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March 23, 2007

Donald G. Murray  
Chair  
Manitoba Securities Commission  
500 - 400 St. Mary Avenue  
Winnipeg, Manitoba  
R3C 4K5

Dear Mr. Murray,

**Re. Incorporation of Licensed Salespersons**

We are writing to provide you with our comments in follow up to the meeting of November 27<sup>th</sup> with Advocis representatives regarding incorporation of licensed salespersons.

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 oldest and largest voluntary professional membership association of financial advisors representing life and health insurance licensees, and mutual fund and securities registrants across the country.

As you are aware, mutual fund advisors in some provinces including British Columbia, Saskatchewan, Ontario and Nova Scotia are permitted to receive the payment of commissions into an incorporated entity, while in Manitoba this is not formally permitted. Most recently, the province of New Brunswick is considering allowing incorporation of individual mutual fund licensees as part of its recognition order of the Mutual Fund Dealers Association (MFDA).

This inter-jurisdictional inconsistency creates an uneven playing field across Canada and is a clear disadvantage to Manitoba advisors. It also creates a noted disparity between how commissions from the sale of insurance products and commissions from the sale of mutual fund products may be received, as insurance regulators permit insurance commissions to be paid into a corporation.

Incorporation is a modern and efficient business structure that offers many practical advantages. A significant number of mutual fund advisors across Canada use corporate structures for business purposes such as tax planning, as well as providing more efficient succession planning and business expansion by easing administrative costs.

Canadian securities legislation generally does not permit incorporated entities, or ‘sales companies’ to register for the purposes of making trades in securities. Many provincial securities acts define a “salesperson” as an individual who is employed by a dealer for the purpose of making trades in securities. The word “individual” does not include an incorporated entity and sales companies do not fall within the definition of “salesperson”. Within the four provinces referenced above, the MFDA is formally recognized by the respective securities commissions. Incorporation of mutual fund licensees has been permitted since 2001 through suspension of MFDA Rule 2.4.1 (*Remuneration, Commissions and Fees – Payable by Member Only*), which is now scheduled to expire on December 31, 2008 after it was recently extended for another two years.

Now that the issue of incorporated representatives resides with the Canadian Securities Administrators (CSA) as part of its overall Registration Reform Project, and is being contemplated for all securities registrants across Canada, it is important that securities regulators work towards a permanent solution. The CSA had indicated early in 2006 in its initial proposal regarding registration reform that it was seriously considering the removal of barriers to individual representatives who wish to carry on their businesses through a personal corporation for tax and estate planning purposes subject to various conditions and subject to resolution of issues relating to liability. We believe that it is important that the CSA develop a permanent solution as it committed to do so in its *Proposed National Instrument 31-103 Registration Requirements* (February 2007).

As an initial step, we encourage the Manitoba Securities Commission (MSC) to explore options to provide mutual fund licensees the ability to incorporate and have commissions paid into personal corporations to put Manitoba mutual fund licensees on equal footing with mutual fund advisors in other provinces. Given that the Manitoba Securities Commission does not formally recognize the MFDA as a self regulatory organization, suspending Rule 2.4.1 is not an option to achieve this objective. However, other viable options exist under the direct market conduct oversight of the MSC that would allow for incorporation.

Advocis believes that rules which currently exist under the MFDA regulatory regime can be adopted and applied analogously in Manitoba to effectively allow for incorporation. Specifically, in the four provinces that currently suspend Rule 2.4.1, MFDA members (dealer firms) and Approved Persons (mutual fund sales representatives) 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 (*refer to MFDA MR-002*); 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 an acceptable approach to allowing for incorporation of mutual fund representatives, while ensuring consumers are adequately protected. The key criteria for allowing incorporation would include:

- Dealer firm is registered with the MSC;
- Registered mutual fund licensee, acting as an agent (representative) of the dealer, would have a written agency contract in place with the dealer;
- The dealer has the responsibility to supervise the sales representative and confirms the dealer's liability for the actions of that representative relating to the dealer's business, making the dealer responsible and liable for the actions of its representative; and
- The MSC retains the right to have access to the books and records of the registrant for the purposes of assessing compliance with securities laws.

As part of this approach, we would also point you to the Province of British Columbia, which has provided greater direction to its registrants by issuing a companion instrument under the British Columbia Securities Act (*Instrument 32-503 Registration Exemption for Salespersons' Corporations*). The rule specifically exempts a corporation from the registration requirement provided that the corporation and the dealer have a written contract under which the dealer is liable for the acts and omissions of the corporation relating to securities business.

As the CSA continues to examine potential legislative amendments to provincial securities acts to permit all advisors to carry on securities related activities through incorporated entities, Advocis believes that any new rules or requirements should not constrict current practices in respect of the type of corporate structures currently in existence. At present, a significant number of mutual fund advisors in Canada use general purpose personal corporations to operate their businesses. Under suspension of MFDA Rule 2.4.1, we are not aware of situations where mutual fund licensees operating through these corporate structures have impeded regulatory scrutiny of their business or shielded themselves from any obligations or liability to clients. These business practices have been undertaken in the absence of legislative requirements within the MFDA regulatory regime. As the MSC and, more generally, the CSA contemplate this issue further, it is important to allow for significant flexibility with respect to the type of corporate structures permitted.

We would be pleased to meet with you to explore this issue further and to address any questions you may have. Furthermore, we would like to take the opportunity to share with you our initial views regarding the CSA's *Proposed National Instrument 31-103 Registration Requirements* and the implementation of the Client Relationship Model. In the mean time, should you have any questions, please do not hesitate to contact me.

Regards,

A handwritten signature in black ink, appearing to be a stylized name, possibly 'A. D.', written in a cursive style.