CFA Societies Canada

Canadian Advocacy Council
120 Adelaide Street West, Suite 2205
Toronto, ON M5H 1T1
+1 (416) 366 3658 tel
www.cfacanada.org

February 23, 2023

VIA EMAIL

Financial Services Regulatory Authority of Ontario
25 Sheppard Avenue West, Suite 100
Toronto, ON
M2N 6S6

Re: *Consultation on Proposed Amendments to the UDAP Rule – Deferred Sales Charges* **(the "Consultation")**

The Canadian Advocacy Council of CFA Societies Canada[1] (the "**CAC**") appreciates the opportunity to provide the following general comments on the Consultation, whereby FSRA is proposing to eliminate deferred sales charges ("**DSC**s") on new segregated fund contracts and place restrictions on the use of DSCs in existing contracts.

We support the proposed amendments to the Unfair or Deceptive Acts or Practices ("**UDAP**") Rule to ban sales of new individual segregated fund contracts that contain a DSC option effective June 1, 2023. We appreciate the consideration given to the broad nature of the ban, which will include amendments to individual variable insurance contracts where as a result, a reasonable person would believe that a DSC becomes less favorable to the insured person.

We agree that the ban will satisfy FSRA's stated purpose of limiting undesirable customer outcomes including unsuitable advice and unexpected fees. In particular, the concerns about the potential for conflicts of interest that may motivate insurance agents to recommend a DSC option even if it is not a suitable option for clients. In the past, we have also had strong concerns about the potential for regulatory arbitrage, given the similarities between certain insurance and securities products and agree that the harmonization of the DSC ban (to the extent possible) with those placed on mutual fund products through comparable changes to securities regulation is appropriate.

[1] The CAC is an advocacy council for CFA Societies Canada, representing the 12 CFA Institute Member Societies across Canada and over 19,000 Canadian CFA Charterholders. The council includes investment professionals across Canada who review regulatory, legislative, and standard setting developments affecting investors, investment professionals, and the capital markets in Canada. Visit www.cfacanada.org to access the advocacy work of the CAC.

CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion of ethical behavior in investment markets and a respected source of knowledge in the global financial community. Our aim is to create an environment where investors' interests come first, markets function at their best, and economies grow. There are more than 190,000 CFA Charterholders worldwide in 160 markets. CFA Institute has nine offices worldwide and there are 160 local societies. For more information, visit www.cfainstitute.org or follow us on LinkedIn and Twitter at @CFAInstitute.

120 Adelaide Street West, Suite 2205
Toronto, ON M5H 1T1
+1 (416) 366 3658 tel
www.cfacanada.org

We also were strongly supportive of the ban on DSCs for mutual funds that was imposed by the securities regulatory authorities last year. In our comment letters, we had noted that the mandate to put clients' interests first may often be in direct conflict with an adviser's compensation structure. The CAC views the current system of financial incentives associated with DSC products as driving sub-optimal behavior. Investors benefit from a structure of economic incentives that promotes transparent, simple fee structures, full attribution of all costs to the end-investor related to their financial advice, and a structure that promotes competition in the distribution of products to investors on the basis of product quality and value-for advice, rather than compensation to advisors.

With respect to individual segregated fund contracts with existing DSC options, we understand that new customer disclosure would be required in connection with new deposits under this option where the insurer does not otherwise have a right under the terms of the contract to remove that option altogether, with the disclosure being slightly different depending on whether the DSC option will remain a sales charge option. If the option is being withdrawn despite instructions to deposit funds under the option, the disclosure should need to be reasonably designed to help the insured choose a suitable alternative sales charge option.

While additional disclosure is helpful, we respectfully submit that the proposed disclosure does not go far enough to help customers truly understand the full cost of their available or chosen sales options, especially given the lack of on-going disclosure on intermediary compensation. As CFA Charterholders, we support rules that foster clear, transparent and comparable disclosure about the costs of investments and financial products. An example is the principles that guide performance disclosure under the Global Investment Performance Standards (GIPS®); fundamentally, that information should be calculated and presented "in a fair and comparable format that provides full disclosure".[2]

It is preferable that these changes are being proposed by way of amendments to the UDAP Rule rather than through guidance, as it is important for enforceability purposes.

While we note the emerging popularity of the 'Advisor Chargeback' option and its impact on lessening the direct fee obligations on a customer relative to a DSC option, we firmly believe that the use of this fee option does not mitigate but in fact compounds the conflict of interest issues in advice inherent in all upfront commission structures, and would urge FSRA to review this option for a ban as well at its earliest opportunity, consistent with our comments to CCIR and CISRO in November of 2022.

Concluding Remarks

We are strongly supportive of both amendments contained in the Consultation, and believe they should be implemented at the earliest opportunity. We think that all upfront compensation options (both DSC and Advisor Chargeback) raise inherent and material conflict of interest issues for advisors that are fundamentally not able to be addressed and resolved in the best interest of clients. We laud this regulatory action by

[2] CFA Institute, Global Investment Performance Standards (GIPS®) Handbook, 3rd ed (2012) at p. 2 (emphasis added). GIPS® is a registered trademark owned by CFA Institute.

FSRA to ban DSCs, and would urge further examination and a ban on the similarly conflict-causing Advisor Chargeback option.

We thank you for the opportunity to provide these comments and would be happy to address any questions you may have. Please feel free to contact us at cac@cfacanada.org on this or any other issue in future.

(Signed) *The Canadian Advocacy Council of*
CFA Societies Canada

The Canadian Advocacy Council of
CFA Societies Canada