



July 31, 2019

Delivered By Email: pward@mfd.ca

Paige Ward
General Counsel, Corporate Secretary and Vice-President Policy
Mutual Fund Dealers Association of Canada
121 King St. W., Suite 1000
Toronto, Ontario M5H 3T9

Dear Ms. Ward:

RE: MFDA Bulletin #0782-P – Proposed Amendments to MFDA Rule 2.3.1(b) (Discretionary Trading)

The Investment Funds Institute of Canada (**IFIC**) appreciates the opportunity to comment on the proposed amendments to MFDA Rule 2.3.1(b) (Discretionary Trading).

IFIC brings together 150 organizations, including fund managers, distributors and industry service organizations, to foster a strong, stable investment sector where investors can realize their financial goals. IFIC operates on a governance framework that gathers member input through working committees. The recommendations of the working committees are then submitted to the IFIC Board of Directors, or board level committee, for direction or approval. This process results in a submission that reflects the input and direction of IFIC's members.

IFIC commends the MFDA for its efforts to be flexible and responsive to the needs of its Members and for taking steps to encourage innovation. We support the objectives of the proposal and agree that allowing limited discretionary trading activity within a mutual fund model portfolio is beneficial to clients.

Our comments and observations focus on five key areas:

- Regulatory Consistency
- Interaction Between Securities Legislation and the MFDA rules
- Mutual Fund Model Portfolio Framework
- Registration and Proficiency
- Regulatory Burden Reduction

Regulatory Consistency

IFIC continues to advocate for regulatory consistency and has commended the MFDA for its recent efforts to align its rules with equivalent IIROC rules.

The proposed amendments intend to achieve, on a more limited basis, what is already permitted for IIROC Members under IIROC rules. However, the proposed amendments are more restrictive in that they require an MFDA Member to either register under securities legislation as a restricted portfolio manager or receive an exemption from such registration.

In contrast, IIROC regulated firms and dealing representatives can rely upon the exemption from adviser registration under National Instrument 31-103 *Registration Requirements, Exemptions and Ongoing*

Registrant Obligations (NI 31-103), provided they comply with the IIROC rules. The applicable IIROC rules outline the framework for conducting discretionary activity, as well as the proficiency and experience requirements for individuals registered to conduct or supervise discretionary activity. As such, any relief from the adviser registration requirement provided to MFDA Members will need to outline the framework, proficiency and experience requirements that are absent in the proposed amendments.

Conversely, if MFDA Members are required to register as a restricted portfolio manager under securities legislation, it will result in duplicative regulation.

While we appreciate that a flexible approach has been taken in the proposal, IFIC believes that relief from registration as a portfolio manager, similar to the relief that has been granted to IIROC registrants, is the better approach. Relief from registration will help achieve regulatory clarity by having a single regulatory oversight body.

Interaction Between Securities Legislation and the MFDA Rules

As described, the proposed amendments allow discretionary trading in mutual fund model portfolios, subject to an MFDA Member being registered as a restricted portfolio manager under securities legislation or receiving an exemption. The proposal does not, however, provide a clear understanding of how the CSA intends to accommodate the proposed amendments within the securities regulatory framework. If the MFDA proceeds with the proposed approach, it will be important to ensure regulatory expectations are clear and not duplicative.

In drafting NI 31-103 the regulators gave consideration to exempting MFDA Members from a number of requirements in favour of equivalent MFDA provisions. Under the proposed amendments neither NI 31-103 nor the equivalent MFDA provisions, adequately contemplate an MFDA Member that is also registered as an adviser under securities legislation. One such example is capital requirements that consider an MFDA Member that is also registered as an investment fund manager, exempt market dealer or scholarship plan dealer, but does not consider an MFDA Member that is also registered as a portfolio manager or restricted portfolio manager.

Requirements that should be reviewed include working capital, insurance, complaints and custody requirements.

Mutual Fund Model Portfolio Framework

The proposal references OSC Staff Notice 81-708 *Model Portfolios of Mutual Funds (81-708)*, which provides information regarding the administration and expected disclosure requirements for mutual fund model portfolios. However, 81-708 pre-dates major regulatory initiatives such as the implementation of NI 31-103, point of sale delivery obligations and the Client Relationship Model Part 2 (**CRM2**).

The MFDA should consider issuing updated guidance to help inform a framework for the administration of mutual fund model portfolios and the related documentation. Some considerations for an updated mutual fund model portfolio framework include:

Definition of a Model Portfolio

The term “model portfolio” is used frequently in the securities industry without the benefit of a regulatory definition to ensure a common understanding of what a model portfolio refers to.

The proposal describes a very restrictive form of model portfolio program. While this kind of program may be common, it is not the only type of model portfolio program in the industry. Model portfolio programs may or may not use a questionnaire and scoring system to determine the most appropriate model portfolio for a client. Model portfolios may also be originated by an individual adviser and implemented centrally by the dealer. It is also important to note that technology has evolved significantly and can now accommodate a variety of customizations.

If the proposal is going to limit discretionary trading to a mutual fund model portfolio program, a regulatory definition is necessary to provide clarity.

Managed Accounts and Exemptions

The definition of managed account in NI 31-103 is “an account of a client for which a person or company makes the investment decisions if that person or company has discretion to trade in securities for the account without requiring the client’s express consent to a transaction”. Implicit in the definition is that discretionary authority must be granted to the person or company in an agreement.

The proposed amendments require MFDA Members to describe the extent of the discretionary authority that will be exercised in the mutual fund model portfolio in their relationship disclosure document, but do not require the client to grant authority through a form of managed account agreement. In contrast, the IIROC framework specifically requires a managed account agreement thus clearly enabling IIROC Members to rely on a number of regulatory exemptions, including:

- an exemption from pre-sale delivery of Fund Facts; and
- an exemption from pre-trade disclosure of charges.

We again believe the IIROC approach works well, therefore MFDA Members should obtain the same level of client instruction as is required by IIROC Members through a managed account agreement.

Registration and Proficiency

Registered Representatives of a Restricted Portfolio Manager

The proposal indicates Approved Persons will be expected to meet the proficiency requirements set out in securities legislation. However, NI 31-103 is silent on these requirements. While the registration and proficiency requirements for an advising representative and a Chief Compliance Officer of a portfolio manager are set out in the instrument, the registration and proficiency requirements for individual registrants of a restricted portfolio manager are not specified. The Companion Policy guidance with respect to relevant investment management experience is equally silent.

IFIC would appreciate clarification regarding the proficiency and experience requirements that will be required for advising representatives and the Chief Compliance Officer under the proposal.

We would also like to note that the bulletin setting out the analysis of the proposal suggests that discretionary trading in mutual fund model portfolios should be limited to fund substitutions and changes to portfolio asset allocations. IFIC believes that the restrictions set out in the bulletin are unnecessary provided the individual registrants that carry out discretionary trading on behalf of the member satisfy the proficiency and experience requirements of an advising representative of a portfolio manager.

Associate Advising Representative

Securities legislation includes an individual registration category for an associate advising representative of a portfolio manager. Similarly, the proposed plain language rewrite of the IIROC Dealer Member Rules includes a registration category for an Associate Portfolio Manager.

We would appreciate confirmation that the proposal intends to allow an individual registration category of associate advising representative, in addition to an individual registration category of advising representative, of a restricted portfolio manager.

Regulatory Burden Reduction

Relief from Registration Requirements

IFIC applauds the MFDA for taking steps to reduce the regulatory burden associated with establishing a mutual fund model portfolio program. This proposal will allow members to engage in limited discretionary trading directly, removing the need to either establish a separate legal entity registered as a portfolio manager or engage the services of an external portfolio manager. As previously stated, IFIC believes the most appropriate way of facilitating limited discretionary activity is to provide relief from registration as a portfolio manager, similar to the approach that has been taken by IIROC. Providing relief will ensure that efforts to reduce regulatory burden are not offset by increasing regulatory complexity and costs through dual registration, oversight and duplicative requirements.

Compliance Examinations and Requests for Information

Absent relief from registration, dually-registered MFDA Members will be subject to compliance examinations and requests for information from both the MFDA and the CSA. If relief from registration as a portfolio manager is not provided, we expect that the MFDA and the CSA will work collaboratively to minimize regulatory duplication and burden on members who offer mutual fund model portfolio programs.

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IFIC is fully supportive of the objectives of the proposal. We look forward to working with the MFDA to help advance this initiative.

We would be pleased to provide further information or answer any questions you may have. Please feel free to contact me by email at mupadhyaya@ific.ca or, by phone 416-309-2314.

Yours sincerely,

THE INVESTMENT FUNDS INSTITUTE OF CANADA



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