VIA E-MAIL

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Member Regulation Policy
Canadian Investment Regulatory Organization
Suite 2600, 40 Temperance Street
Toronto, Ontario M5H 0B4

memberpolicymailbox@ciro.ca

Trading and Markets
Ontario Securities Commission
20 Queen Street West, 22nd Floor
Toronto, Ontario M5H 3S8

TradingandMarkets@osc.ca

CSA Secretariat
Tour de la Bourse
2010-800, Square Victoria
Montréal (Québec) H3C 0B4

csa-acvm-secretariat@acvm-csa.ca

Market Oversight Alberta Securities Commission Suite 600 250-5th Street SW, Calgary Alberta T2P

CIRO-Reporting@asc.ca

Re: Rule amendments relating to the proposed adoption of an Incorporated Approved Person compensation option (CIRO Bulletin 26-0150)

The Portfolio Management Association of Canada (**PMAC**) appreciates the opportunity to provide comments to the Canadian Investment Regulatory Organization (**CIRO**) and the Canadian Securities Administrators (**CSA**) on CIRO's proposed rule amendments relating to the adoption of an Incorporated Approved Person (**IAP**) compensation option (the **Proposal**). While the Proposal is focused on CIRO Approved Persons, we direct our comments to the CSA as well, given the potential implications for the broader securities regulatory framework and other registration categories.

PMAC represents over 320 investment management firms registered to do business in Canada as portfolio managers (**PMs**) with the members of the CSA. PMAC's members encompass both large and small firms and manage total assets in excess of $4 trillion as fiduciaries for institutional and private client portfolios.

PMAC's mission statement is "advancing standards". We are consistently supportive of measures that elevate standards in the industry, enhance transparency, improve investor protection, harmonize regulation and benefit the capital markets as a whole.

Our key recommendations are set out below, followed by a more detailed discussion of our concerns.

KEY RECOMMENDATIONS

1. **Do not adopt the Proposal.** CIRO has not demonstrated that the anticipated benefits of a broader incorporated compensation regime justify its costs, regulatory and legislative complexity, potential investor-protection implications and industry disruption. Given these concerns and the significant competing demands on both CIRO's and the CSA's regulatory resources, we recommend that CIRO discontinue this initiative rather than devote further resources to its development and implementation.

2. **Address existing directed-commission issues directly and separately.** The existing directed-commission model is used by a relatively small segment of the industry and raises unresolved securities law, tax and registration concerns. If the objective is to harmonize compensation rules and create a level playing field, this can be achieved more directly by eliminating the directed-commission model across CIRO dealer members. Any existing arrangements that do not comply with applicable laws should be corrected or unwound without implicating the broader securities industry.

While we do not support proceeding with the Proposal, if CIRO and the CSA nevertheless wish to pursue incorporated compensation, we recommend that the following matters be addressed before any broader framework is adopted:

3. **Demonstrate a sufficient public-interest benefit.** CIRO has not demonstrated how the Proposal would improve investor outcomes, access to advice or capital-market efficiency. Its principal anticipated economic benefits would accrue to incorporated advisors, while the Proposal would impose additional costs and regulatory burdens on firms, which may be passed on to investors, and would increase investor-protection risks by complicating supervision, access to records and regulatory accountability.

4. **Resolve the tax-policy and tax-administration implications.** The anticipated economic benefits of incorporated compensation are fundamentally tax-driven, yet uncertainty remains regarding their availability and magnitude. If the Proposal is to be pursued, it is imperative that the relevant tax-policy, fiscal and administrative implications first be resolved. This should include obtaining written clarification from the Canada Revenue Agency and Revenu Québec regarding the tax treatment of payments to IAPs, firms' reporting and withholding obligations, and their potential exposure if that treatment is subsequently challenged.

5. **Assess implications across registration categories and business models.** We recommend that CIRO and the CSA consider the issue jointly from the outset, with a comprehensive assessment of the implications across registration categories and business models. A CIRO-only framework would place CSA-registered PM firms at a competitive disadvantage in recruiting and retaining investment professionals performing substantially similar activities. A coordinated approach would help ensure that any resulting framework appropriately accommodates different business models, avoids unjustified regulatory disparities and does not create opportunities for regulatory arbitrage. Any such assessment should also consider the additional supervisory obligations, information and access requirements, associated costs, and increased potential personal regulatory liability exposure of ultimate designated persons (each a **UDP**) and chief compliance officers (each a **CCO**).

Discussion

The Proposal builds on an inadequate model

The Proposal would replace the current directed-commission arrangement available to certain mutual fund dealing representatives with an IAP option for client-facing CIRO Approved Persons. In our view, the appropriate starting point is not whether all CIRO advisors should receive access to the same incorporation opportunity, but whether permitting advisor-owned corporations to receive compensation connected to registerable activity is warranted.

CIRO has identified concerns about the existing directed-commission arrangements, including whether corporations currently receiving directed commissions are limiting themselves to non-registerable activity. Where existing arrangements do not comply with securities or tax law, they should be corrected or unwound. Although transition may be onerous for affected individuals, the relatively small legacy population should not, without a demonstrated broader policy benefit, drive a fundamental redesign of compensation rules across the industry. Moreover, under the Proposal, affected mutual fund dealer Approved Persons would be required to transition from existing directed-commission arrangements in any event.

The benefits case, including the underlying tax assumptions, has not been established

The principal anticipated economic benefits of the Proposal are tax advantages for advisors who incorporate, rather than benefits to investors. Moreover, it is uncertain whether these tax advantages would materialize or how significant they would be. For example, the potential application of the personal services business rules under

the *Income Tax Act* could limit the anticipated tax benefits.[1] Even if some advisors benefit from incorporation, CIRO has not demonstrated how those private benefits would justify the broader costs, regulatory complexity and potential investor-protection risks associated with the Proposal.

The uncertainty regarding tax treatment also creates risks for sponsoring firms. Although participation would be voluntary, competitive pressures are expected to leave firms with little practical choice but to offer the option to recruit and retain advisors. Firms would therefore incur significant implementation and administrative costs, as well as potential financial exposure if the tax treatment of these arrangements is subsequently challenged, including regarding reporting and withholding obligations.

The Proposal could also have broader fiscal implications if widespread adoption affects federal or provincial tax revenues. These consequences warrant consideration by the relevant government authorities before any regulatory framework facilitating incorporated compensation is introduced.

While we do not support proceeding with the Proposal, if CIRO and the CSA nevertheless pursue incorporated compensation, it is critical that the tax implications be clarified before any framework is finalized. In particular, we recommend obtaining written clarification from the Canada Revenue Agency and Revenu Québec regarding the anticipated tax treatment of IAP arrangements, firms' reporting and withholding obligations, and their potential exposure if that treatment is subsequently challenged.

Broader costs and competitive effects need to be assessed

If adopted, the Proposal will impose significant operational and administrative costs on sponsoring firms and their advisors. For firms that currently employ their advisors, introducing an IAP option is expected to affect employment arrangements, pension participation, benefits, payroll and withholding obligations, and the allocation of responsibilities among the firm, advisor and corporation. These changes could also affect other team members whose employment, compensation, benefits or supervision are connected to the advisor's business. Advisors who incorporate would face additional legal, accounting and administrative costs to establish and maintain their corporations.

The Proposal also leaves important questions regarding client relationships unresolved. It is unclear how rights and responsibilities relating to client relationships, records, servicing arrangements and associated revenues would be allocated among the sponsoring firm, advisor and IAP, particularly when an advisor incorporates or

[1] *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.), subsection 125(7), definition of “personal services business”; Canada Revenue Agency, Fact sheet: Personal services business

leaves the firm. Existing agreements may need to be revised, and questions may arise regarding client disclosure, notification or consent. Beyond these contractual considerations, clients must clearly understand who is responsible for the services they receive, who they should contact if problems arise and what happens to their accounts if their advisor leaves the sponsoring firm. While firms may negotiate the commercial terms of their arrangements with IAPs, these matters cannot be left entirely to private agreements where they affect regulatory accountability, client rights and investor protection.

The additional corporate layer would also introduce supervisory complexity, raising questions about the standard of reasonable supervision applicable to sponsoring firms and the information and access rights necessary to meet their regulatory obligations. Firms, including their UDPs and CCOs, would need to oversee IAP activities, obtain necessary records, monitor ownership arrangements involving family members, trusts or other non-registrants, and ensure that non-registrants do not receive compensation connected to registerable activity. These responsibilities could become particularly burdensome for firms supervising numerous separately incorporated entities, each with its own ownership, governance, financial arrangements and records. The associated compliance costs and supervisory challenges would increase with the number of IAPs. This additional complexity will impede effective supervision and make it more difficult to establish accountability when problems arise, increasing investor-protection risks and the potential personal regulatory liability exposure of UDPs and CCOs.

Incorporated compensation should not be considered in isolation from other registration categories

We acknowledge the CSA's indication that comments on the Proposal may inform consideration of a harmonized approach for other registrants. However, the possibility of future harmonization does not address the competitive disparities that would arise from introducing an incorporated compensation framework for CIRO Approved Persons without first considering its implications for other registration categories. In some cases, PM firms may compete with CIRO member firms for investment professionals and private-client mandates, and their registered individuals may perform substantially similar investment management and advisory activities. A CIRO-only framework would give CIRO member firms an additional, potentially tax-advantaged compensation option that PM firms could not offer, placing them at a competitive disadvantage in recruiting and retaining talent. In our view, substantially similar activities should not be subject to materially different compensation frameworks without a demonstrated regulatory justification.

The Proposal's focus on client-facing registrants also raises particular concerns for PM businesses. The distinction between client-facing and non-client-facing activities does

not necessarily reflect the roles performed by advising representatives. For example, an advising representative may manage portfolios while also maintaining client relationships, with responsibilities spanning separately managed accounts, investment funds and institutional mandates. Other advising representatives may perform substantially similar investment management activities with little or no direct client interaction. It is therefore unclear why eligibility for incorporated compensation should depend on whether an individual is characterized as client-facing rather than on the nature of the registerable activities performed.

These concerns further support our recommendation that CIRO not proceed with the Proposal. If incorporated compensation is nevertheless pursued, we recommend that CIRO and the CSA consider the issue jointly from the outset, across all relevant registration categories and business models, rather than developing a framework for CIRO Approved Persons that may subsequently be extended or adapted for other registrants. This would allow the policy rationale, appropriate scope and competitive implications to be assessed consistently across the securities regulatory framework before any framework is adopted.

Comparisons with the U.S. and other professions are not determinative

CIRO refers to approaches in other professions and jurisdictions, but those comparisons require caution. The 2025 U.S. Securities and Exchange Commission staff no-action position, followed by FINRA guidance in 2026, permits broker-dealers to pay transaction-based compensation to registered representative-owned personal services entities only under detailed conditions. Among other things, the owners and registered personnel must be registered with the same broker-dealer, the entity's location must be a branch or office of supervisory jurisdiction, and the broker-dealer remains responsible for supervision and records. That framework is tied to the U.S. broker-dealer model and does not extend to discretionary advisory activity. It therefore cannot, on its own, establish that the broader Canadian registration, fiduciary and compensation issues have been resolved.

Comparisons with other professions, such as lawyers and physicians, also have limitations. While those professions permit certain forms of professional incorporation, they operate under different regulatory, governance and supervisory frameworks. In particular, the securities regulatory framework requires an individual registrant to operate through a sponsoring firm that remains responsible for supervision and compliance, with specific regulatory responsibilities assigned to individuals such as the firm's UDP and CCO. Introducing a separate incorporated entity into that relationship would create significant supervisory challenges and increase the exposure of the sponsoring firm, UDP and CCO.

The fact that incorporation can be accommodated within another profession's framework therefore does not establish that it can be readily accommodated within the securities regulatory framework.

Regulatory resources should be directed toward higher-priority initiatives

We question whether the Proposal represents an appropriate use of limited regulatory resources at a time when CIRO, the CSA and the industry face significant competing priorities. Geopolitical uncertainty, economic pressures, concerns about the competitiveness of Canada's capital markets and rapid technological change are creating significant challenges for regulators and market participants alike. CIRO's recent cybersecurity incident further underscores the importance of prioritizing fundamental regulatory responsibilities, including cybersecurity, operational resilience and the protection of investors and market integrity.

By contrast, the Proposal would require significant regulatory and legislative changes, impose substantial implementation costs on firms and introduce additional supervisory complexity, without a demonstrated corresponding public-interest benefit. In our view, the resources required to develop and implement such a framework would be better directed toward initiatives that address more pressing regulatory risks and demonstrably advance investor protection and market integrity.

CONCLUSION

For these reasons, PMAC recommends that CIRO not proceed with the Proposal. If the objective is to harmonize compensation rules and create a level playing field, this could be achieved more directly by eliminating the directed-commission model.

If CIRO and the CSA nevertheless wish to consider incorporated compensation further, we recommend that they do so together from the outset, across relevant registration categories and business models. Any broader reform should proceed only if supported by a clear, evidence-based case demonstrating that the anticipated benefits, including meaningful public-interest benefits, justify the costs, regulatory complexity and industry disruption. The tax treatment and related policy implications must also be resolved, and the supervisory and operational implications fully assessed, before any framework is adopted.

If you have any questions, please contact Katie Walmsley (kwalmsley@pmac.org) or Victoria Paris (vparis@pmac.org). We would be pleased to discuss our comments and recommendations further.

Sincerely,

PORTFOLIO MANAGEMENT ASSOCIATION OF CANADA

"Katie Walmsley"

Katie Walmsley
President

"Geoff Grove"

Geoff Grove
Co-Chair
Industry Regulation & Tax Committee

Chief Compliance Officer and Head of Compliance for Latin America, BlackRock