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June 8, 2017

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

The Secretary
Ontario Securities Commission
20 Queen Street West
19th Floor, Box 55
Toronto, Ontario M5H 3S8

Me Anne-Marie Beaudoin
Corporate Secretary
Autorité des marchés financiers
800, square Victoria, 22e étage
C.P. 246, tour de la Bourse
Montréal (Québec) H4Z 1G3

Re: CSA Consultation Paper 81-408 – Consultation on the Option of Discontinuing Embedded Commissions

Dear Sirs/Mesdames:

Citibank Canada Investment Funds Limited (“**CCIFL**”) appreciates the opportunity to provide comments to the Canadian Securities Administrators (the “**CSA**”) on CSA Consultation Paper 81-408 – *Consultation on the Option of Discontinuing Embedded Commissions* (the “**Consultation Paper**”).

About Citibank Canada Investment Funds Limited

CCIFL is a wholly-owned subsidiary of Citibank Canada, a Canadian chartered bank, which is in turn an indirect subsidiary of Citigroup, Inc. CCIFL is a registered portfolio manager and exempt market dealer in eight of the provinces of Canada, and a registered mutual fund dealer in Ontario and British Columbia. CCIFL sells securities of pooled investment funds to institutional and high net worth individual clients of Citibank Canada on a private placement basis and through accounts managed by CCIFL under the terms of an investment management agreement.

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Comments on the Consultation Paper

CCIFL recognizes the potential investor protection and market efficiency issues arising from the prevailing practice of remunerating dealers and their representatives for mutual fund sales through commissions, including sales and trailing commissions, paid by investment fund managers (“**embedded commissions**”) and supports the consideration of different compensation models. However, CCIFL submits that the potential option of discontinuing embedded commissions and transitioning to direct pay arrangements should not apply: (i) to investment funds sold in the exempt market under the accredited investor exemption set out in section 2.3 of National Instrument 45-106 *Prospectus Exemptions* (the “**Accredited Investor Exemption**”); (ii) in particular, to investment funds that are sold under the Accredited Investor Exemption to the category of investors defined as “permitted clients” in section 1.1 of National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing Registrant Obligations* (“**NI 31-103**”) (“**Permitted Clients**”); and (iii) above all, to exempt foreign investment funds sold to Permitted Clients.

The focus of the discussion in the Consultation Paper is on “mutual funds that are reporting issuers and members of the organization of such mutual funds”. CCIFL supports the consideration of alternative fee arrangements for mutual funds that are Canadian reporting issuers. All such funds are subject to the same regulations, and, therefore, a change in compensation arrangements will apply to all issuers equally and would be unlikely to have an adverse effect on competition, investor access to these mutual funds or to investment advice from dealers of these mutual funds. However, the Consultation Paper also states (*emphasis added*):

Recognizing that the fee structure of various types of investment funds and structured notes commonly includes embedded commissions, and with the aim of promoting a level playing field amongst comparable investment products and limiting opportunities for regulatory arbitrage, we currently anticipate that any regulatory proposal to discontinue embedded commissions would affect:

- an “investment fund”, as defined under securities legislation and
- structured notes,

whether sold under a prospectus or in the exempt market under a prospectus exemption.

Accredited Investor Exemption

CCIFL submits that any discontinuation of embedded commissions should not apply to investment funds sold in the exempt market under the Accredited Investor Exemption. The Accredited Investor Exemption only allows sales to sophisticated, typically institutional, investors with sufficient financial knowledge and investment experience to understand and take on the risks associated with certain investment offerings. These investors have access to complex and higher-risk investments that are not available to a typical retail investor. As such, CCIFL believes that the objectives of promoting a level playing field amongst comparable investment products and limiting opportunities for regulatory arbitrage would not be undermined by permitting embedded commissions for investment funds sold in the exempt market



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under the Accredited Investor Exemption, as the investment products offered pursuant to this exemption are not available to retail investors in any event.

The Consultation Paper identified three key investor protection and market efficiency issues in Canada related to embedded commissions:

1. Embedded commissions raise conflicts of interest that misalign the interests of investment fund managers, dealers and representatives with those of investors;
2. Embedded commissions limit investor awareness, understanding and control of dealer compensation costs; and
3. Embedded commissions paid generally do not align with the services provided to investors.

CCIFL respectfully submits that these investor protection issues are not of particular concern with respect to investors purchasing pursuant to the Accredited Investor Exemption. These investors tend to have a greater awareness and understanding of dealer compensation costs, particularly as the relevant fees are explicitly disclosed in writing in the applicable offering documents (thereby making them fully transparent to the investors). In addition, these investors typically have more bargaining power when it comes to negotiating fees than a typical retail investor. In some circumstances, investors relying on the Accredited Investor Exemption may prefer to compensate dealers through embedded commissions, rather than through a direct pay model.

The Accredited Investor Exemption, in and of itself, demonstrates that the CSA recognize that accredited investors do not need the protections of prescribed disclosures as in a prospectus, including investment fund costs. It would be inconsistent to nevertheless require prescribed commission disclosure.

Permitted Clients

CCIFL submits that, in particular, any discontinuation of embedded commissions should not apply to Permitted Clients purchasing investment funds under the Accredited Investor Exemption. CCIFL asserts there are no compelling investor protection reasons to prevent Permitted Clients, all of whom are sophisticated investors with investment expertise, from purchasing investment funds in the exempt market solely because such investment funds may include embedded commissions. Permitted Clients are sophisticated clients who do not require the level of protection normally afforded to retail investors. Permitted Clients tend to be experienced investors and may have more bargaining power in negotiating the fees they pay to dealers and brokers. Compensating dealers through embedded commissions may be a Permitted Client's preferred approach to paying for advice in certain circumstances.

The CSA has recognized that Permitted Clients do not require the investor protections afforded to retail investors by exempting dealers from the know-your-client and suitability assessment requirements in NI 31-103 for Permitted Clients, if the Permitted Client consents (see sections 13.2(6) and 13.3(4)). This demonstrates that Permitted Clients are well equipped to assess the suitability of investments, and CCIFL submits that this should reasonably extend to the assessment of compensation arrangements.



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Exempt Foreign Investment Funds

CCIFL submits that any discontinuation of embedded commissions should, above all, not apply to foreign investment funds that are sold to Permitted Clients in the exempt market. Foreign investment funds that are not Canadian reporting issuers are not subject to Canadian regulations and may be permitted to continue embedded commissions pursuant to regulations in their home jurisdiction. The discontinuation of embedded commissions will prevent sophisticated Canadian investors who fall into the category of Permitted Clients from investing in such foreign investment funds, limiting their available foreign investment options.

It is desirable for Permitted Clients in Canada to have cost-effective access to global investment products, thereby necessitating effective access to the brokers and dealers entitled to trade and provide advice in respect of such investment products. These brokers and dealers may be regulated in foreign jurisdictions, many of which permit embedded commissions as a form of compensation. By discontinuing embedded commissions on investment funds sold to Permitted Clients under the Accredited Investor Exemption, the CSA will effectively preclude access to certain foreign investment products and to the advice of brokers and dealers entitled to trade such investment products.

The CSA has recognized that over the years there has been an increasing interest in, and opportunities for, investment in foreign securities by sophisticated Canadian investors. For example, with the implementation of NI 31-103 in 2009, a structure was put in place for facilitating access by sophisticated clients to trading of foreign securities through foreign dealers that satisfy the international dealer registration exemption in section 8.18 of NI 31-103. CCIFL submits that discontinuing embedded commissions on foreign investment funds would limit the investment products available to Permitted Clients in Canada and may prevent such Permitted Clients from accessing the expertise of foreign dealers of such investment funds.

CCIFL submits that certain benefits of embedded commissions, such as access to advice of foreign dealers and heightened competition for foreign investment funds, may outweigh the issues or harms of embedded commissions in these particular circumstances.

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CCIFL appreciates the opportunity to submit these comments to the CSA on the Consultation Paper. If CSA staff has any questions concerning the matters discussed in this letter, please contact Robert McGuire, Chief Executive Officer, at (416) 947-4147 or [REDACTED]

Yours sincerely,

[REDACTED]

Robert J. McGuire
Chief Executive Officer