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January 12, 2007

Secretary  
New Brunswick Securities Commission  
85 Charlotte Street, Suite 300  
Saint John, NB  
E2L 2J2

Dear Secretary,

**Re. Recognition of Mutual Fund Dealers Association as a Self Regulatory Organization in New Brunswick**

Advocis welcomes the opportunity to provide its comments on the consultation paper concerning the granting of recognition to the Mutual Fund Dealers' Association of Canada (MFDA) as a Self-Regulatory Organization (SRO) in New Brunswick, released on November 9, 2006.

Advocis, the Financial Advisors Association of Canada, is a national professional association that is committed to preparing, promoting and protecting financial advisors in the public interest. We do this by providing a professional platform including career support, designations, best practices direction, education, timely information and professional liability insurance. This strengthens the relationship of trust and respect between financial advisors and their clients, the public, and government. Advocis is Canada's largest association of financial advisors, representing life and health insurance licensees, and mutual fund and securities registrants across the country for over a century.

The consultation paper seeks responses to four broad areas of consideration related to the proposed Terms and Conditions of Recognition of the Mutual Fund Dealers' Association of Canada as a Self-Regulatory Organization for Mutual Fund Dealers ("Terms and Conditions") as stated in Schedule A, which are addressed in turn. Any comments regarding rules impacting MFDA members and their Approved Persons are in reference to the most current MFDA Rules document dated December 1, 2006, unless otherwise specified.

**1. Recognition of the MFDA in the public interest:**

Advocis believes that it is important for securities regulation to be harmonized, streamlined and modernized across Canada, with an objective of creating a flexible, administratively efficient regime with reduced regulatory burden. Currently, a number of provincial jurisdictions across Canada recognize the MFDA. In general, member firms apply compliance policies and procedures that currently meet MFDA requirements in all jurisdictions they are operating in, regardless of whether the MFDA is formally recognized as the SRO. As a result, financial advisors registered to

distribute mutual funds are already complying with these rules, in addition to the rules in their respective province's securities legislation and corresponding regulations. Therefore, in principle, Advocis is not opposed to formally recognizing the MFDA in the Province of New Brunswick.

Notwithstanding the above, Advocis continues to engage the MFDA on regulatory matters to ensure consumers are adequately protected, either through enhanced investor protection or the strengthening of public confidence in the Canadian mutual fund industry. Our goal is to ensure that rules actually enhance consumer protection and are developed in such a way as to minimize the costs of compliance. Furthermore, we are encouraging all regulators to consider principles based regulation, where possible, as a viable alternative to prescriptive rules in the regulation of financial services intermediaries. Given the already significant degree of prescriptive regulation found in the Securities Act and in rules of the recognized SROs, principles based approaches to regulation in various areas need to be seriously contemplated at this juncture.

On this front, Advocis has been following, with great interest, the Canadian Securities Administrators (CSA) Registration Reform Project, which is intended to harmonize, streamline and modernize the registration regime across Canada. An integral part of the CSA's Registration Reform Project is the implementation of various elements of the previously proposed Fair Dealing Model, which was introduced originally in 2004 by the Ontario Securities Commission. The proposal came under heavy criticism at that time as being too complex, introducing a substantial number of new rules, and demonstrating little benefit to consumers. The initiative has been recently renamed the Client Relationship Model, but our understanding is that its intent remains the same – creating an enhanced rules based regulatory regime impacting financial planning professionals where well-established accreditation standards already exist.

In its Proposal on Registration Reform – Part II (July 31, 2006), the CSA states that the regulators will clarify requirements relating to how registrants deal with clients and documentation provided to a client such as the general duty to act honestly, fairly and in good faith; know your client obligations; and duty to assess suitability of investments. It is our understanding that these aspects of market conduct oversight will be implemented through a more onerous, rules-based regulatory regime, and that the MFDA has been given a mandate to introduce some of these concepts by way of new or modified rules for its members and their Approved Persons.

We fail to understand why securities regulators are considering moving to an even more prescriptive regulatory system in these specific areas of market conduct. Advocis believes that prescribing rules regarding the relationship between financial planning professionals and consumers imposes an external framework for the regulation of advice givers. The definition of the skills and specific knowledge necessary to deliver professional financial planning advice to the public should be the responsibility of professional standard-setting institutions. We believe that proposals being contemplated by the CSA and the SRO working groups to implement the Client Relationship Model are contrary to raising the professionalism of financial advisors and minimize the attributes of financial planning designations. This does not promote the best interests of consumers.

In addition, Advocis is of the view that the potential layering of more rules and regulations governing how financial advisors interact with their clients may be contrary to the objectives set out in Section 10 of the proposed Terms and Conditions, which states, in part:

#### 10. PURPOSE OF RULES

(A) The MFDA shall, subject to the terms and conditions of its recognition and the jurisdiction and oversight of the Commission in accordance with securities legislation,

establish such rules as are necessary or appropriate to govern and regulate all aspects of its business and affairs and shall in so doing:

- (iii) seek to promote public confidence in and public understanding of the goals and activities of the MFDA and to improve the competence of members and their Approved Persons;
- (iv) seek to standardize industry practices where appropriate for investor protection;

It is important regulations are designed in such a manner as to ensure that they are appropriate, necessary, and consumers receive meaningful information, which is not overly complex in the investment decision making process. Our concern is that the Client Relationship Model may be moving in the opposite direction, which is contrary to promoting public confidence.

While we intend to provide formal comments to the CSA on its Registration Reform Rule, expected in early 2007, we would also appreciate the opportunity to provide comments directly to the New Brunswick Securities Commission on any proposed changes to MFDA Rules to implement elements of the Client Relationship Model. We address this issue in more detail below in the section dealing with the approval and rejection process of MFDA rules.

With respect to Terms and Conditions sub-section 7(B) regarding periodic review of members' Approved Persons we would encourage the New Brunswick Securities Commission to coordinate with the MFDA for the purpose of eliminating or reducing duplication of reviews in order to ensure that the compliance burden of financial advisors is kept to a minimum. Moreover, Advocis would appreciate being apprised of the standard that will be set by the Commission regarding the frequency of reviews of Approved Persons.

## **2. Suspension of MFDA Rule 2.4.1 pertaining to incorporated salespersons:**

At the release date of the Terms and Conditions, the suspension of MFDA Rule 2.4.1 in the Provinces of British Columbia, Saskatchewan, Ontario and Nova Scotia was scheduled to expire on December 31, 2006. Since then, the Securities Commissions in these provinces have extended the suspension period to December 31, 2008. In its recognition of the MFDA, we encourage the New Brunswick Securities Commission to suspend Rule 2.4.1 and allow for incorporation of mutual fund sales representatives to coincide with the suspension period accepted by other provinces, ending December 31, 2008.

While suspending the Rule during this period will allow advisors to operate their businesses through corporate entities, provided all other conditions are met, the suspension period has always been intended as a transition period towards a more permanent solution. A permanent policy will instill greater certainty in the industry and will allow incorporation (personal corporations) to continue to be an acceptable business structure in conducting securities related activities. Subsection 14(A) of the Terms and Conditions states that the Commission intends on working towards the development of amendments to applicable securities legislation to allow an Approved Person to carry on securities related business within the meaning of MFDA rules through a corporation while preserving that Approved Person's and the mutual fund dealer's liability to clients for the Approved Person's actions. However, Advocis believes that Subsections 14 B) through E) are sufficient to satisfy any concerns the Commission may have regarding liability issues, which require the member and Approved Person to adhere to all existing MFDA rules and policies. Specifically, MFDA members and Approved Persons adhere to MFDA Bulletin MR-0002

Payment of Commissions to Non-Registered Entities, which states that commissions can be paid to a corporation if (Section 2):

(a) the Member and its Approved Persons agree, and cause any recipient of commissions on behalf of Approved Persons that is itself not registered as a dealer or salesperson to agree to provide the Member, the applicable securities commission and the MFDA with access to its books and records for the purpose of determining compliance with the rules of the MFDA and applicable securities legislation. A sample form of agreement is attached as Schedule “A” hereto; and

(b) the Member complies with all of the other MFDA Rules in effect. The transition period for Rule 2.4.1 does not diminish the Members’ and Approved Persons’ obligations and responsibilities to comply with all of the other MFDA Rules.

In particular, Members will have to structure their relationships with Approved Persons to comply with Rule 1. For instance, where a Member conducts business through Approved Persons acting as agents, the Member must still comply with Rule 1.1.5, which requires the Member to have a written agency agreement with its Approved Persons confirming the Member's responsibility to supervise the Approved Person and confirming the Member's liability for the actions of the Approved Person relating to the Member's business. Therefore, regardless of the remuneration arrangement between a Member and an Approved Person, the Member is responsible and liable for the actions of its Approved Person in accordance with the MFDA Rules.

We believe that this forms the basis of a permanent approach to allowing for incorporation of mutual fund representatives, while ensuring consumers are adequately protected. At present, a significant number of mutual fund advisors in Canada use corporate structures to simplify administrative costs, tax and estate plan and facilitate business expansion, which do not impede regulatory scrutiny of their business or shield them from any obligations or liability to clients. These business practices have been undertaken in the absence of legislative requirements. Under current suspension of MFDA Rule 2.4.1 in the four provinces noted above, dating back to 2001 in some cases, we are not aware of any major issues or concerns related to instances of an Approved Person escaping direct liability to his or her clients while operating under a personal corporation business structure.

### **3. Business models that support distribution of mutual funds despite lack of MFDA membership:**

One of the key aspects of the CSA Registration Reform Project is to review existing registration categories with a view to streamline and harmonized firm categories. It is our understanding that all jurisdictions, including New Brunswick, are in the process of reviewing their local categories and determining if there are justifiable reasons for keeping them. Within the context of business models that support the distribution of mutual funds outside of MFDA membership, we have been working closely with the British Columbia Securities Commission (BCSC) over the past few years to introduce the independent-owner operator (IOO) registration category, which the BCSC has endorsed in principle. As a member of the CSA, we encourage the New Brunswick Securities Commission to consider our proposal within the context of the Registration Reform Project and its own registration category review initiative.

Advocis’ proposal would introduce a registration category owned and operated by registrants that will act solely as intermediaries for direct trades between clients and mutual fund managers, deposit-

taking institutions and life insurance companies, similar in nature to that which currently exists in the insurance licensing regime. As its key principles, the IOO would meet appropriate standards with regards to financial planning advice and the suitability of any products sold. As self-supervised for regulatory compliance purposes, it must have at least five years recent continuous experience as a mutual fund and life insurance licensee with the corresponding proficiency and continuing education requirements. Consumers would easily identify advisors holding out as professionals through recognized designations and would have the benefits of enhanced protection through mandatory errors & omissions liability insurance.

The main features of the IOO proposal are provided in the attached letter to the CSA Registration Reform Project secretariat. We would be pleased to provide you with additional details regarding our proposed model.

#### **4. Approval / rejection process of MFDA rules, by-laws, practices and policies:**

Section 11 of the Terms and Conditions (Rules and Rule Making) sets out procedures the MFDA must follow in changing or introducing new rules. While sub-sections A) through E) outline the duties of the MFDA as it relates to advising and seeking formal approval of the New Brunswick Securities Commission, it does not provide any guidance regarding how key stakeholders and the public in general can provide input on public policy matters prior to the development and approval of rule changes. Notwithstanding any formal procedures the MFDA may have within its by-laws in soliciting stakeholder input regarding the introduction or changes to its rules and the procedures in notifying the Commission of such rule changes, Advocis strongly believes that the New Brunswick Securities Commissions should seek public input independently prior to accepting material changes or introduction of new rules impacting Approved Persons, such as the ones currently being contemplated under the proposed Client Relationship Model. Only then can the New Brunswick Securities Commission ensure that that formal recognition of the MFDA continues to be in the public's best interest.

As for how the Commission should notify the public about the approval/rejection of an MFDA Rule, we believe that all registered advisors need to be apprised of changes and that the Commission could issue a newsletter or bulletin to registrants for this purpose, along with an accompanying press release, where deemed necessary. This would complement any public release procedural policies of the MFDA regarding rule changes.

We would be pleased to meet with you to discuss any or all of our comments with you in more detail, and look forward to working with the New Brunswick Securities Commission to ensure that the regulatory framework is modern, efficient and adequately protects consumers.

Sincerely,



Steve Howard  
President & CEO