to an explicit agreement, and then for Counsel to facilitate the investor's payment of dealer compensation by collecting payments from the investor's investment (through periodic redemptions).Today many fund manufacturers have aSeries D equivalent(often named FB series) and there are other fund manufacturers who offer the same negotiable attributes of Series D in an existing series.

In the last few years, we have also seen a number of investment fund managers, including Counsel, announcing fee cuts, trailer fee cuts, administration fee cuts, preferred pricing programs as well as an increasing number of share classes with lower management expense ratios (MERs) year-over-year.[15]Asset-weighted (MERs) and management fees for long-term funds also continue to decline.[16]

Finally, Canada is now home to more than 80 fintech firms.[17] We believe the increasing innovation and technology we're seeing in the market from both fintech start-ups and from incumbents offers investors choices in product distribution and advice, as well as increase price and competitive pressure on incumbents to demonstrate alignment of fees with the overall level of services and advice provided. We welcome this, and anticipate representatives providing advice will be able to differentiate themselves from asset allocation, advice 'light' platforms.

5. Alternative Regulatory Options to Discontinuing Embedded Commissions

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[14]Source: Strategic Insight, Retail Brokerage and Distribution, Summer 2015.

[15]December 2014 – December 2015, source: Insight Advisory Service, July 2016.

[16]Excludes funds with performance fees, funds with management fees charged at account level and labour sponsored funds, source: Insight Advisory Service, July 2016.

[17]Source: PwC, Canadian Banks 2016 Embracing FinTech movement, 2016.

In our view, any potential incremental or possible "complementary" benefit that the CSA anticipates could be achieved through the discontinuation of embedded commissions will be minimal, by comparison to the very real and significant impact to some stakeholders, particularly medium to small independent dealers, their representatives and their clients.[18]To the extent the CSA continues to consider that any of their concerns are not fully addressed, we believe there are other regulatory options available to address such concerns.

(a) **Dealers Offer a Direct-Pay Option** – If the CSA concludesthat there continues to be a need to further enhance investor awareness, understanding and control of dealer compensation, we recommend the CSA considers the regulatory option of requiring all dealers who offer an embedded commission arrangement to also have a direct-pay arrangement option available to all investors. This option could take the form of dealers allowing investment fund managers to facilitate investor payment to dealers of compensation, as contemplated in the Consultation Paper.The inclusion of a direct-pay option would allow both compensation arrangements to be presented and explained to the investorat account opening, or by notification to existing investors, and then give investors a clear choice in remuneration methods while still preserving investor choice.

(b) **Enhanced Dealer Supervision of Advisory Services** –A more impactful and fulsome regulatory response for the CSA to consider to address the CSA's concern thatthe "one-size-fits-all" nature of embeddedcommissions may not align well with the services and advice actually being provided,would be to explicitly enhance the guidance to specify that the dealer has a supervisionobligation to ensure that a commensurate level of advice and service is in fact being provided in exchange for the payment by the dealer to the representative. This would be the case whether that payment is embedded or not.

(c) **Greater Specificity at Account Opening** - The CSA could also consider revisiting the guidance relating to CRM to requiregreater specificity in the current relationship disclosure delivered to investorsat account openingof the advice and services that will be provided in exchange for the dealer compensation to be paid.

(d) **Discontinuing Variable Trailers** - If the CSA takes issue with embeddedcommission rates that vary over the course of the investment, we would submit that it is certainly within the CSA's purview to provide notice that CSA staff will no longer receipt prospectuses with such arrangements

6. Impact on Independent Dealersand their Clients

A ban on embedded commissions will have considerable financial and operational impacts for IPC, and more importantly, on the level of service and advisory support we will be able to provide to our advisors and clients. As at March 2017,mutual fund trailing commissions accounted for 37% of the revenues in IPCSC, and upwards of 95% in IPCIC. Many MFDA dealer members will likely have similar dependencies on these sources of revenue. Evidence drawn from the MFDA Client Research Report indicates that of the assets

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[18]As noted by the MFDA, advisors with a book size of less than $2 million are more reliant on DSC commissions to finance their operations. A mandatory switch to fee-based or direct-pay arrangements will therefore have a greater impact on those smaller advisors who are more reliant on DSC commissions (Source: MFDA Bulletin #0721-C – MFDA Client Research Report: A Detailed Look into Members, Advisors and Clients, May 23, 2017, p14 (MFDA Client Research Report).

held by MFDA members, 6% are in no-load funds, 3% are in F class funds and 6% are in fund company administered fee based programs.[19]

As noted above, embedded commissionsare not strictly limited to advisor compensation in exchange for investment advice, but rather support a broad range of servicesprovided by the advisor and dealer to the investor. In addition to a potential loss in the level of services and advisory support we will be able to provide to our advisors and clients should a ban on embedded commissions proceed, we are also concerned that discontinuing embedded commissions may lead to fewer Canadians seeking financial advice.Canadian focused research suggests that despite the high level of trust and reliance investors'place on their financial advisor, only 16% of investorssurveyed would be willing to continue their advisory relationship if it resulted in upfront costs to them.[20]We also note that among Canadians, there's still a strong preference for taking guidance from a financial advisor over advice generated through an algorithm or robo-advisor.[21]

We anticipate that it will be unlikely that we will be able to transition all of the approximately 75% of our retail clientsnot currently in a direct-pay arrangement into a direct-pay arrangement. Coupled with the potential of fewer modest investors seeking advice, we may have feweraccounts to amortize fixed administrative and operational costs resulting inhigher fees for those investors who remain. Today our average fee-based account typically falls within the mid-market to affluent range, whereas most embedded commission accounts fall within the mass-market range. To date, we have been able to subsidizethe administrative and operational costs of more modest size accounts to service these investors through scale – a ban on embedded commissions will impede our ability to do so.[22]

Transitioning to direct-pay arrangements will also cause considerable disruption to investors, requiring accounts to bere-visited and re-papered in the absence of discretionary relief. As noted, IPC would have to take corrective action forapproximately 75%of its clients, which will take considerable time and cause considerable cost, as well as create the need for additional compliance oversight and reviews.

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[19] Ibid.

[20]Pierre Lortie, *A Major Setback For Retirement Savings: Changing How Financial Advisers Are Compensated Could Hurt Less-Than Wealthy Investors Most* (Vol 9, 13, April 2016)

[21] HSBC, *Trust in Technology: Country Report/Canada* (May 24, 2017).

[22]The MFDA Client Research Report (p 15) supports this conclusion, finding:

> Advisors may be using the embedded DSC commission paid by the fund company upon purchase to finance the cost of offering advisory services to mass market clients. If so, a ban of embedded compensation would eliminate the DSC commission and may result in advisors having to charge clients an upfront fee to cover the cost of their services. As mass market households are less likely to be able to afford direct-pay arrangements and are less likely to be eligible for fee-based programs, they would be the most impacted by a ban of embedded compensation.

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With respect to transitioning to direct-pay arrangements, today IPCSC is carried by NBCN Inc. and relies on its systems for fee-based accounts. Accordingly, we will only be able to offer other types of direct-pay options that NBCN Inc. builds into its systems. For IPCIC, today we have our own nominee platform for fee-based accounts. To the extent other direct-pay options may be introduced, we will have to contract with our back office system supplier to make these available. The time for this transition, as well as cost, will in large part be in the hands of our service providers. For our IPCIC client name business, for anything other than using the fund manufacturer to collect fees based upon a percentage of assets (i.e.D series), we will have to build our own systems to charge and collect fees. All of these system changes will take significant time and cost and with a limited number of back office system suppliers, as we noted, the cost and timing of these changes will be uncertain. Until the back office systems are up and running and these different direct pay options are available,we will not be able to begin the process of transitioning our clients. A related issue that should not be overlooked is how to address clients in non-registered plans or registered plans who do not respond or refuse to move to a direct-pay arrangement. We anticipate that in such instances discretionary relief or regulatory guidance may be necessary.

Conclusion

We firmly believe that the impact of the regulatory actions taken to date, once fully implemented, together with the changes already underway in the market, will substantially achieve the CSA's objectives across all compensation models without the need to implement a ban on embedded commissions.We submit the CSA should allow for any change in business models to occur organically where there is evidence to suggest it is occurring. As theCSA continues to contemplate changes to mutual fund fee models, we urge the CSA to be mindful that discontinuing embedded commissions may have the unintended consequence on modest investors of limiting access to, and increasing the cost of, the very advice contemplated by CSA CP 33-404 to help Canadian investors achieve their long-term investment needs and objectives.

A ban on embedded commissions unnecessarily restricts consumer choice.In our view, there are alternative regulatory options to discontinuing embedded commissions that are able to address any residual issues identified by the CSA, without the same negative impact on independent dealers and their clients and without reducing competition and innovation in our markets that a ban on embedded commissions may cause.We urge the CSA to consider the importance of embedded commissions for dealers operating within the financial planning channel and the potential devastating impacts a ban may have on their operations and solvency, to the detriment of their clients.

An advisor's greatest value to an investor is their ability to help steer the investor's emotions and ensure that they stay the course and commit to their long-term financial plan. Anecdotally, and based on our experience, many do-it-yourself investors have the unfortunate tendency of 'buying high' and 'selling low'.[1]

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[1]Based on research completed by JP Morgan and Chase within its 2014 Guide to Retirement, an investor holding units of the S&P500 composite index between 1993 and to 2013, who missed out on the 10 best trading days would have annualized returns of 5.4%, relative to 9.2% had they remained fully invested(Source: https://am.jpmorgan.com/us/en/asset-management/gim/adv/insights/guide-to-the-markets/viewer).

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Just as we anticipate that each of the 11 targeted reforms and best interest standard proposed under CSA CP 33-404 will require considerable implementation time, so too will the transition to direct-pay arrangements. It is difficult for us to respond to the transition options in the Consultation Paper without a clear understanding of the CSA's direction with respect to both of these proposals. The question is not simply how long theprocess will take to transition to direct-pay arrangements, but how long it will take in combination with a number of other significant regulatory reforms underway. Taking a lesson from CRM2 implementation, we urge the CSA to work collaboratively and early with the MFDA and IIROC and with all registrants as the consultation process continues, so that there is a shared appreciation of thetimeframes needed. For example, we believe further consideration will be needed as to what the CSA would expect regarding the transition to direct-pay arrangement with respect to each client, and whether or how advisors will gather the consent of each client and document the account. The CSA's willingness to grant or codify discretionary relief to facilitate various aspects of a transition under CSA CP 33-404 and the Consultation Paper will also be relevant in determining the implementation time that dealers, their representatives and their clients will need.

Finally, in the Consultation Paper the CSA seem to have positioned the discussion of active vs. passively managed funds as active management being an undesirable outcome for investors that will be remedied through the discontinuation of embedded commissions. In our view, both passive and actively managed investment products are important for our client base, and for maintaining an efficient and vibrant capital markets. As currently expressed by the CSA, we are concerned that some registrants will be inclined to favour passively managed products, not because it is what's most suitable for the client, but because of the perceived regulatory bias and compliance pressures against actively managed funds. We ask that the CSA be mindful of this issue going forward.

We thank you for the opportunity to provide comments on the Consultation Paper. Please feel free to contact me if you wish to discuss this further or require additional information.

Yours truly,
Investment Planning Counsel, Inc.

John G. Novachis

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