FAIR | Canadian Foundation *for* Advancement *of* Investor Rights

April 30, 2012

Marsha Manolescu
Director, Capital Markets Policy
Alberta Finance and Enterprise
522 Terrace Building
9515 - 107 Street
Edmonton, Alberta T5K 2C3
Sent via e-mail to: marsha.manolescu@gov.ab.ca

Pierre Rhéaume
Ministère des Finances du Québec
Directeur général, Droit corporatif et politiques relatives au secteur financier
12, rue Saint-Louis
Québec, Québec G1R 5L3
Sent via email to: pierre.rheaume@finances.gouv.qc.ca

RE: Incorporation of Individual Representatives Project Update

Thank you for the opportunity to comment on the proposed model (the "Model") and supporting draft legislative amendments to securities legislation ("Legislative Framework") to allow for the incorporation of individual representatives of registered dealers and advisers, including individual registrants of group scholarship plans and exempt market dealers ("individual registrants") (the "Incorporation Project").

The Provincial/Territorial Council of Ministers of Securities Regulation (the "Council") approved this stage of the Incorporation Project in July 2011[1]. As well, on December 12, 2011, the Government of Saskatchewan introduced Bill 14, The Securities Amendment Act, 2011, which, if passed, will allow individual registrants of registered dealers and advisers to conduct registrant activities through a professional corporation in that province. Bill 14 received second reading on March 13, 2012 and is currently before the Standing Committee on Intergovernmental Affairs and Justice. The working group of provincial/territorial government officials (the "Working Group") of the Council is now seeking feedback on the Model and Legislative Framework.

FAIR Canada is a national, non-profit organization dedicated to putting investors first. As a voice of Canadian investors, FAIR Canada is committed to advocating for stronger investor protections in securities regulation. Visit www.faircanada.ca for more information.

FAIR Canada Comments and Recommendations – Executive Summary:

1. **FAIR Canada is opposed to the incorporation of individual registrants of registered dealers and**

[1] See Progress Report for the period January 2011 to December 2011 of Provincial/Territorial Council of Ministers of Securities Regulation (the "Council") at page 3.

advisers in Canada as it will weaken efforts to protect Canadians and will not further the essential mandate of securities regulation. It is essential that governments and regulators be the guardians of the public with respect to securities regulation. Allowing the incorporation of individual registrants will impede rather than help governmental and regulatory efforts to protect consumers.

2. Incorporation of individual registrants of registered dealers and advisers will result in a higher level of risk to Canadian investors and a lower risk to registrants themselves. This should not be countenanced by the Working Group, who, we believe, should shelve the Incorporation Project.

3. The fact that the majority of the responses to the Consultation Paper dated December 20, 2010 (the "Consultation") supported the adoption of a statutory incorporation model should bear little or no weight in the deliberations of governments as to whether to proceed with the Incorporation Project. Most Canadians would have been completely unaware of the 2010 consultation. Those who responded were mainly those who stand to benefit.

4. FAIR Canada notes that there appears to be an absence of any benchmarking to other jurisdictions such as the United States, the United Kingdom, or Australia in respect of allowing individual registrants to incorporate. There is no discussion as to whether other jurisdictions have considered allowing for the incorporation of individual registrants, and if so, the results of any such deliberations. We recommend that benchmarking to other jurisdictions be undertaken.

5. A number of significant investor protection problems with the existing framework of securities regulation have been identified which should be a higher priority for governments and regulators than the Incorporation Project. Reforms should focus on improving investor protection rather than changing business structures so as to reduce tax liability for registrants.

6. Allowing individual registrants to incorporate "professional corporations" would contribute to Canadian consumers' misunderstanding of the nature of the client-advisor relationship. Regulators and governments should not assist the financial industry in misleading consumers and helping them to profit from Canadians' trust. If consumers are told their "advisor" is a "professional corporation", this will further misrepresent the standard of care and the nature of the services provided and will exacerbate the misalignment of obligations and expectations.

7. FAIR Canada notes that professionals outside of the financial industry who have been allowed to incorporate, such as doctors and lawyers, are in a much different situation from individual registrants and maintain a fundamentally different relationship to their clients or patients. The comparisons are not apt.

8. The argument for a level playing field between registrants, and in particular between insurance agents who can incorporate and individual registrants on the securities side who cannot, should not allow for a "race to the bottom". Insurance regulators (in particular, the Canadian Council of Insurance Regulators) have become increasing concerned about possible regulatory gaps and risks to consumers given the evolution of the insurance distribution channel and are examining the various roles, responsibilities, accountabilities and level of oversight of insurance agents, Managing General Agencies ("MGAs") and insurers. **In light of the regulatory gaps and potential (or actual) harm to consumers that results, any move towards emulating such a structure should be strenuously opposed.**

9. **The fundamental issue is that the legal relationship that currently exists between the registered dealers/advisers and their individual registered representatives will not be preserved if those individual registrants are permitted to incorporate professional corporations. Incorporation**

fundamentally undermines the legal foundation of the relationship between the registered dealer/adviser and its individual registered representatives, as the current securities regulatory structure presumes the structure of an employer-employee or employee-agent relationship.

10. Incorporation, in our view, will fundamentally undermine the legal foundation of such a relationship.

11. FAIR Canada provides specific comments on the Model and the Legislative Framework below in section 8.

12. If the Incorporation Project nonetheless proceeds, it is essential to investor protection that the professional corporation be easily searchable in a comprehensive national registration database. In addition, if the Incorporation Project proceeds, FAIR Canada strongly recommends that it require that professional corporations be members of a self-regulatory organization ("SRO") (namely the Mutual Fund Dealers Association of Canada ("MFDA") or the Investment Industry Regulatory Organization of Canada ("IIROC") backed by a compensation fund and be required to participate in the Ombudsman for Banking Services and Investments ("OBSI"). The professional corporation should also be expressly liable for any fines levied by regulators or SROs on the individual registrant.

1. Incorporation of individual registrants will undermine consumer protection.

1.1. **It is FAIR Canada's submission that permitting the incorporation of individual registrants of registered dealers and advisers in Canada will weaken efforts to protect Canadians and will not further the essential mandate of securities regulation. It is essential that governments and regulators be the guardians of the public with respect to securities regulation. Allowing the incorporation of individual registrants will impede rather than help government and regulator's efforts to protect the investing public.**

1.2. Incorporation of individual registrants of registered dealers and advisers will result in a higher level of risk to Canadian investors and a lower risk to registrants themselves, as is explained below. This should not be countenanced by the Council, who, we believe, should shelve the Incorporation Project.

1.3. The fact that the majority of responses to the Consultation Paper dated December 20, 2010 (the "Consultation") supported the adoption of a statutory incorporation model should bear little or no weight in the deliberations of governments as to whether to proceed with the Incorporation Project. The overwhelming majority of responses were received from registrants and industry participants who stand to directly benefit should incorporation be allowed given that it would reduce the amount they would pay in tax and would result in limiting their potential liability. In no way can the responses constitute a statistical sample of the general Canadian population's opinion on the subject matter. Most Canadians would have been completely unaware of the 2010 consultation. Whether it is in the public interest, and in particular, whether it furthers the mandate of securities regulation to protect the investing public, is the essential question which must be addressed with respect to the Incorporation Project.

2. Benchmarking to other jurisdictions is required.

2.1. FAIR Canada notes that there is an absence of any benchmarking to other jurisdictions such as the United States, the United Kingdom, or Australia in respect of allowing individual registrants to

incorporate. There is no discussion as to whether other jurisdictions have considered allowing for the incorporation of individual registrants, and if so, the results of any such deliberations. **We recommend that benchmarking to other jurisdictions be undertaken and publicly disseminated prior to any further legislative action.**

3. Governments and securities regulators should focus on consumer protection priorities given problems with the existing framework of securities regulation.

3.1. The current statutory framework of securities regulation necessarily has come under increasing scrutiny and review as a result of a conflation of factors which include the global financial crisis, rapid capital market changes, increasing complexity and interconnectedness of markets and the increased reliance that is being placed on individual Canadians by governments to save for their own retirement needs. This has the consequence of increasing the number of Canadians who are invested in the capital markets, despite their low financial literacy. This scrutiny and review has revealed significant problems which should be a priority for governments and regulators and certainly should be addressed ahead of any initiative by governments to reduce the tax liability of individual registrants by allowing them to incorporate. **Reforms should focus on improving investor protection rather than changing business structures so as to reduce tax liability.**

3.2. Reducing tax revenues by allowing individual registrants to incorporate should not be a priority of Canadian governments, particularly in these times of austerity and budget cuts. **Safeguarding and improving the financial well-being of Canadians by protecting them from fraud and other wrongdoing, as well as from being sold products that are not suitable and do not meet their needs, should be the priority of governments.**

3.3. FAIR Canada strongly believes that the priority of governments and regulators should:

(1) institute a **best interest of the client standard** on those purporting to provide financial advice to Canadians, and

(2) improve the transparency of the relationship between the individual registrant and consumers by various measures. These measures need to include requirements regarding the reporting to consumers of the costs and performance of their investments (which have already been sold to them) and providing comprehensible disclosure of the key information needed to make a decision as to whether to purchase a given investment product, before it is sold to them.

3.4. FAIR Canada notes that recent research indicates that most Canadian investors believe that their "financial advisor" has a legal duty to put the client's best interests ahead of his or her own personal interests. **That is, most Canadian investors believe there is already a fiduciary duty imposed on their advisor**[2]. Canadian investors rely on their advisor for investment information and trust their advisor to provide advice that benefits the client first. Given their belief that the registrant will put the client's best interest first, investors find little reason to be concerned about fees and they often have little or no idea about the fees that they pay, or the amount their advisor

[2] Investor Education Fund "Investor behaviour and beliefs: Advisor relationships and investor decision-making study" written by The Brondesbury Group, Toronto, ON, 2012 at page 2. Available online at http://www.networkfso.org/Resolving-disputes-between-consumers-and-financial-businesses_Fundamentals-for-a-financial-ombudsman_The-World-Bank_January2012.pdf See also OSC Investor Advisory Panel submission on the OSC's draft Statement of Priorities at page 4. Available online at http://www.osc.gov.on.ca/documents/en/Securities-Category1-Comments/com_20110427_11-765_ananda.pdf.

gets paid, with fewer than half of advisors disclosing this information to them[3]. FAIR Canada believes that this impression that registrants have a duty to act in the best interests of the client can be attributed, at least in part, to advertising and marketing by the financial services industry designed to promote financial consumers' trust.

3.5. We believe that allowing individual registrants to incorporate "professional corporations" would further contribute to consumers' misunderstanding of the nature of the client-advisor relationship. Regulators and governments should not assist the financial industry in misleading consumers and helping them to profit from Canadians' trust when such registrants are only obligated to meet a suitability standard. If consumers are told their "advisor" is a "professional corporation", this will further misrepresent the standard of care and the nature of the services provided, thereby exacerbating the misalignment of obligations and expectations.

3.6. **FAIR Canada believes that the priority of the Council and regulators should be to propose a regulatory model that requires all market intermediaries to put their clients' interests first.** Other leading jurisdictions, particularly the U.S., the U.K. and Australia have made significant movements towards this type of standard. Canada is lagging behind in this important area of financial services regulation.[4]

4. Other professionals who have been permitted to incorporate owe a fiduciary duty to their clients and must meet higher proficiency standards.

4.1. Professionals outside of the financial industry who have been allowed to incorporate, such as doctors and lawyers, are in a much different situation from individual registrants and maintain a fundamentally different relationship to their clients. Such professionals must meet high educational and proficiency standards in order to gain entry to the profession and are subject to fiduciary obligations.

4.2. **Individual registrants currently are subject to minimal proficiency standards and are not subject to a fiduciary duty. For example, to sell mutual funds, one need only pass a course such as the Canadian Securities Course offered by the Canadian Securities Institute and one does not necessarily need a high school diploma.**

4.3. Individual registrants who are incentivized to sell products that benefit them financially at the expense of their clients should not be permitted to call themselves "professional corporations". The prerequisite qualifications that are required in order to sell financial products should be re-examined to determine whether higher standards are necessary in order to protect financial consumers. This should be a key priority for governments and regulators. The ability of registrants to support the financial literacy of their clients depends on the proficiency, knowledge and skills of the registrant. **Current proficiency standards are inadequate given the increasing complexity of**

[3] Investor Education Fund "Investor behaviour and beliefs: Advisor relationships and investor decision-making study" at pages 24-26 and page 34.

[4] The Ontario Securities Commission states in its draft Statement of Priorities for the financial year to end March 31, 2013 that it is re-evaluating the adviser-client relationship to consider whether an explicit statutory fiduciary duty or other standard should apply to all advisers and dealers in Ontario. The research underway will be completed, and a paper on the adviser's duty to clients will be prepared and published in consultation with the CSA, OSC Notice 11-766. Available online at http://www.osc.gov.on.ca/documents/en/Securities-Category1/sn_20120330_11-766_rfc-sop-2013.pdf.

financial products and the degree of unconditional trust and confidence that is placed by many consumers on the registrants they utilize.

5. Do not lower standards in an effort to level the playing field.

5.1. Industry groups such as Advocis (The Financial Advisors Association of Canada) have stressed the need to have a permanent, harmonized solution to allow for a level playing field between registrants, and in particular, between those who are insurance agents (who are allowed to incorporate) and those who are securities registrants. With respect, the distribution of insurance is structured very differently than the securities industry and such insurance agents (who may be incorporated) are subject to very minimal supervision and regulation which should not be emulated on the securities side. **The Incorporation Project should not level the playing field by reducing standards, which would result in a "race to the bottom".**

5.2. Insurance agents do not conduct their business through one dealer but rather can conduct their business through multiple MGAs and may conduct their business through more than one incorporated entity[5]. Insurance regulators have become increasingly concerned about possible regulatory gaps and risks to consumers given the evolution of the insurance distribution channel and are examining the various roles, responsibilities, accountabilities and level of oversight of insurance agents, MGAs and insurers. **In light of the regulatory gaps and potential (or actual) harm to consumers that results, any move towards such a structure should be strenuously opposed.**

6. The Model and the Legislative Framework must be assessed against certain principles.

FAIR Canada set out in its submission dated February 25, 2011 the principles against which a Model or Legislative Framework should be assessed against. These principles derive from the 1999 CSA Distribution Structures Committee Position Paper (the "Committee"). In particular, we consider the following principles to be critical in assessing the Model and the Legislative Framework:

1. **The dealer or adviser must be legally responsible for the acts of its individual registrants;**
2. **The dealer or adviser must exercise an appropriate level of supervision over its individual registrants;**
3. **All conflicts of interest must be disclosed to the client and the client must be aware of all of the types of investor protection that are available to the client; and**
4. **The dealer and regulators must be able to adequately perform their oversight function.**

6.2. IIROC's submission of February 25, 2011 also indicated its support for the Committee's principles and proposed the following additional principles which we also support:

[5] See Advocis submission dated April 8, 2011 Re CCIR Issues Paper at page 3. Available online at http://www.advocis.ca/regulatory-affairs/RA-submissions/2011/Resp-CCIR-Issues-apr8-11.pdf.

1. The individual registrant should be personally responsible for complying with individual registration requirements and regulatory obligations and should be personally responsible to the regulator for failures to comply; and
2. The individual registrant should only be allowed to achieve the tax efficiencies of incorporation in full compliance with all applicable laws.

As stated in its submission, "[a]ny incorporation model should be consistent with these principles, address the regulatory and accountability issues identified in the CSA Paper and ensure the protection of the investing public."[6]

7. The Model or Legislative Framework is incompatible with the fundamental nature of dealer and adviser regulation.

7.1. **The fundamental issue is that the legal relationship that currently exists between the registered dealers and advisers and their individual registrants will not be preserved if those individual registrants are permitted to incorporate professional corporations.** Incorporation fundamentally undermines the legal foundation of the relationship between the registered dealer and adviser and their individual registrants, as the current securities regulatory structure presumes the structure of employer-employee or employee-agent relationship.

7.2. **Currently, investors are protected from wrongdoing by individual registrants through their supervision by registered dealers and advisers.** Compliance at the individual registrant level is the responsibility of the registered dealers and advisers. It is the registered dealers and advisers that, by regulation, are: "…responsible for having a compliance system that promotes compliance by the firm and individuals with securities law."[7] Key to the entire system is the requirement for registered firms to "provide reasonable assurance that the firm and each individual acting on its behalf complies with securities legislation..."[8]

7.3. This is achieved since the individual registrants are employees, partners or agents of a registered dealer or advisor[9] and their acts are, in law, the acts of the registered dealer or adviser.

7.4. FAIR Canada believes that permitting the incorporation of individual registrants will fundamentally alter the relationship between registered dealers/advisers, individual registrants and their clients. Incorporation, in our view, will fundamentally undermine the legal foundation of such a relationship. For further details, refer to our earlier submission dated February 25, 2011.[10]

7.5. In the Model and the Legislative Framework, the relationship between the registered dealer and adviser and its individual registrants is fundamentally altered by allowing a "professional corporation" to insert itself between the registered dealer/ adviser and the individual registrant

---

[6] See IIROC's submission, dated February 25, 2011, online: <http://www.finance.alberta.ca/publications/other/2011-0225-rosemary-chan-iiroc.pdf>.

[7] See OSC Ongoing Requirements – Compliance System – Information for: Dealers, Advisers and Investment Fund Managers, online: <http://www.osc.gov.on.ca/en/Dealers_compliance-system_index.htm> (accessed April 30, 2012).

[8] National Instrument 31-103, s. 11.1(a).

[9] IIROC Dealer Member Rule 39 also allows employment and agency, but not any incorporated salespeople.

[10] FAIR Canada submission dated February 25, 2011. Available online at <http://faircanada.ca/wp-content/uploads/2011/01/CSA-incorporation_of_dealer_reps.pdf>.

for whom the dealer and adviser traditionally had responsibility and liability in respect of acts performed in the discharge of their duties.

8. Specific comments on the Model and the Legislative Framework.

Definitions and Legislative Provisions Demonstrate the Fictional Nature of the Relationships

8.1. The "professional corporation" is defined in the Legislative Framework as "a corporation that provides services as a dealer or adviser to clients through one or more RPC [registered professional corporation] representatives." **Why should an incorporated entity be permitted to "provide services as a dealer or adviser" while not having to maintain and comply with the current requirements imposed on registered dealers and advisers (i.e. capital adequacy and bonding requirements etc.)?** Any entity (in this case, the RPC) that employs a registered individual has traditionally had to be a registered dealer that meets capital adequacy and other securities requirements as a dealer. This will no longer be the case.

8.2. The definition of "RPC representative" in the Legislative Framework is strained. The definition provides that the RPC representative is "...an individual who provides services as a dealer or adviser to clients: (i) as a representative of a registered dealer or adviser acting on behalf of the dealer or adviser..." - this ignores the fact that there is an incorporated entity between that RPC representative and the registered dealer or adviser – and "...(ii) as an employee of or on behalf of a registered professional corporation" – this ignores the fact that the RPC representative is (or was) an employee of the registered dealer or adviser and has now inserted a corporate entity between the dealer and him or herself.

8.3. The fictional nature of the professional corporation is made clear upon examination of new section 37.1. This section asserts in subsection (2) that "[t]he legal relationship between an RPC representative and the dealer or adviser on whose behalf the RPC representative acts is not affected by the fact that the RPC representative provides services to clients through a professional corporation." **This attempts to ensure that the RPC representative is really an employee or agent of the registered dealer or adviser and the professional corporation is a fiction inserted between the two to attempt to avoid tax liability.** The problem is that despite the assertion in the statute, the corporation is a different legal entity than an individual and it will alter the fundamental nature of the legal relationship between the individual registrant and the registered dealer or adviser.

8.4. The statute also attempts to maintain the degree of control and supervision that the registered dealer and adviser has traditionally exerted over an individual registrant who is their employee or agent by the inclusion of subsection 37.1(3) which provides that "[a] dealer or adviser has the same legal authority over a professional corporation as the dealer or adviser has over the RPC representative who provides services to clients through the professional corporation." How can the dealer, which is a corporate entity, have the same amount of control and supervision (legal authority) over an unrelated corporate entity as it has over its own employees? Again, the assertion in the statute is at odds with the structure being created.

8.5. Most importantly, it is not clear that the fact that the corporation has been inserted into the relationship will maintain the same degree of legal liability that the individual registrant (now the RPC representative) has to the client, or the same degree of legal liability that the registered dealer

has to the client despite subsection 37.1(6) of the Legislative Framework which states "[t]he liability of an RPC representative to a client is not affected by the fact the RPC representative provides services to the client through a professional corporation" and subsection 37.1(7) which states "[t]he liability of a registered dealer or registered adviser to a client of an RPC representative is not affected by the fact that the RPC representative provides services to the client through a professional corporation." It is not clear that the statutory provisions will be determinative in the event of a dispute where a court would examine the legal relationships between the parties, the facts of the situation, the arguments of the parties as well as the Legislative Framework when determining liability.

8.6. Section 37.1 attempts to maintain the existing legal relationship between registered dealers and advisers and their registered representatives (individual registrants) who are their employees or agents. However, the legal relationship is, in reality, altered by the insertion of the corporation. If what is desired is what is set out in section 37.1 – to maintain the current set of legal relationships, responsibilities and liabilities, why allow the individual to incorporate? Why fundamentally change the relationship and then try to assert that you have not done so? The only rationale is the reduction of the tax liability of the individual registrants. This simply is not sufficient to justify putting investors at risk.

8.7. FAIR Canada strongly recommends that the Incorporation Project not be pursued. If it is, we strongly recommend that registered dealers and advisers be responsible for any fines levied on the registered professional corporation or the RPC representative in light of the fact that the flow of liability is weakened given the imposition of the corporation between the dealer and its representatives should this project proceed.

8.8. Despite the Legislative Framework, it is not clear that the goal of this project – reducing tax liability of individual registrants through incorporation – will be achieved given existing tax legislation and related jurisprudence. **It is quite possible that the CRA will deny the proposed tax benefits since they may very well run afoul of the "personal services business" rule or general anti-avoidance rule (GAAR) under the *Income Tax Act*.** The end result of the Legislative Framework could be to add a greater burden on securities regulators to "approve" the corporations through the process of allowing them to be registered and create a situation where individual registrants and/or their dealers can attempt to avoid liability to their clients and make compliance and enforcement of existing securities laws more difficult.

Restricting the Business to provide Securities-Related Activities

8.9. The Model and the Legislative Framework provide that the professional corporation must be a single-purpose vehicle restricted to providing only securities-related activities. Registration of the professional corporation will only occur if its articles of incorporation "restrict its business to engaging in the business of providing services as a dealer or adviser to clients."

8.10. FAIR Canada recommends that, if the Incorporation Project proceeds, the definition of "securities related activities" include "any business or activity….which constitutes trading or advising in any investment product…" and be drafted as broadly as possible to ensure it covers any investment product related activities. It should also ensure that all securities and investment product related activity, including marketing, selling and advising, is required to be conducted through a registered

dealer and adviser (other than the professional corporation).

8.11. Consumers have suffered losses at the behest of unsupervised outside business activities and there exists the potential for greater investor losses as a result of unsupervised outside business activity. FAIR Canada believes that not permitting securities related business to be conducted outside of the registered dealer/adviser would serve to protect the interests of financial consumers. This is necessary to protect investors so that:

- consumers being sold securities or investment products or advised with respect to securities or investment products by a RPC representative are protected by the controls, supervision and oversight of the registered dealer;
- to prevent client confusion;
- to appropriately address conflicts of interest; and
- to ensure that the investments of individuals who invest with a RPC representative are covered by a compensation fund.

8.12 Outside business activities that are not securities-related activities should not be allowed to be conducted by the RPC representative or their professional corporation

8.13 FAIR Canada believes that allowing incorporation will make it more difficult for registered dealers to supervise and police unapproved outside business activities and that this will increase risks to consumers.

One RPC Representative/One Professional Corporation

8.14 The Model and the Legislative Framework require securities regulators to "approve" the corporation after review to ensure that the articles of incorporation restrict the voting shares of the professional corporation so that it can be owned only by one or more RPC representatives and that the director of the professional corporation must be an RPC representative. The owner of the voting shares will be prohibited from pledging, entering into a voting trust, proxy or other type of arrangement vesting the right to exercise voting rights in another who is not a registered representative under securities laws.

8.15 **This imposes a large compliance burden on securities regulators given the large numbers involved and will require a considerable shift in resources or added resources in order to provide effective oversight.** FAIR Canada is concerned that securities regulators will not be able to provide effective oversight over this process in order to adequately protect investors. If they shift resources or add resources to provide adequate oversight, this will take resources away from other priorities of the securities commissions which have far greater importance than the Incorporation Project and should take precedence.

9. Essential that professional corporations be searchable in a national registration database.

9.1. If a professional corporation is registered, then it must be easily searchable in the national registration database. This will of course add complexity to any search by Canadians who wish to find out if the person or entity they are dealing with is registered and in good standing with the

regulators. Given the importance of dealing with a registrant and the potential losses that Canadians may suffer if they fail to do so (for example, Earl Jones defrauded Canadians of millions of dollars), it is essential that the professional corporation be easily searchable.

10. If the Incorporation Project proceeds, require SRO membership backed by a compensation fund.

10.1. If the incorporation project proceeds, despite the significant concerns noted above, incorporation should only be permitted for those registered dealing or advising representatives who are members of an SRO and backed by a compensation fund.

10.2. FAIR Canada has indicated its concern, in its recent submission[11] to the Canadian Securities Administrators ("CSA"), about the fact that many Canadians are being sold prospectus-exempt securities by exempt market dealers in reliance on the accredited investor exemption despite the fact that those investors do not qualify under the current criteria. The Ontario Securities Commission, in OSC Staff Notice 33-735, and the Alberta Securities Commission, in Staff Notice 33-704, identified a number of issues of concern relating to investors such as unsatisfactory suitability due diligence, know-your-client non-compliance, inadequate disclosure and failure to reasonably determine if the person is, in fact, an accredited investor and, therefore, does not need a prospectus to provide the investor with prospectus-related protections.

10.3. FAIR Canada has recommended that exempt market dealers that are performing investment dealer-like activities should be required to join IIROC and not be permitted to avoid SRO-level oversight given the lack of suitability inquiries, the lack of disclosure of the payments received by sellers when investors purchase the exempt market security and the many conflicts of interest that appear to be rife in this part of the market. We believe that this would result in better protection for investors through closer supervision and heightened compliance requirements, as well as insolvency coverage through a compensation fund such as the Canadian Investor Protection Fund.

10.4. **In light of the fact that the current system is already not adequately protecting investors, incorporation for exempt market dealers should not be permitted until such time as these other more urgent problems have been rectified. We would also suggest that such incorporation should not be permitted until such time as the exempt market dealers have become members of an SRO (namely IIROC or the MFDA) so that better supervision can occur (and thereby improve compliance with the existing securities regulations) and so that investors can obtain much-needed protection in the event of the insolvency of an exempt market dealer.**

11. If the Incorporation Project proceeds, require participation in OBSI.

11.1. All individual registrants who are permitted to incorporate should be required to participate in OBSI so that consumers have access to an independent, fair, accountable and efficient external dispute resolution provider in the event that a complaint is not resolved internally. Requiring participation in OBSI by all incorporated entities (including through the dealer that they must conduct all their securities-related business with) would allow the system to meet Canada's

[11] FAIR Canada, "RE: Review of Minimum Amount and Accredited Investor Exemptions" (February 29, 2012), online: <http://faircanada.ca/wp-content/uploads/2011/01/120229-FAIR-Canada-submission-re-MA-AI-exemptions.pdf>.

international obligations under the G20 High-Level Principles on Financial Consumer Protection[12].

We thank you for the opportunity to provide our comments and views in this submission. We welcome its public posting and would be pleased to discuss this letter with you at your convenience. Feel free to contact Ermanno Pascutto at 416-214-3443 /ermanno.pascutto@faircanada.ca or Marian Passmore at 416-214-3441/ marian.passmore@faircanada.ca.

Sincerely,

Canadian Foundation for Advancement of Investor Rights

[12] G20 High-Level Principles on Financial Consumer Protection, October 2011. In particular, Principle 9 requires that "Jurisdictions should ensure that consumers have access to adequate complaint handling and redress mechanisms that are *accessible, affordable, independent, fair, accountable, timely and efficient*….Recourse to an independent redress process should be available to address complaints that are not efficiently resolved via the financial services providers and authorized agents internal dispute resolution mechanisms." [emphasis added] Available online at http://www.oecd.org/dataoecd/58/26/48892010.pdf.