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Nova Scotia Securities Commission
Superintendent of Securities, Newfoundland and Labrador
Superintendent of Securities, Yukon Territory
Superintendent of Securities, Northwest Territories
Superintendent of Securities, Nunavut

CSA Notice and Request for Comment
Proposed Amendments to National Instrument 81-105 Mutual Fund Sales Practices and Related Consequential Amendments
http://www.osc.gov.on.ca/documents/en/Securities-Category8/csa_20180913_81-105_mutual-fund-sales.pdf

As a former "salesperson" employed in the securities industry, required by my employer to use the unapproved term "Investment Advisor", I feel qualified to comment on the two issues raised in the Consultation paper.

The first involves the case of OEO's (aka Discount brokers) selling a security that has a built in Legal obligation to provide unique services and personalized advice. Clearly, an OEO cannot provide personalized advice under its registration so it should not offer A series mutual fund for sale. If it does, it should be sanctioned by the applicable regulator, IIROC. IIROC has in fact determined that such sales are in breach of its conflict of interest rules and has guided that dealers make rebates to clients. IFIIC, the fund industry trade Association has publicly stated that the discount broker channel is wholly inappropriate for selling A series mutual funds. And investor advocates have urged regulators for years to stop this investor harm.

There is more than enough evidence therefore for regulators to order OEO's cease trading in A series mutual funds There is no need for the CSA to use a convoluted approach as proposed to protect DIY investors to contain this mis-selling. The real issue here is some ugly combination of deceit, overcharging, mal-disclosure, misrepresentation and conflict-of-interest. This should not be viewed as merely a NI81-105 sales practice issue. It is a complete ethical breakdown that harms investors, the reputation of the marketplace and the financial services industry.

Of course, there are other harms caused by this financial assault on the retail investor. For example, certain fund companies have been denied access to the discounter platform because they have refused to pay the trailer commission to appear on the shelf. There is also the question of deception. Fund Facts is very clear- the trailer commission is for personalized advice and, albeit unspecified, some services not provided as integral to the client account Agreement. This is a legal document as it forms part of the Simplified Prospectus for the mutual fund. OEO's cannot comply with this obligation yet they process trades and they do so without even warning that no advice or unique services can or will be provided. Is this not plain and simple misrepresentation? If so, why spin wheels talking about it; simply enforce the policy and penalize any firm that charges for services that it cannot provide.

The CSA has stated that there is approximately $25 billion of A series mutual funds with OEO's. What is 1% of $25 Billion? Ans. About $250 million per year for ZERO advice for as long as OEO clients own the A series funds! Who pays this $250 million? Of course it's the investor! Who benefits? Of course, the securities industry. And what is the OSC/MFDA/IIROC doing to correct this? Nothing? You mean this supposedly tightly controlled industry has done nothing to correct this?

CBC's Erica Johnson reports on an ex fund industry employee and his experience with OEO's. Steve Pozgaj and his wife paid almost $5,000 in trailer fees last year, for advice he says he never got and that discount brokers aren't legally allowed to give. You have to see this video : https://www.cbc.ca/news/thenational/diy-investors-fight-back-against-trailer-fees-cbc-go-public-1.4826351

If regulators cannot protect investors given this arsenal of facts, there is something very wrong with our regulators. It is absolutely shameful that the CSA is asking investors to comment on the blatantly obvious and not even issuing an Investor ALERT Bulletin warning investors of their inaction and failure to protect.

The second issue involves the controversial Deferred Sales Charge option in the sale of Prospectus qualified mutual funds. The vast majority of mutual fund clients aren't forthrightly told about the DSC/5% upfront commission and only find out about DSC's when they need to access some of their money or see the poor performance of the fund that was recommended to them and want out. DSC sold mutual funds are an effective way for a fund salesperson and his/her employer to make a quick buck and handcuff their clients to them for 6 or 7 years. The loser, as usual, is the trusting investor.

The CSA has, sadly, decided to retain embedded commissions but is now attempting to deal only with the most harmful strain, the DSC option.

Professor Douglas Cumming's empirical research report on embedded commissions https://www.osc.gov.on.ca/documents/en/Securities-Category5/rp_20151022_81-407_dissection-mutual-fund-fees.pdf demonstrates that investments under the DSC option have the least sensitivity to past performance out of all purchase options but nonetheless $241 billion dollars of assets under management were held in DSC funds (back-end and low load funds) at the end of 2015.This suggests massive mis-selling, locking clients into a fund for 7 years for no good reason instead of recommending no-load funds , the prevailing 0% FEL option, Index funds or low cost ETF's .

Per MFDA Conflicts-of-Interest Rule 2.1.4".. b. *In the event that such a conflict or potential conflict-of- interest arises, the Member and the Approved Person shall ensure that it is addressed by the exercise of responsible business judgment influenced only by the* ***best interests*** *of the client and in compliance with Rules 2.1.4(c) and (d). c. Any conflict or potential conflict-of-interest that arises as referred to in Rule 2.1.4(a) shall be immediately disclosed in writing to the client by the Member, or by the Approved Person as the Member directs, prior to the Member or Approved Person proceeding with the proposed transaction giving rise to the conflict or potential conflict of interest*". If this rule was really being adhered to, it is inconceivable that proper business conduct would involve the sale of a DSC fund, especially to a family struggling to put away their modest savings for retirement or a senior/retiree. The sale of a DSC fund is not a shining example of proper business, it is pure deceptive, monkey business. As an aside, it was 19 years AFTER its 1998 adoption, that regulators finally took the first NI81-105 enforcement action!

Supporters of the DSC option state that it provides access to advice [albeit conflicted sales advice, not fiduciary advice] for small accounts. But consider this BCSC finding: "While respondents with smaller portfolios saw improvements to their general and specific fee knowledge in greater numbers than those with larger portfolios, they were by far the least likely to have taken any action – 65% of those with portfolios smaller than $50k have done nothing since the first CRM2 report, compared to just one-in-five of those with portfolios over $250k… Just 53% of respondents were satisfied with the value received for the fees paid. https://investright.org/wp-content/uploads/2018/10/Investor-Readiness-For-Better-Investing-Part-4.pdf This suggests that smaller investors are not taking action even when they understand the nature and size of the fees. Why would that be? The CSA should try to find out why and the associated investor protection implications. To not investigate this immediately raises important questions about the neutrality and professional integrity of the CSA.

The MFDA's 2017 Client Research Report http://mfda.ca/wp-content/uploads/2017_MFDA_ClientResearchReport.pdf indicates it has identified seniors as a particular concern with respect to the mis-selling of DSC funds and that dealers may be using DSC commissions to finance the cost of their operations to mass market clients. In other words, DSC sold funds appear to be targeted at the most vulnerable investors. The MFDA Client research study continues: "Advisors with a book size of less than $2 million are most reliant on DSC commissions to finance their operations with 53% of their book in DSC funds. As advisor book size increases, the amount of DSC within the book decreases and mutual fund assets shift to FE and NE funds". Elimination of the DSC option would therefore accelerate the switch to fee-based, direct pay arrangements, 0% FEL or no -load funds. It would also cause dealers to change their business models. That's a good thing .To be sure, that would increase investor protection and decrease misalignment of interests.

Except for Fidelity and perhaps another firm, the MER of a DSC sold fund is identical to a FE load fund. If the true cost of the DSC series fund were calculated, it would be higher than the FE series. We see this in the Fidelity funds. As a result, the DSC cost structure is being subsidized by other unitholders. How is this fair?

It is ironic that industry participants are decrying a ban because it will limit access to advice for small investors while the Small Investor Protection Association, the voice of small investors, supports a ban of the DSC sold mutual fund. Perhaps self-interests are at play?

Given all the evidence of actual and potential harm to retail investors I recommend the DSC option be prohibited immediately. You have known for far too long about the dangers to investors of this option which benefits only the salesperson and the securities firm. If anything, one could argue that your reluctance to take any action serves to demonstrate that regulatory capture occurred long ago.

To make the point with yet another example, why does the governing legislation state that the approved title was "salesperson" until 2009 at which point it was changed to "dealing representative"? I challenge you to send me one business card for each securities firm that uses the correct title.

Instead of using the legally mandated title, the employer provides business cards that state "investment advisor" or "financial advisor". Why would this supposedly tightly regulated securities industry with the OSC and its SROs, the MFDA and IIROC, not have caught and corrected this misrepresentation of the title?

Why must the approved title be utilized at all times in every profession except for the securities industry? Why would the Real Estate Council of Ontario (RECO) punish not just the real estate salesperson but also the employing real estate firm, if any title not approved by RECO is used? Can a lawyer say he/she is an attorney? No? Why not?

Can anyone say they are a lawyer? Can anyone say they are a doctor or an architect or an engineer or…

Is it not a joke that the OSC/MFDA/IIROC allow titles to be used that mislead, misrepresent and which are not approved by the legislation? Whose interests are being served by this misrepresentation? Think about it. It is certainly not the consumer that is being protected by this misrepresentation. Follow the money as they say and the money goes straight from the consumer/customer/investor to the industry! And where are all the lawyers and professional accountants who are well employed in the OSC/MFDA/IIROC who know first hand that you use the approved title or else major sanctions will be immediately imposed on your creativity?

Shameful conduct by the regulators of this “tightly regulated industry”. Is the relationship not a bit too cozy, too tight? I mean when was the last OSC consultation with consumers? If memory serves me well, it was hosted at the CBC Toronto building years ago. What kind of balance and accountability is that?

Please feel free to contact me if there are any questions on my submission.

Permission to publicly post is granted.

Sincerely.
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former Sales Person/Dealing Representative
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