April 28, 2025

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
Office of the Superintendent of Securities, Newfoundland and Labrador
Office of the Superintendent of Securities, Northwest Territories
Office of the Yukon Superintendent of Securities
Ontario Securities Commission
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island

Me Philippe Lebel
Corporate Secretary and Executive Director, Legal Affairs
Autorité des marchés financiers
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The Secretary
Ontario Securities Commission
20 Queen Street West
22nd Floor, Box 55
Toronto, ON M5H 3S8 Fax: 416-593-2318
comments@osc.gov.on.ca

Dear Sirs/Mesdames:

Re: Canadian Securities Administrators (CSA) Proposed Amendments to National Instrument 81-105 Mutual Fund Sales Practices and Proposed Changes to Companion Policy 81-105 Mutual Fund Sales Practices – The Principal Distributor Model

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About Portfolio Strategies Corporation

Portfolio Strategies Corporation ("PSC") is a Calgary-based dealer, member of the Canadian Investment Regulatory Organization, registered mutual fund dealer and exempt market dealer in

British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Quebec, New Brunswick, Nova Scotia, Newfoundland and Labrador, Prince Edward Island and the Northwest Territories, and investment fund manager in Alberta and Ontario.

Comments

We think it is fair to say that most of us in the investment industry, and many consumers were shocked to find out that the nationwide DSC or manufacturer paid commission ban from the CSA in June 2022 did not actually apply to principal distributors or potentially the dominant bank players. Discussions regarding the DSC ban and chargeback options took place over many years with submissions from both industry and consumer advocacy groups. We were led to believe that this was an outright ban of DSC or similar manufacturer paid commissions, and that there were no exceptions or exemptions. In our opinion the CSA has been unusually silent in this regard. We are also wondering if the DSC or chargeback option, or manufacturer paid commission option, was properly disclosed to investors in the mutual fund "fund facts". As far as we know the "client focused reforms" and DSC ban did not grant any exemptions to principal distributor funds.

We feel quite strongly that if the DSC and chargeback options, or similar payments, were banned for the vast majority of retail wealth advisors, they should be banned completely and not just most of the way. Chargeback options and manufacturer paid commissions incentivize principal distributor advisors to keep clients invested in poor performing proprietary funds, until the chargeback period expires. This is a massive conflict of interest which the CSA flagged back in 2023, so why are they still permitted today?

Along these same lines principal distributors should be required to give mandatory disclosures to their clients or prospects that other competing products may be available elsewhere with better historical performance and at a lower cost. All commissions paid to dealers by mutual fund manufacturers should also be clearly disclosed.

Banks as principal distributors have material conflicts of interest and they have been well documented over the years. In addition to offering critical banking services to consumers they offer other services such as investments, credit cards, loans, lines of credit and mortgages – all subject to cross selling or tied selling, which is supposed to be illegal. Banks have refused to admit that tied selling is happening, responding that they are merely offering consumers discounts on other products or services if they consolidate their accounts at that same bank. That is clearly not the case when a bank manager or loan officer tells a small business owner that they can't get a loan or mortgage at that bank at a reasonable rate unless they move their RRSPs and other investments to them. That is coercion, plain and simple, if the business owner feels that they have no choice in the matter. Aggressive sales practices at banks have been well publicized in the media for many years, even prompting the OSC/CSA to investigate such practices. Selling clients overpriced products and services that consumers don't need, according to bank employees that have gone public about this, are clearly a conflict of interest and not in the client's best interest. Banks reduce competition, potentially offer reduced investment returns from a lack of competitively priced options or restricted product shelves (the exact opposite of the Ontario task force's intended outcome). This continuing bank domination of our industry is not in the consumer's best interest, so why does the CSA sit on their hands and do nothing about it? And why has the OSC report on bank's restricting their product shelves not been made public?

Other "non bank" principal distributors have similar conflicts of interest when they sell proprietary mutual funds that earn the dealers a manufacturer paid commission from certain mutual fund companies. The incentive to keep retail wealth clients invested in underperforming proprietary mutual funds presents the same conflicts as the chargeback option – the dealer or advisor do not want to pay back commissions to the manufacturer if clients redeem their mutual funds before a set period of time has elapsed.

We feel quite strongly that Principal Distributors should be restricted to a single mutual fund family. In almost all cases, Principal Distributors can't be trusted to offer better, lower cost investment options alongside their proprietary funds. The temptation to attract clients with award winning funds, only to end up selling clients a proprietary fund in the end, is a typical "bait and switch" strategy. This will lead to more client confusion. A manufacturer paid commission or chargeback DSC option in a proprietary fund versus a no chargeback DSC or manufacturer paid commission option is a huge conflict of interest.

Another important issue that the CSA needs to consider regarding proprietary funds is that banks and other Principal Distributors may not allow "in kind" transfers out to other dealers, without disclosing this negative sales practice to new clients. This could lead to adverse income tax consequences for clients if they are forced to crystalize capital gains at an inopportune time, when their stated preference was to retain the original fund at a non Principal Distributor dealer to get better service or advice. Further, large transfer out fees are similar to DSC fees. These negative sales practices need to be clearly disclosed in the Fund Facts or other sales documents.

Finally, there is a statement in this request for comment that exemptions may be granted in the future if the proposed amendments don't fit with a Principal Distributor's business model. We find this statement to be quite puzzling. A retail client's best interest is paramount and should always come first.

Answers to specific consultation questions

1. *The Proposed Amendments clarify that a principal distributor cannot have multiple principal distributor relationships except where it acts as principal distributor for mutual funds in the same mutual fund family. Are there any circumstances under which a dealer should be permitted to act as a principal distributor for more than one mutual fund family? In responding, please explain the advantages and disadvantages of such a model as compared to a participating dealer model for both investors and market participants. In particular, please outline the specific benefits for investors as they pertain to competition, cost and investor choice. Please provide quantitative data, where relevant, to support your answer.*

   Yes, a dealer may act as a principal distributor for more than one mutual fund family if the families are related through common ownership. We see no specific benefits for investors, as competition remains limited.

2. *If your answer to question #1 was yes, please also comment on the following:*
   (i) *What are the specific circumstances under which a principal distributor should be allowed to act for more than one mutual fund family?*

A principal distributor should only be allowed to act for more than one mutual fund family when the families are related through common ownership.

(ii) *If a principal distributor could act for more than one mutual fund family, should the compensation arrangements between the principal distributor be required to be the same or substantially similar in respect of each mutual fund family? If not, how could we ensure that any compensation arrangement differences would not influence a principal distributor to favour the mutual fund family with the most favorable compensation structure?*

Yes, if a principal distributor could act for more than one mutual fund family, the compensation arrangements between the principal distributor should be required to be the same or substantially similar in respect of each mutual fund family.

(iii) *What factors and considerations would be relevant to determining the appropriate number of mutual fund families for which a dealer should act as principal distributor? Explain how the distinction between principal distributors and participating dealers does not become blurred as the number of mutual fund families distributed by the same principal distributor increase.*

The number should be limited to one or two mutual fund families to ensure that principal distributor advisors can stay informed. Limiting this also helps maintain a clear distinction between principal distributors and participating dealers.

(iv) *Should there be minimum duties and obligations owed by the principal distributor in respect of each principal distributor relationship? Should those obligations be the same across all mutual fund families for which the dealer acts as principal distributor?*

Principal distributors should meet minimum duties, including standard KYC and KYP requirements, for each relationship. Yes, the obligations should be the same across all mutual fund families for which the dealer acts as principal distributor.

(v) *Should mutual funds that have a principal distributor be exclusively distributed by the principal distributor and not be distributed by other principal distributors or participating dealers?*

No, mutual funds should not be exclusively distributed by one principal distributor. Allowing all dealers access promotes a level playing field and increases competition.

3. *Do the Proposed Amendments fully address potential investor protection concerns for existing principal distributor business models and any foreseeable new mutual fund distribution business*

models? Are there any other considerations, limits or factors about a principal distributor arrangement that we should consider?

No, the proposed amendments don't fully address investor protection concerns. DSC and chargeback options, along with manufacturer-paid commissions, must be terminated to align with other distribution models.

4. *The Proposed Amendments to NI 81-105 will come into force 18 months after the final publication date. Does this provide sufficient time for dealers that act as a principal distributor for more than one unaffiliated manager to transition their practice, operational model and compensation arrangements? Does this provide sufficient time for impacted investment fund managers to make alternate distribution arrangements for their mutual fund securities prior to the effective date? If not, please explain.*

   Yes, 18 months provides sufficient time for dealers acting as principal distributors for multiple unaffiliated managers to transition their practices, operational models, and compensation arrangements. It also does provide sufficient time for impacted investment fund managers to make alternate distribution arrangements for their mutual fund securities prior to the effective date.

5. *Some principal distributors may currently use chargebacks. Chargebacks involve a compensation practice where a representative is paid upfront commissions and/or fees from the dealer when their client purchases securities. Chargebacks occur when investors redeem their securities before a fixed schedule as determined by the dealer, and the dealing representative is required to pay back all or part of the upfront commission/fees to the dealer. In June 2023, the CSA announced that it would be reviewing the use of chargebacks in the mutual fund industry due to concerns about potential conflicts of interest associated with this practice. The CSA is of the view that the use of chargebacks raises a significant conflict of interest for principal distributors in the distribution of mutual fund securities and we are considering the appropriate regulatory steps. We are requesting additional feedback on this practice.*

   We agree that the use of chargebacks present significant conflict of interest issues for retail mutual fund clients. The incentive to keep clients in underperforming fund families, to avoid paying back commissions, is simply too great as the dealer's or advisor's best interests are put before the client's best interests.

If you would like to talk about any of the points we have raised in a future discussion, please contact me at [redacted]

Yours Truly,

[redacted]

Mark S. Kent, CFA, CLU
President & CEO