Federation of Mutual Fund Dealers
Fédération des courtiers en fonds mutuels

October 23rd, 2020 VIA EMAIL ONLY

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Dear: Sirs/Mesdames,

Re: CSA Consultation Paper 25-402 *Consultation on the Self-Regulatory Organization Framework*

The Federation of Mutual Fund Dealers ("Federation") has been, since 1996, Canada's only dedicated voice of mutual fund dealers. We currently represent dealer firms with over $124 billion of assets under administration and greater than 24 thousand licensed advisors that provide financial services to over 3.8 million Canadians and their families. As such we have a keen interest in all that impacts the dealer community, its advisors, and their clients.
We appreciate the opportunity to submit our comments on these important issues. We have combined targets and consultation question comments together under the respective 'Issues" headings.

General

- The current regulatory environment is seen as ill-suited to fundamental changes in the needs and expectations of investors. In particular, the current regulatory environment is seen as siloed and as not lending itself well to investors looking for a consolidated and seamless service experience.

- The Paper states, "In addition to each SRO having equal numbers of industry and independent board members, both IIROC and the MFDA have industry advisory committees that serve as a forum for advising the SROs on regulatory and policy initiatives, industry trends and practices, as well as voicing industry concerns directly to the regulators." The industry advisory committees should not be

grouped together as their relationship with their SRO, structure and reporting are very different. At IIROC there is independence from the SRO, there is transparency and accountability.

- The Paper also said, "SRO staff have developed specialized skills and expertise in their roles, assisting them in delivering oversight of the industry." The Federation has commented previously that more and ongoing staff education is required to ensure that staff do in fact develop and maintain the skills and expertise necessary in the execution of their roles.

- There can be no true investor confidence in the regulatory system unless there is distribution of disgorged funds to harmed investors nationally. It is vital to the trust and confidence people have in the capital markets and in a regulator's enforcement capabilities.

- The cost of regulation is perceived to trickle down to the investor, but it is small book investors who are viewed as being at greatest risk of being negatively affected by regulatory burden. Dealers suggested that the effect of regulatory burden - as evidenced by compliance costs associated with audits, technology platform updates and human resources requirements – drives firms to focus on clients whose books generate sufficient fees to fulfil regulatory requirements and meet the cost of business operations.

- We look forward to a discussion on the role and responsibilities that an investor obligates themselves to upon initiating a relationship with an investment professional. For example, exhibiting a modicum of effort towards acting in alignment with their financial plan, and pursuing some measure of self-education regarding their investments. Currently investors benefit financially from ignorance because admitting to being financially knowledgeable could very well limit potential compensation and reimbursement from losses (not related to market losses). The 'reasonable person' standard should also apply to the investor; complete financial ignorance is not 'reasonable'.

- We would suggest that a metric for regulatory success be developed. The impact of the regulators should not be underestimated or ignored.

- We note our agreement with the Capital Markets Modernization Taskforce[1], in particular;
    1. Term limits for key appointments
    2. A dispute resolution avenue for dealers who have issues with their SRO. We add that could include the provincial regulator, without adding a new regulatory body.

Issue 1: Duplicative operating costs for dual platform dealers

We think that the Issue as stated above would be more accurately drafted as *Overall regulatory cost for all dealers, inclusive of dual platform dealers*.

We think that Targeted Outcome: "A regulatory framework that minimizes redundancies that do not provide corresponding regulatory value". would be more inclusive as *A regulatory framework that provides the lowest possible cost to all industry participants, while providing the maximum regulatory benefit to all investing Canadians.*

Contributing factors to duplicative costs include:
1. The requirement to print anything.
2. An SRO mandating the posting of letters out to all clients when an advisor has a compliance issue with one client.
3. System upgrades to accommodate promotional items tracking of pens and ball caps.
4. Operationalizing CFR conflicts.

There should be no instances where duplicative costs are necessary and/or warranted.

Issue 2: Product-based regulation

The Targeted Outcome as written is, "a regulatory framework that minimizes opportunities for regulatory arbitrage, including the consistent development and application of rules." We would suggest this be expanded to include "including the ongoing development of rules, and a harmonized application of those rules."

We would suggest that the industry would be better served by a blended approach, product and advice-based regulation. This would enhance robust future regulatory development around the oversight and alignment of commissions, advice, product distribution, and investor protection across all categories.

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[1] See https://www.ontario.ca/document/capital-markets-modernization-taskforce-consultation-report-july-2020/21-improving-regulatory-structure Self-regulatory organizations (SROs), 3. Strengthen the SRO accountability framework through increased OSC oversight

With respect to product arbitrage, since the formation of the MFDA there has been a slow but consistent migration from mutual funds to segregated funds and of those advisors giving up their mutual fund licenses. We realize that while segregated funds are not currently, viewed as securities, we feel it's important to continue to remind everyone that this is still an issue.

Issue 3: Regulatory inefficiencies

The Targeted Outcome states "A regulatory framework that provides consistent access, where appropriate, to similar products and services for advisors and investors." We think a definition of "where appropriate" would be beneficial.

We would agree with previous commenters who suggested that the CSA's costs would be reduced if there was only one SRO.

With respect to ETFs specifically, the Federation has been working with the industry broadly since 2005 in an effort to find a workable solution(s) to the processing, technology and market access challenges facing an MFDA dealer if their advisors want to sell ETFs. We have had some success; however, it seems that an elegant solution remains elusive. To-date there has been no will to facilitate a change that would remove some market exclusivity over the product.

Regarding regulatory inefficiencies, we would like to point out that the differing interpretations discussed in the Paper are not limited to inter-organizations, they apply to each organization internally and regionally. This is problematic.

MFDA Members are being held to a standard we believe is unreasonable, the standard that Members comply with the MFDA's published "recommendations". It has long been believed in the industry, and by CSA Members that "recommendations" were, as defined, "a suggestion or proposal as to the best course of action". If a dealer achieves what is intended by the recommendation, their own solution should be acceptable.

With respect to handling issues that span multiple registration categories we would suggest that for the benefit of the client, the integrity and efficiency of the industry, cooperative agreements between financial services regulators should be a requirement. Had these been in place, the largest application to the MFDA's Investor Protection Fund likely would have been avoided.[2]

Issue 4: Structural inflexibility

[2] See https://www.albertasecurities.com/News-and-Publications/News-Releases/2018/10/Alberta-Securities-Commission-Sanctions-W-H-Stuart-Mutuals-Ltd--M-Dianne-Stuart-W-Howard-Stuart and https://mfda.ca/mfda-investor-protection-corporation/w-h-stuart-mutuals-ltd/

We acknowledge the succession-planning challenges that IIROC dealers have in recruiting MFDA advisors and their frustration with the 270-day rule. As food for thought, here is what the OSC published in 2007 when they were asked by the IDA to remove the 270-day rule:

"The Commission has considered the suggestion to remove the 270 Day Requirement and decided not to do so at this time. The purpose of the temporary status of 'restricted representative' is to facilitate the transition of newly hired IDA salespersons who already have qualifications appropriate to the sale of mutual funds into fully qualified IDA salespersons. The effect of combining [the removal of the cap on the number of mutual fund only salespeople permitted at full-service dealerships] with the removal of the 270 Day Requirement would be to change the purpose of having restricted representatives at IDA members. It would become possible for individuals hired as restricted representatives to remain so indefinitely, allowing IDA members to have unlimited numbers of representatives qualified only to deal in mutual funds. However, as our securities regulatory system is presently structured, it is the role of the MFDA to act as the self-regulatory organization (the SRO) for firms and individuals whose dealer activities are limited to sales of mutual funds. The consequences of removing the 270 Day Requirement would be to permit a business model that would be inconsistent with the design of the existing regulatory system. Also, if a sufficient number of the MFDA's larger members were to transfer their operations to IDA affiliates, the ongoing viability of the MFDA could be undermined. We therefore believe that it is appropriate to maintain the 270 Day Requirement until such time as the roles of these SROs in our regulatory system is re evaluated."

If you determine to maintain two SROs, we recommend that any proposed rule changes go through the appropriate comment processes. Know, that should you eliminate the 270-day requirement, or allow IIROC advisors to redirect commissions to corporations, should you continue to blur the lines between the SROs and thereby the channels, the IIROC channel will erode the MFDA channel. While we can't speak for all stakeholders, we know that diminishment would not be productive for the industry or the investing public.

The current regulatory framework lags industry innovation, it is reactive. Being slow to acknowledge financial advice as a profession is one example. Changing the proficiency requirement for Liquid Alternative products is another.

With respect to equal access to advice for all investors, including rural or underserved communities, the Paper acknowledges that in those communities a client would likely find an MFDA rather than an IIROC advisor. The issue seems to be access to a wider variety of products rather than advice. There are online options so long as the client has access. Canada is not equal everywhere when it comes to technology.

You asked how changes in client preferences have impacted the business models. Clients want to be able to see all their investments on one statement, they would like to deal with just one advisor for all of their financial services needs. They want to be able to deal with their advisor remotely, especially at these times.

Regarding the Targeted Outcome "A flexible regulatory framework that accommodates innovation and adapts to change", there should always be an open door to industry participants with regulators when it comes to discussing ideas for the future. Without this collaboration the regulator becomes a barrier to entry, an inhibitor to progress and an agent not acting in the best interests of investors or the industry serving them.

Issue 5: Investor confusion

In the Targeted Outcome "a regulatory framework that is easily understood by investors and provides appropriate investor protection", 'easily understood' would benefit from additional clarity. Investors generally do not know what a regulatory 'anything' is beyond the desk of their advisor, so 'easily understood' needs defining.

The entire industry would benefit from a definition of "investor protection".

- The client assumes that somehow, they're going to get their money back (regardless of the reason for any loss).
- Regulators hope they're preventing harm and punishing harmful acts.

While on the home page on every regulatory site there are instructions on how to make a complaint, the same information is readily available on all dealer and advisor sites and is provided to every client individually. However, this information is only important to a client when they need it, and when they do, they usually don't remember where to go. It would be helpful if someone were to publish a flow chart, i.e. complaint to advisor → works, great; doesn't work → dealer → works, great; doesn't work, MFDA… → OBSI → Civil suit. Keep it simple.

Regarding investors' awareness of investor protection funds, they know when the advisor tells them, and it's a positive. However, when it's needed will they remember? Do they know how to access that as opposed to the other avenues available? Our industry is complicated to navigate.

Issue 6: Public confidence in the regulatory framework

With respect to the Targeted Outcome "A regulatory framework that promotes a clear, transparent public interest mandate with an effective governance structure and robust enforcement and compliance processes":

- The public can only have confidence in something it knows exists.
- A 'framework' alone is not a sufficient target. The framework must be supported by the resources required.

- "Effective" governance seems a low bar when we are including transparency, fair representation, oversight, etc.
- We deserve a moderate, reasonable, discussion-comes-first culture of compliance in the interest of investors and a healthy marketplace. We agree that it's important to have strong compliance processes, but we struggle under an enforcement culture.

Issue 7: Separation of market surveillance from statutory regulators

The Targeted Outcome "an integrated regulatory framework that fosters timely, efficient access to market data and effective market surveillance, to ensure appropriate policy development, enforcement and management of systemic risk" is sound but in considering the separation above, it would be valuable to understand the rationale for the current structure. A tremendous amount of resources were directed into the IDA/RS merger. We would like to understand what, in practice, isn't working.

In conclusion, we again thank the CSA and individual regulators for engaging in this consultation on SRO Review. We look forward to the further development of an intentional framework that integrates and streamlines the many disparate aspects of advice and securities regulation across the country in the most cost effective and frictionless manner we can achieve collaboratively.

While the creation of a single SRO model solves many of the issues the entire industry faces generally, the myriad details and specific needs particular to the different channels will be an enormous challenge to integrate and differentiate between; to balance the enhancement of each and the whole in a manner that fosters a fair and competitive marketplace, through a prism of investor protection. We support the CSA in this process and remain available to discuss these issues in further detail and look forward to opportunities to do so.

Regards,

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