

Member Regulation Policy

Canadian Investment Regulatory Organization

Suite 2600

40 Temperance Street

Toronto, Ontario M5H 0B4

e-mail: memberpolicymailbox@ciro.ca

Disgorgement – Proposed Amendments to the Mutual Fund Dealer Rules

<https://www.ciro.ca/newsroom/publications/disgorgement-proposed-amendments-mutual-fund-dealer-rules>

The proposal to bring mutual fund dealers in line with investment dealers is a positive development. This will allow CIRO access to increased collected disgorged cash to deliver to harmed Main Street investors.

An issue with the program is that only the ill-gotten gains of the Dealer representative are recovered- the Dealer retains its share. When investors file claims they will not distinguish between the harm caused by the representative and the Dealer- their service Agreement is with the Dealer.

Edward Deming's classic work, particularly his "94% rule," posits that the vast majority of performance variation comes from the system. This includes the processes, tools, training, and management structures in place. Only a small percentage of the variation is due to individual deficiencies or negligence. Because management designs and controls the system, they are primarily accountable for its outcomes. So when a representative of the Dealer is before a Hearing Panel, the chances of Dealer accountability are virtually 100%.

Supervision failure can often be attributed to management compensation practices such as higher commissions for select products, monthly sales targets and commissions to supervisors based on their team's sales performance as well as poor employee training,

systems or equipment. The odds are very high that the root cause of mis-selling is traceable to Dealer management policies, practices, controls and processes.

The G21/OECD High level principles of financial consumer protection Principle 9 states: Financial service providers should also be responsible and accountable for the actions of their intermediaries. <https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/financial-consumer-protection/G20-OECD-FCP-Principles.pdf>

Indeed, Ontario Securities Commission CEO Grant Vingoe has been quoted as saying sales pressures and incentivization may be driving concerning behaviours in a recent report on mutual fund Dealers at bank branches.

CIRO's Guide How to make a complaint

(<https://www.ciro.ca/office-investor/how-make-complaint>) is very clear: "CIRO Members are responsible to you, the investor, for monitoring the actions of their advisors and employees to ensure that they comply with the by-laws, rules and policies governing their activities." Since CIRO Members are responsible for monitoring, it is basic logic that the Dealer is responsible when the monitoring fails to prevent harm to a client of the Member Dealer.

Therefore, the proposal should be made fair by holding the CIRO registered Dealers accountable for supervision that failed to prevent harm by their employees/ representatives. This money will be near 100% collectible, adding greatly to the disgorged pool of funds available to investors.

I recommend that CIRO find a mechanism to provide such a disgorgement process or proceed with enforcement actions against Dealers where supervision failed.

Having the Dealer disgorge ill-gotten gains will incent improved supervision and improve representative compensation practices to comply with the Client Focused Reforms. The long term result will be less money to disgorge because there will be less investor harm.

The initiative can be further enhanced by aggressively pursuing non-payers and seeking additional enforcement powers for collection.

An extra benefit of suggested changes will be that CIRO, as an industry self-regulator, demonstrating that it can act decisively against its Members when required.

As an aside, when disgorged money is transferred to investors, CIRO must ensure that investors are informed of their rights to claim for losses above the amount of disgorged funds provided.

Periodic reporting of the results from the disgorgement initiative will increase public awareness and engagement.

I appreciate the opportunity to provide an input on this important initiative.

Harvey Buksa