

### 13.3 Clearing Agencies

#### 13.3.1 FundSERV Inc. – Notice and Request for Comment – Application for Recognition as a Clearing Agency

##### NOTICE AND REQUEST FOR COMMENT

##### FUNDSERV INC.

##### APPLICATION FOR RECOGNITION AS A CLEARING AGENCY

#### A. Background

On March 1, 2011, subsection 21.2(0.1) of the *Securities Act* (Ontario) (OSA) came into force which prohibits clearing agencies from carrying on business in Ontario unless they are recognized as a clearing agency or are exempt from the requirement to be recognized by order of the Ontario Securities Commission (Commission).

FundSERV Inc. (FundSERV) has applied (the Application) to the Commission for recognition as a clearing agency pursuant to section 21.2 of the OSA.

FundSERV offers electronic business services to the investment industry. FundSERV's core service is its infrastructure for the placement and reconciliation of orders for mutual funds. Centralized payment exchange facilities are available to its participants and for those who choose, to settle orders, on a net basis, through payment exchange currently handled by a Canadian chartered bank through the Large Value Transfer System operated by the Canadian Payments Association.

In assessing the Application, staff followed the process set out in OSC Staff Notice 24-702 - *Regulatory Approach to Recognition and Exemption from Recognition of Clearing Agencies* (OSC Staff Notice 24-702).

#### B. Draft Order

In the Application, FundSERV has addressed the applicable criteria for recognition as a clearing agency. Subject to comments received, staff will recommend that the Commission grant a recognition order with terms and conditions to FundSERV based on the proposed draft recognition order (Draft Order) that is attached as Appendix A to the Application.

FundSERV provides limited clearing agency functions related to the centralized payment exchange facilities. The business model of FundSERV, however, does not involve many features engaged in by other clearing agencies and central counterparties such as credit enhancement, the assumption of counterparty risk, netting, novation or custody. Consequently, the limited clearing agency functions pose little systemic risk. The Draft Order is, therefore, tailored to FundSERV's circumstances and imposes requirements that are proportional to the level of risk and the level of activities engaged in by FundSERV. It requires FundSERV to comply with the following terms and conditions relating to:

1. Governance
2. Fees
3. Access
4. Rules and Rulemaking
5. Due Process
6. Risk Management
7. Systems and Technology
8. Financial Viability and Reporting
9. Outsourcing
10. Information Sharing and Regulatory Reporting

#### C. Comment Process

The Commission is publishing for public comment the Application and Draft Order. We are seeking comment on all aspects of the Application and Draft Order.

You are asked to provide your comments in writing and delivered on or before April 1, 2012, addressed to:

c/o John Stevenson, Secretary  
Ontario Securities Commission  
20 Queen Street West  
Suite 1903, Box 55  
Toronto, Ontario M5H 3S8  
E-mail: [jstevenson@osc.gov.on.ca](mailto:jstevenson@osc.gov.on.ca)

We request that you also submit an electronic copy of your submission. The confidentiality of submissions cannot be maintained as a summary of written comments received during the comment period will be published.

Questions may be referred to:

Winfield Liu  
Senior Legal Counsel, Market Regulation  
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wliu@osc.gov.on.ca

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**BY DELIVERY AND  
ELECTRONIC FILING**

Ontario Securities Commission  
20 Queen Street West, Suite 1903  
Toronto, Ontario M5H 3S8  
Attention: Secretary to the Commission

**Re: Application of FundSERV Inc. requesting to be recognized as a clearing agency under the Securities Act (Ontario)**

Dear Sirs/Mesdames:

FundSERV Inc. ("**FundSERV**"), a Canadian corporation with its head office located in Toronto, Ontario, is hereby applying to the Ontario Securities Commission (the "**Commission**") for an order (the "**Order**"), pursuant to Section 147 of the Securities Act (Ontario) (the "**Act**"), recognizing FundSERV as a clearing agency in Ontario under subsection 21.2(0.1)(1).

FundSERV is a leading provider of electronic business services to the Canadian investment industry. Established in 1993 (with active encouragement from the Commission), FundSERV operates on a cost-recovery basis, serving more than 700 organizations and their business units and providing online access to over 10,000 investment instruments. FundSERV also supports the customer staffed committees and working groups that address issues and develop electronic data and security standards for the industry.

FundSERV does not believe it is, or should be viewed as, a clearing agency in the conventional sense. Rather, it operates a value-added network with a variety of application services for business-to-business transaction processing. The core service is to provide the network infrastructure for its customers to place and reconcile their orders through efficient, secure data exchange, and for those who so elect, to enable them to settle their orders through a payment exchange handled by the Royal Bank of Canada through the Large-Value Transfer System ("**LVTS**") operated by the Canadian Payments Association.

FundSERV is dedicated to meeting the needs of all participants in the investment industry. Its data standards and security infrastructure enable the industry to continue to apply technology for the ultimate benefit of the Canadian investing public. Through efficient, secure data exchange, customers have the ability to place, reconcile and net settle orders.

FundSERV's business model does not involve credit enhancement, the assumption of counter-party risk, novation or custody. Rather, its service is similar to other back-office suppliers and service bureaus, facilitating common standards and providing communications infrastructure through which its participants' data flows. It is neither the author, auditor nor guarantor of such data (or the resulting transactions). As noted below, participants may (and do) choose alternative arrangements.

Among other things, Commission Staff Notice 24-702 Regulatory Approach to Recognition and Exemption from Recognition of Clearing Agency dated March 19, 2010 requires FundSERV to describe how it satisfies the specific criteria outlined in Appendix A thereof which are relevant to FundSERV's activities in Ontario. Accordingly, FundSERV has reproduced below the criteria in *italics*, followed by a description of how FundSERV satisfies each criterion or why the criterion is not relevant to FundSERV because of the nature and scope of its activities in Ontario.

**PART 1 GOVERNANCE**

1.1 *The governance structure and governance arrangements of the clearing agency ensures:*

- (a) *effective oversight of the clearing agency;*
- (b) *the clearing agency's activities are in keeping with its public interest mandate;*
- (c) *fair, meaningful and diverse representation on the governing body (Board) and any committees of the Board, including a reasonable proportion of independent directors;*
- (d) *a proper balance among the interests of the owners and the different entities seeking access (participants) to the clearing, settlement and depository services and facilities (settlement services) of the clearing agency;*
- (e) *the clearing agency has policies and procedures to appropriately identify and manage conflicts of interest;*

- (f) *each director or officer of the clearing agency, and each person or company that owns or controls, directly or indirectly, more than 10 percent of the clearing agency is a fit and proper person; and*
- (g) *there are appropriate qualifications, limitation of liability and indemnity provisions for directors and officers of the clearing agency.*

Extensive information concerning FundSERV's structure and governance is available on its website ([www.fundserv.com](http://www.fundserv.com)). The following summarizes and amplifies elements thereof.

FundSERV is a Canadian corporation incorporated in 1997. It is owned by 10 shareholders (not one of which owns more than 10% of the outstanding shares of the corporation). Specifically, FundSERV's Board is comprised of representatives of some of the largest mutual fund manufacturers in Canada (AGF Management Ltd., Fidelity Investments Canada ULC, Franklin Templeton Investments Corp. and Invesco Trimark Ltd.). Other Board members are representatives of some of the largest integrated fund manufacturers/distributors in Canada (C.I. Investments Inc., CIBC Asset Management Inc. and Goodman and Company Investment Counsel Ltd.). Another is involved in fund manufacturing and distribution as well as life insurance (MacKenzie Financial Corporation). A service provider (International Financial Data Services (Canada) Limited) represents the interests of its customers (primarily small to medium sized manufacturers). Finally, IROC represents the interests of distributors. The composition of the Board reflects FundSERV's history and ownership structure. Our Board consists of nominees from these 10 shareholders, up to four independent directors chosen by the shareholders on recommendation of the Human Resources and Governance Committee ("**HRGC**") (which also assesses their independence on a case-by-case basis) and the CEO. All directors must meet qualification and conflict of interest criteria defined in FundSERV's by-laws, and they are protected in part by limitations of liability, indemnification, and insurance coverage.

The owners, on recommendation of the Board, determined in 2004 that the input of independent directors would enhance FundSERV's governance structure and help ensure that the interests of different participants are addressed. One independent position is currently vacant by design. Only the four independents are remunerated; the 10 shareholder representatives are not compensated for their services.

The primary manner in which stakeholder interests are addressed is through FundSERV's customer-driven operational committee structure. Participation on such committees is open to all customers.

Our mission is "To provide reliable and resilient value-added network and application services for B2B initiatives that minimize risk and promote timely, automated interactions that reduce cost within the Canadian investment industry". The bulk of our work is driven by our Standards Steering Committee ("**SSC**") and Mandatory Standards Committee ("**MSC**"). The SSC is established by the Board of Directors to advise the corporation on the strategic direction of workflow management, systems and related standards for business transactions that would benefit from standardization. The SSC utilizes an evaluation model to select, review and prioritize new initiatives. The SSC has the authority to establish working committees as circumstances dictate. The SSC reports to the Board of Directors, and consists of 20-25 members who are industry experts and/or subject matter experts and who are able to effect change at their own organizations. The SSC ensures the interests of different participants (fund manufacturers, dealers, brokers, regulators, etc) are met. The HRGC of the Board (which includes two independent directors) ensures each director and officer is a fit and proper person by seeking a mix of competencies, commitment, and independent judgment that will enhance the effectiveness of the Board. Employees and internal officers are subject to background screening, including credit checks, reference checks, criminal checks, education verification and verification of past employment. Our shareholders perform their own checks for their nominees to the Board.

The purpose of the HRGC, in part, is to:

- identify individuals qualified to become Board members, consistent with criteria approved by the Board;
- recommend to the Board the persons to be nominated for election as directors at any meeting of shareholders and the persons (if any) to be elected by the Board to fill any vacancies on the Board; and
- recommend to the Board the directors to be appointed to each committee of the Board.

FundSERV has policies and procedures in place to identify and manage conflicts of interest. Codes of Conduct (the "**Codes**") set forth legal and ethical standards of conduct for directors, officers and employees. The Codes are intended to deter wrongdoing and to promote the conduct of all business in accordance with high standards of integrity and in compliance with all applicable laws and regulations. They further outline the high standards by which personnel are expected to conduct themselves in order to provide a positive work environment in which all parties can achieve maximum productivity and job satisfaction.

The management team focuses on running the business and meets frequently to discuss organizational, operational and other corporate matters. FundSERV's internal operational projects are overseen by the project control board ("**PCB**"), which is the

semi-monthly forum where projects are tracked and presented to executives and senior management for review and decision making. All project managers are required to attend and report on each of their projects according to the project scope and impact. Once a month, a Project Scorecard is produced summarizing status, issues, budget and future tasks for each project. PCB members include the executive team (CEO, CFO and CIO), and 6 senior managers from both the IT and business divisions.

## **PART 2 FEES**

2.1 *All fees imposed by the clearing agency are equitably allocated. The fees do not have the effect of creating unreasonable barriers to access.*

2.2 *The process for setting fees is fair and appropriate, and the fee model is transparent.*

FundSERV operates on a cost recovery basis, whereby any surplus is refunded pro rata to customers via an annual rebate. FundSERV has never paid, and does not foresee paying in the future, a dividend to its shareholders. All paid customers, whether they are owners or not, pay fees according to the same fee schedule and are entitled to a pro-rata rebate on the same basis.

Our 2010 revenue was \$27.7M with a \$7.4M rebate to customers based on usage (net \$20.3M). FundSERV has benefited from consistent revenues and margins by utilizing a cost-based fee structure. With prudent management of our expenditures, our fees provide an adequate working capital cushion. This fee structure achieves the following objectives: i) it is fair and equitable to any and all customers, ii) it allows us to attract as many participants as possible without being exclusionary, iii) it enables us to weather cyclical market fluctuations, and iv) it avoids us having to seek funding or capital from shareholders or customers.

Participation in FundSERV is voluntary. As 50% of the market has chosen alternative processing solutions, this fee structure is regularly reviewed with a view to determining whether and how FundSERV might attract a greater customer mass to reduce industry costs and risks, to increase capacity, and to ensure a dynamic customer-driven standard-setting process.

The Board of FundSERV periodically reviews fee structures. Fees were last revised by the Board of Directors in 1998, after consultation with the SSC. FundSERV has a standard participant agreement which includes the fee schedule and provides a complete list of all fees and other charges imposed for use of its services. FundSERV provides 90 days advance notice, in writing, of any changes to such fees or charges to users/subscribers prior to their implementation.

Since 1998, FundSERV has added many services at no incremental costs to customers, including non-financial updates (NFUs), fund set-up file automation (FD file), PKI FundPORTAL/FundSERV Connect security, N\$M service via LVTS, alternative products (hedge funds, segregated funds, principal-protected notes), flexible settlement dates, XML file formats, client automation, business continuity planning including redundant network routers and connections for customers and FundCOM web-based inquiry. Rather than altering the fees charged to customers, FundSERV has varied the rebates. As a result, net fees are variable, and are based on FundSERV's expenses.

The use of a transactional based fee model with a no annual license fee ensures accessibility to all participants wishing to use FundSERV's services regardless of the number of transactions processed per month. The model is transparent and there are no hidden charges.

## **PART 3 ACCESS**

3.1 *The clearing agency has appropriate written standards for access to its services.*

3.2 *The access standards and the process for obtaining, limiting and denying access are fair and transparent. A clearing agency keeps records of*

(a) *each grant of access including, for each participant, the reasons for granting such access, and*

(b) *each denial or limitation of access, including the reasons for denying or limiting access to an applicant.*

FundSERV is a network providing access to participants rather than an intermediary to any transactions. The terms and conditions for access are specified to both customers and vendors prior to joining FundSERV. In summary, the basic access conditions include network connectivity testing as well as banking tests and regulatory checks. We also have established rules for the layout of transactions flowing through the network (we do not regulate the content). FundSERV does not put up capital to support financial transactions.

FundSERV is open to any customer (including certain sponsored foreign participants) who can meet our technical standards, thereby decreasing system risk and advancing the industry goal of decreasing processing time, cost and risk. Offshore funds

are distributed through Canadian dealers' back offices. The dealers are responsible for ensuring offshore funds are sold to appropriate investors (eg: non-Canadians). We require an onshore sponsor to be responsible for the settlement obligation of the foreign participant due to time zone differences. We review all participant's regulatory registration annually to ensure good standing. As an inclusive community, we meet the needs of many participants in both regulated and unregulated marketplaces, including offshore funds, segregated product, hedge funds and structured product such as principal-protected notes. Maintaining the integrity of our system is paramount when potential customers join to use our services.

The overwhelming majority of participants are regulated. The exceptions are certain segregated fund dealers (managing general agents or MGAs) where, we understand that regulatory initiatives are currently underway to extend regulation to such distributors as well. Acceptable domestic regulators include OSFI, each of the provincial/territorial securities regulators, IIROC and the MFDA. For foreign participants, FundSERV obtains written confirmation of good-standing from their domestic regulator, as well as an agreement from their Canadian sponsor, assuming responsibility for the foreign-based entity's settlement obligations in the event of non-payment. Likewise, for the MGAs noted above, FundSERV obtains written confirmation from their insurance carrier as to its responsibility for managing its distribution partners. Via the customer contract, participants represent they are in compliance with applicable regulatory requirements each and every time they utilize FundSERV's services. FundSERV further monitors regulatory websites and subscribes to the notification lists of the MFDA, IIROC, OSFI and the various provincial/territorial securities regulators for any relevant notices that could impact or alter the status of its customers.

As noted above, each participant signs a standard agreement which sets forth the terms for access, term and termination, fees, warranties, limitation of liability, client's responsibilities and data confidentiality, indemnification, and excusable delays. Each participant goes through documented training and testing/acceptance phases before going live on the network. Once live, their status is available to the community through an online directory. FundSERV has not denied or limited access to any applicant.

Most terminations have been initiated upon receipt of a written request from a customer and are effected in an orderly manner. Some notifications are received from regulators (or by FundSERV's monitoring of regulatory actions (e.g., cease trade orders or bankruptcies)). Where appropriate, FundSERV removes any pending trades and settlements. FundSERV initiated terminations have historically been limited to non-payment of invoices and only in the case of inactive customers. For active customers, these are generally rectified after one or more requests for payment by FundSERV.

FundSERV has a dominant but not exclusive market share for third party retail funds, which, in turn, constitutes approximately 50% of the market (with bank and proprietary funds and distribution channels constituting the other half of the market).

FundSERV has moved beyond servicing the 'plain vanilla' mutual fund market by addressing the investment fund industry's need for alternative products. With a mandate to reduce time, cost and risk of customer processing, we have started to also focus on other markets such as GICs. Despite being owned predominantly by fund companies, recent business initiatives such as GICSERV have been driven by distributors. In fact, much of FundSERV's current and future standards' (GICSERV) development will be for the benefit of the industry at large, and not the originating fund company shareholders. The inclusivity of access to FundSERV and our operational efficiency has encouraged non-traditional customers to seek out FundSERV to resolve their processing inefficiencies.

#### **PART 4 RULES AND RULEMAKING**

- 4.1 *The clearing agency's rules are designed to govern all aspects of the settlement services offered by the clearing agency, and*
  - (a) *are not inconsistent with securities legislation,*
  - (b) *do not permit unreasonable discrimination among participants, and*
  - (c) *do not impose any burden on competition that is not necessary or appropriate.*
- 4.2 *The clearing agency's rules and the process for adopting new rules or amending existing rules should be transparent to participants and the general public.*
- 4.3 *The clearing agency monitors participant activities to ensure compliance with the rules.*
- 4.4 *The rules set out appropriate sanctions in the event of non-compliance by participants.*

FundSERV operates a \$20M enterprise with a staff complement of approximately 80 employees. Much of our success and efficiency is directly attributable to our many industry volunteers. Despite being a small organization in terms of headcount, we rely on volunteers who are industry experts and/or subject matter experts to promote the efficient and timely development of standards to keep industry costs low. Annual costs of at least \$300 million are currently being removed from the industry due to FundSERV's standards.

FundSERV's greatest asset is our community of users. FundSERV is effectively the investment industry's central meeting place – fostering collaboration and ease of doing business. Our customers, via an effective and transparent standard-setting process, direct FundSERV's development. The business model relies heavily on industry volunteers, who collectively spend hundreds of hours advancing our 'open access' model. FundSERV draws on the resources of the industry and thus is effectively run by the industry.

A release of our standards takes a minimum of 16 months. The process starts with requirements going to the SSC until March, SSC approval in April, requirements documented usually by June, technical and industry review by July, standards published in October, development/QA testing until the following March, industry testing from April until June and finally implementation in mid June. All participants (and their vendors) are invited and encouraged to participate in the technical review, industry review, and industry user acceptance testing (“UAT”). Formal comment periods exist for all participants.

When implementing the standards, we first solicit topics for inclusion from the industry, establish working groups, develop requirements, send requirements out for review to the entire industry, begin development and ensure adequate time for customer testing and acceptance and implementation. Our entire standards handbook is available on the internet to all authorized participants.

While the Board sets strategy and monitors performance, the SSC selects projects and approves standards. The SSC consists of members who are industry experts and/or subject matter experts and who are able to effect change at their own organizations. Further committees include the MSC (to enforce standards adherence) and the Technical Advisory Committee (to provide recommendations on security, infrastructure and development). These committees are complemented by working groups who develop detailed specifications.

FundSERV issues a bulletin to its entire customer base seeking interested parties to apply to serve on the SSC. An ad-hoc committee of the SSC reviews applications received, conducts interviews where appropriate, and recommends new members, which are then voted on by the existing SSC. Criteria for selection include relevant industry knowledge, ability to represent their constituents and ensuring that FundSERV's diverse customer base is fully represented.

FundSERV has established a set of standard rules for processing, and standardized agreements with all participants to ensure transparency. All participants have the same access to services and support at no additional cost.

FundSERV is solely a carrier of electronic data and does not hold funds nor manage accounts on behalf of clients, it does not provide centralized facilities for the clearing of trades in securities, nor does it act as a depository of securities. While monitoring is electronic, it focuses on data format integrity by highlighting irregularities, rejects, connectivity concerns, etc. Participants are provided with a phone number to contact FundSERV to anonymously report customers who are not adhering to standards. There are financial penalties for those participants not adhering to standards or missing deadlines for transmitting file data. Such penalties are not to the benefit of FundSERV (as any penalties collected are rebated back to the industry at large without factoring into the payor participants pro-rata share), but are in place to deter non-conformance to industry-agreed standards that ultimately impact other participants.

FundSERV has never invoked its right to suspend or terminate for non-compliance. To date, suasion has proven sufficient.

## **PART 5 DUE PROCESS**

5.1 *For any decision made by the clearing agency that affects an applicant or a participant, including a decision in relation to access, the clearing agency ensures that:*

- (a) *applicant or a participant is given an opportunity to be heard or make representations; and*
- (b) *the clearing agency keeps a record of, gives reasons for, and provides for appeals or reviews of, its decisions.*

If any participant materially or repeatedly defaults in performing its duties or obligations described in the FundSERV Agreement, the agreement provides the participant with 30 days to resolve the situation. FundSERV keeps written records detailing the actions taken and subsequent decisions. To date, compliance by suasion has proven effective. If suspension or termination were to be invoked, or reinstatement denied, there would be a right of appeal to FundSERV's Board of Directors.

For instances where participants do not use the electronic processing standards deemed mandatory by the SSC, they are entitled to appeal to the Mandatory Standards Appeals Committee, a sub-committee of the Board. Ultimately, there is little benefit to the industry at large if customers are removed due to non-conformance. In fact, this has never occurred, as FundSERV instead uses suasion rather than financial penalty to ensure cooperative adherence to standards by all participants.

## PART 6 RISK MANAGEMENT

- 6.1 *The clearing agency's settlement services are designed to minimize systemic risk.*
- 6.2 *The clearing agency has appropriate risk management policies and procedures and internal controls in place.*
- 6.3 *Without limiting the generality of the foregoing, the clearing agency's services or functions are designed to achieve the following objectives:*
1. *Where the clearing agency acts as a central counterparty, it rigorously controls the risks it assumes.*
  2. *The clearing agency minimizes principal risk by linking securities transfers to funds transfers in a way that achieves delivery versus payment.*
  3. *Final settlement occurs no later than the end of the settlement day. Intraday or real-time finality is provided where necessary to reduce risks.*
  4. *Where the clearing agency extends intraday credit to participants, including a clearing agency that operates net settlement systems, it institutes risk controls that, at a minimum, ensure timely settlement in the event that the participant with the largest payment obligation is unable to settle.*
  5. *Assets used to settle the ultimate payment obligations arising from securities transactions carry little or no credit or liquidity risk. If central bank money is not used, steps are to be taken to protect participants in settlement services from potential losses and liquidity pressures arising from the failure of the cash settlement agent whose assets are used for that purpose.*
  6. *If the clearing agency establishes links to settle cross-border trades, it designs and operates such links to reduce effectively the risks associated with cross-border settlements.*
- 6.4 *The clearing agency engaging in activities not related to settlement services carries on such activities in a manner that prevents the spillover of risk to the clearing agency that might affect its financial viability or negatively impact any of the participants in the settlement service.*

While FundSERV does not perform core clearing agency functions, it recognizes the need for proper risk management and maintains a risk assessment process to identify and manage risks. FundSERV has a 'public company' mindset despite its private company status. For example, the Board's Audit/Finance/Risk Committee (chaired by an independent director) meets at least quarterly. At the management level, FundSERV periodically conducts an independent enterprise risk management ("ERM") assessment to identify, assess and mitigate risks. The ERM assessment was first conducted to respond to general business demands for more diligent and robust risk mitigation capabilities. It is intended to educate and raise awareness for both management and the Board by reviewing and reporting on the critical risks and opportunities facing FundSERV. In addition, our controls are audited annually under Section 5970 of the Canadian Institute of Chartered Accountants ("CICA") Handbook ("Section 5970") standards, while our financial results are also audited annually.

To support the independent ERM assessment noted above, FundSERV established an internal risk management committee ("RMC"). On a quarterly basis (or more frequently if required) the RMC identifies, assesses, mitigates and reports on current and future risk events and remediation efforts to the Board's Audit/Finance/Risk committee. Composed of senior management personnel, the RMC has concluded that our primary risk is ensuring the availability of our network and application services.

Availability of our network and application services was recognized by our Board as our *raison d'être* and thus embedded into the organization's mindset when 'reliable and resilient' were added to our mission statement as follows: "To provide reliable and resilient value-added network and application services for B2B initiatives that minimize risk and promote timely, automated interactions that reduce cost within the Canadian investment industry". FundSERV has developed and currently maintains a robust and reliable business continuity program that ensures the availability of people, services and technology. We are capable of fully operating from both our Toronto or Mississauga locations and conduct industry wide business continuity exercises annually to ensure all customers are both capable and vigilant of industry continuance in the event of an outage. In addition, participants can always transact without FundSERV's assistance. FundSERV's internal Business Continuity Plan ("BCP") Steering Committee assesses the business continuity management profile for the organization and decides on improvement actions that need to be acted upon in a timely manner, providing a forum to ensure that there is clear direction and visible management support for business continuity initiatives. The BCP Steering Committee members include the executive team (CEO, CFO and CIO), and 4 senior managers from both the IT and business divisions.

FundSERV's Net Settlement Messaging ("NSM") service facilitates the exchange of customer net settlement payment messages. Payments from customers in a net payable position are directed to those in a net receivable position through Royal

Bank via LVTS for Canadian dollar amounts and the Fedwire for US dollar amounts. N\$M is completely redundant, with backup facilities at the desktop, site, and network levels. The mechanics involved with calculating net settlement amounts centre around data provided by participants. Trade and settlement dates for data provided to FundSERV by distributors are calculated based on the corresponding fund profile provided by manufacturers. All calculations use the settlement instruction records returned by the fund companies. FundSERV does not carry out any calculations to determine the individual settlement amount for any trade or commission related transaction.

Every participant in a net payable position must pay the full amount provided to them, even if they believe the amount to be incorrect. A participant that disputes the amount payable must still pay the full amount to FundSERV. After the participant has paid the full amount, the problem can be resolved in one of two ways: the participant can deal directly with the counterparty or the participant can settle within N\$M on a subsequent settlement date when the manufacturer submits amending contracts. The transaction goes in as a late settlement.

Default risk is significantly mitigated using the N\$M model – FundSERV ensures that all monies are collected from customers in the morning before authorizing the release of funds in the afternoon to those customers receiving monies. FundSERV has a small line of credit to deal with the occasional minor discrepancy; however, in recent years, it has never been used. FundSERV does not fund any customers; instead we have a robust process to back-out any failing party and rerun the settlement process for the industry. Instead of funding a failed payment, we remove the failing customer and recalculate payment totals. In short, FundSERV facilitates the settlement process; payments are not made by FundSERV.

Although we are prepared to deal with a customer default scenario and have plans in place to avoid such payment failures, it is not a significant concern as evidenced by past experience. Payment failures are extremely rare in occurrence, and no adverse consequence has ever arisen. When participants fail to make a payment we remove them. Based on past experience and the current complement of controls and mitigation processes, our likelihood assessment is that a significant adverse consequence would not occur.

The controls surrounding N\$M are multi-faceted. Roles are segregated to ensure customer bank account setup, deletion and changes are authorized and validated. Staff with authorization to release payments are authorized by personnel outside of the finance area. Two personnel are required to authorize the release of any payment to customers in a receivable position. All monies are held in accounts designated as in-trust. In addition, insurance is maintained.

Overall, controls provide reasonable assurance that client access to FundSERV's core applications and data is restricted and set up based on authorized service agreements. Controls within FundSERV's core applications provide reasonable assurance that client transactions, as authorized by clients, are processed and executed. Controls provide reasonable assurance that changes to the existing FundSERV core applications are authorized, tested, approved, properly implemented and documented.

FundSERV maintains approximately \$27 million of P&C insurance, \$5 million of E&O insurance and \$25 million of D&O insurance. It also maintains a Financial Institution Bond for \$100 million (\$50 million per occurrence).

**PART 7 SYSTEMS AND TECHNOLOGY**

7.1 *For its settlement services systems, the clearing agency:*

- (a) *develops and maintains,*
  - (i) *reasonable business continuity and disaster recovery plans,*
  - (ii) *an adequate system of internal control,*
  - (iii) *adequate information technology general controls, including controls relating to information systems operations, information security, change management, problem management, network support, and system software support;*
- (b) *on a reasonably frequent basis, and in any event, at least annually, and in a manner that is consistent with prudent business practice,*
  - (i) *makes reasonable current and future capacity estimates,*
  - (ii) *conducts capacity stress tests to determine the ability of those systems to process transactions in an accurate, timely and efficient manner,*
  - (iii) *tests its business continuity and disaster recovery plans; and*

(c) promptly notifies the regulator of any material systems failures.

7.2 The clearing agency annually engages a qualified party to conduct an independent systems review and prepare a report in accordance with established audit standards regarding its compliance with section 7.1(a).

FundSERV has built a reliable hub and spoke network that is widely acknowledged to be the most efficient investment fund transaction processing system. This centralized hub has both direct and web-based connections. As described in the previous section, FundSERV has developed and currently maintains a robust and reliable business continuity program that ensures the availability of people, services and technology in the event of a catastrophe or pandemic. We are capable of fully operating from either or both of our Toronto or Mississauga locations and conduct industry wide business continuity exercises annually to ensure all customers are both capable and vigilant of industry continuance in the event of an outage. The alternate data and operations facility allows rapid (less than 30 minutes) switching of operations to this secondary data centre should the primary data centre experience a disaster. In the event of a business disruption, this near-real time data replication will let clients immediately resume business operations. The secondary data centre has been in place since 2005. We operated completely from our secondary site (which has workspace for over 50 people) as recently as November 2011 as a planned exercise to demonstrate our capability of servicing the industry. The next such exercise is scheduled to occur in September 2012. All business continuity related systems are tested yearly and are included in the annual Section 5970 audit report.

FundSERV's information technology department deploys a wide range of automated tools that continually monitor capacity, queues, system performance, response times and similar matters. This electronic monitoring system also generates emails to a wide range of staff advising of warnings and errors. FundSERV provides the following information technology services for its customers:

- Information Systems Function Management
- Systems Development and Maintenance
- Computer Security
- Computer Operations
- Business Continuity Management
- Physical and Environmental Security
- Identification and Authentication Security

The IT risk management committee is responsible for ensuring that IT risk is addressed and effectively managed so as to maintain an acceptable level of control and assurance. The committee evaluates and assesses the level of risk to the infrastructure and ensures that the appropriate action is taken to mitigate identified risks.

FundSERV's internal change advisory board ("CAB") ensures that all FundSERV changes are assessed and prioritized prior to being implemented into production. The approval process includes ensuring that the change has been properly documented, resourced and scheduled with a communication and back out plan if applicable. All changes that could impact FundSERV's customers or production infrastructure must be approved by CAB before being implemented. CAB has representation from both FundSERV's technical and business management areas.

Our infrastructure operates FundSERV's proprietary workflow management applications that have real-time, batch or web interfaces. FundSERV standards and business processing rules are defined by customers and are contractually protected, thereby ensuring consistent processes across the entire industry and a central source for common reference data.

## **PART 8 FINANCIAL VIABILITY AND REPORTING**

8.1 The clearing agency has sufficient financial resources for the proper performance of its functions and to meet its responsibilities and allocates sufficient financial and staff resources to carry out its functions as a clearing agency in a manner that is consistent with any regulatory requirements.

As noted above (see Part 2), FundSERV's financial flows are relatively simple. We have one single revenue source. Our expenses are categorized as employment, technology, general/admin, or occupancy. The only funds that flow through FundSERV are about \$28 million in gross revenue, of which approximately a third is rebated back to customers based on their pro-rata usage.

The determination of the user rebate is designed to reduce FundSERV's taxable income to zero. Accounting income fluctuates depending on the tax basis of FundSERV's assets. All current and future FundSERV expenditures are funded from operations.

We are currently looking at attracting other products such as GICs to complement our ability to reduce (and spread) processing costs and mitigate the impact of industry volatility. Any such new business, if it materializes, would not be subsidized or otherwise at the expense of our core investment fund offering. The nature of our ownership ensures that we will not lose our focus on servicing our current core customer base.

FundSERV's annual financial statements are audited by PricewaterhouseCoopers LLP and are publically available in our annual report that is distributed to all customers. The integrity of the fee structure and rebate process is vetted via committees and the Board.

## **PART 9 OPERATIONAL RELIABILITY**

9.1 *The clearing agency has procedures and processes to ensure the provision of accurate and reliable settlement services to participants.*

As previously described, FundSERV has developed and currently maintains a robust and reliable business continuity program that ensures the availability of people, services and technology.

The control objectives specified in FundSERV's Section 5970 report meet comparable industry standards. The description of controls is intended to provide our clients, and their auditors, with information about the control environment, practices and policies of FundSERV. The description has been prepared taking into consideration the guidance contained in Section 5970 for audits of controls at a service organization.

Specifically, the control objectives within the Section 5970 report cover:

- core application Services
- Net Settlement Messaging
- the information technology function
- the billing process
- information protection activities

FundSERV's N\$M service ensures that all monies are collected from customers in the morning before authorizing the release of funds in the afternoon to those customers receiving monies. By utilizing the LVTS framework through the Royal Bank, our settlement process provides for:

- a simple process that is controlled by participants
- a process strongly endorsed by the Bank of Canada and the Commission
- finality of payment, and
- a consistent process for Canadian and US dollar payments

Our customers are not required to use the N\$M service – it is an optional service that many of our customers do not avail themselves of. In the rare event of unavailability of N\$M, the industry participants can communicate directly with each other, as is the case for some today.

## **PART 10 PROTECTION OF ASSETS**

10.1 *The clearing agency has established accounting practices, internal controls, and safekeeping and segregation procedures to protect the assets that are held by the clearing agency.*

FundSERV is a communications network. Securities and cash are not held nor exchanged by FundSERV on behalf of participants.

**PART 11 OUTSOURCING**

11.1 *Where the clearing agency has outsourced any of its key functions, it has appropriate and formal arrangements and processes in place that permit it to meet its obligations and that are in accordance with industry best practices. The outsourcing arrangement provides regulatory authorities with access to all data, information, and systems maintained by the third party service provider required for the purposes of regulatory oversight of the agency.*

FundSERV does not have any material outsourcing agreements.

**PART 12 INFORMATION SHARING AND REGULATORY COOPERATION**

12.1 *For regulatory purposes, the clearing agency cooperates by sharing information or otherwise with the Commission and its staff, self-regulatory organizations, exchanges, quotation and trade reporting systems, alternative trading systems, other clearing agencies, investor protection funds, and other appropriate regulatory bodies.*

FundSERV is transparent to the industry (see [www.fundserv.com](http://www.fundserv.com)) and fully responsive to any information request from the Commission. It commits to ongoing cooperation with the Commission and is committed to share information with the Commission and its staff, and, as appropriate, other regulatory bodies and will cooperate with recognized or exempt clearing agencies at the direction of the Commission, subject to applicable privacy or other laws governing the sharing of information and the protection of personal information.

**SUBMISSION**

FundSERV submits that it is not a clearing agency in the conventional sense, nor does it give rise to systemic risk concerns. Rather, FundSERV provides the network infrastructure for its customers to place and reconcile orders through efficient, secure data exchange and, for those who so elect, to enable them to settle orders through a payment-exchange handled by the Royal Bank of Canada through the Large-Value Transfer System operated by the Canadian Payments Association. The nature of FundSERV's business model (which does not involve credit enhancement, the assumption of counter-party risk, novation or custody) as well as the level of transparency and cooperation which FundSERV has always maintained with the Commission will be formalized under the proposed Order.

We enclose a cheque in the amount of \$5,250, payable to the Commission, representing the fee payable for this application.

Yours truly,

Brian Gore  
President & CEO

**Appendix A**

**IN THE MATTER OF  
THE SECURITIES ACT  
R.S.O. 1990, CHAPTER S.5  
AS AMENDED (Act)**

**AND**

**IN THE MATTER OF  
FUNDSERV INC.**

**ORDER  
(Section 21.2)**

**WHEREAS** FundSERV Inc. (FundSERV) had filed an application dated February 13, 2012 (Application) with the Ontario Securities Commission (Commission) pursuant to section 21.2 of the Act requesting an order recognizing FundSERV as a clearing agency.

**AND WHEREAS** FundSERV has represented to the Commission that:

1. FundSERV is a Canadian corporation with its head office located in Toronto, Ontario;
2. FundSERV is a provider of electronic business services to the Canadian investment industry;
3. FundSERV's core service is to provide the network infrastructure for its customers to place and reconcile orders through efficient, secure data exchange;
4. FundSERV provides centralized payment exchange facilities (clearing agency services), for those customers who so elect, to settle orders, on a net basis, through payment exchange currently handled by a Canadian chartered bank utilizing the Large Value Transfer System operated by the Canadian Payments Association;
5. FundSERV's business model does not involve credit enhancement, the assumption of counter-party risk, novation or custody;
6. FundSERV operates on a cost-recovery basis, serving more than 700 organizations and their business units and providing online access to over 10,000 investment fund instruments;
7. While FundSERV has developed business continuity systems, market participants can and do transact without FundSERV's assistance; and
8. FundSERV also supports the customer staffed committees and working groups, that include users of the clearing agency services, that address issues and develop electronic data and security standards for the industry;

**AND WHEREAS** the Commission considers it appropriate to set out in an order the terms and conditions for the recognition of FundSERV as a clearing agency, which terms and conditions are set out in Schedule "A" attached;

**AND WHEREAS** FundSERV has agreed to the terms and conditions as set out in Schedule "A";

**AND WHEREAS** based on the Application and the representations FundSERV has made to the Commission, the Commission is satisfied that granting an order would not be prejudicial to the public interest;

**THE COMMISSION HEREBY RECOGNIZES** FundSERV as a clearing agency pursuant to section 21.2 of the Act, subject to the terms and conditions set out in Schedule "A";

**DATED** February \_\_\_\_, 2012

**SCHEDULE "A"**

**FUNDSERV INC.**

**TERMS AND CONDITIONS**

**GOVERNANCE**

1. FundSERV's governance arrangements will be designed to promote the objectives of the users (participants) of its services and its shareholders.
2. Without limiting the generality of the foregoing, FundSERV's governance structure and governance arrangements will ensure:
  - (a) effective oversight of FundSERV;
  - (b) FundSERV takes into consideration the public interest ;
  - (c) fair, meaningful and diverse representation on the Board and any committees of the Board, including a reasonable proportion of independent directors;
  - (d) FundSERV's Board has the capacity to effectively consider the interests of FundSERV's various stakeholders;
  - (e) FundSERV has policies and procedures to appropriately identify and manage conflicts of interest;
  - (f) each director or officer of FundSERV, and each person or company that owns or controls, directly or indirectly, more than 10 percent of FundSERV is a fit and proper person; and
  - (g) there are appropriate qualifications, limitation of liability and indemnity provisions for directors and officers of FundSERV.
3. FundSERV will not, without the Commission's prior written approval, make significant changes to its governance structure or constating documents.

**FEES**

4. Fees imposed by FundSERV for the clearing agency services will be equitably allocated. The fees will not have the effect of creating unreasonable barriers to access.
5. The process for setting such fees will be fair and the fee model will be transparent.

**ACCESS**

6. FundSERV will have transparent written standards for access to its clearing agency services.
7. The access standards and the process for granting, limiting or denying access to the clearing agency services will be fair and transparent. FundSERV will keep records of
  - (a) each grant of access, and
  - (b) each denial or limitation of access, including the reasons for denying or limiting access to an applicant.

**RULES AND RULEMAKING**

8. FundSERV will establish rules that are necessary or appropriate to govern the clearing agency services it offers.
9. FundSERV will ensure that its rules relating to the clearing agency services
  - (a) are not inconsistent with securities legislation,
  - (b) do not permit unreasonable discrimination among participants, and

- (c) do not impose a burden on competition that is not necessary or appropriate.
- 10. FundSERV will submit its rules for approval in accordance with the rule protocol attached as Appendix "A" to this Schedule "A", as amended from time to time.
- 11. FundSERV's rules and the processes for adopting new rules or amending existing rules will be transparent to participants.
- 12. FundSERV will monitor participant activities to ensure compliance with such rules. Such rules will set out appropriate sanctions in the event of non-compliance by participants.

**DUE PROCESS**

- 13. For any decision made by FundSERV that materially affects an applicant or a participant in respect of the clearing agency services, including a decision in relation to access, FundSERV will ensure that:
  - (a) an applicant or a participant is given an opportunity to be heard or make representations; and
  - (b) FundSERV keeps a record of, gives reasons for, and provides for appeals or reviews of, its decisions.

**RISK MANAGEMENT**

- 14. FundSERV will maintain appropriate risk management policies and procedures.
- 15. FundSERV will carry its activities that do not relate to the clearing agency services in a manner that minimizes the spillover of risk that might adversely affect its financial viability or operations or negatively impact any of its participants.

**SYSTEMS AND TECHNOLOGY**

- 16. For its systems, FundSERV will:
  - (a) develop and maintain,
    - (i) reasonable business continuity and disaster recovery plans,
    - (ii) an adequate system of internal control,
    - (iii) adequate general computer controls, including controls relating to information systems operations, information security, change management, problem management, network support, and system software support;
  - (b) on a reasonably frequent basis, and in any event, at least annually, and in a manner that is consistent with prudent business practice,
    - (i) make reasonable current and future capacity estimates,
    - (ii) conduct capacity stress tests to determine the ability of those systems to process transactions in an accurate, timely and efficient manner,
    - (iii) test its business continuity and disaster recovery plans; and
  - (c) promptly notify the Commission staff of any material systems failures.
- 17. FundSERV will annually engage a qualified party to conduct an independent systems review and prepare a report in accordance with established audit standards regarding its compliance with section 16(a) and such report will be provided to Commission staff.

**FINANCIAL VIABILITY AND REPORTING**

- 18. FundSERV will maintain sufficient financial resources to meet its responsibilities and allocate sufficient financial and staff resources to carry out its clearing agency services.

19. FundSERV will provide to Commission staff unaudited quarterly financial statements within 60 days of each quarter end and audited annual financial statements, together with any annual report to the shareholders and participants, within 145 days of each year end.
20. If FundSERV fails to maintain, or anticipates that it will fail to maintain a cash and accounts receivable balance equal to or greater than four months of expenses, it shall immediately notify Commission staff and advise what steps are being taken to address the situation.

**OUTSOURCING**

21. Where FundSERV decides to outsource any of its functions supporting or critical to its clearing agency services, it will have appropriate and formal arrangements and processes in place that permit it to meet its obligations in the provision of the clearing agency services and under this Order, and which are in accordance with industry best practices.
22. The outsourcing arrangement shall provide Commission staff with access to all data, information, and systems maintained by the third party service provider required for the purposes of regulatory oversight.

**INFORMATION SHARING AND REGULATORY COOPERATION**

23. FundSERV will provide such information as may be reasonably requested from time to time by, and otherwise cooperate with, the Commission or its staff.
24. Unless otherwise prohibited under applicable law, FundSERV will share information and otherwise cooperate with recognized self-regulatory organizations, investor protection funds, marketplaces, recognized and exempt clearing agencies, and other regulatory bodies as appropriate.
25. FundSERV will comply with Appendix "B" to this Schedule setting out the reporting obligations, as amended from time to time, regarding the reporting of information to the Commission.

APPENDIX "A"

**RULE PROTOCOL REGARDING THE REVIEW AND APPROVAL  
OF FUNDSERV INC. RULES  
BY THE ONTARIO SECURITIES COMMISSION**

**1. Purpose of the Protocol**

On [\_\_\_\_\_, 2012], the Ontario Securities Commission (Commission) issued a recognition order ("Recognition Order") with terms and conditions governing the recognition of FundSERV Inc. (FundSERV) as a clearing agency pursuant to subsection 21.2(1) of the *Securities Act* (Ontario) ("Act"). To comply with the Recognition Order, FundSERV must, among other things, submit its rules to the Commission for approval. This protocol sets out the procedures for the submission of a rule by FundSERV and the review and approval of the rule by the Commission.

**2. Definitions**

In this protocol:

"rule" means any new requirement or an amendment to or deletion of an existing requirement relating to the clearing agency services as defined in the Recognition Order, that would have an impact on FundSERV, its participants, other market participants, or the capital markets in general, relating to:

- (a) Access to the clearing agency services;
- (b) The rights and obligations of FundSERV or participants using the clearing agency services;
- (c) Fees or costs charged to participants for use of the clearing agency services;
- (d) Risks to FundSERV or its participants;
- (e) The process for or the transparency of making rules;
- (f) Competition among participants, other market participants or in the capital markets; or
- (g) Material costs of compliance with the rule.

All other terms have the respective meanings ascribed to them in the Recognition Order and in securities legislation as that term is defined in NI 14-101.

**3. Procedures for Review and Approval of Rules**

**(a) Documents**

For a rule, FundSERV will provide to the Commission, where applicable, the following documents in electronic format or by other means as agreed to by Commission staff and FundSERV from time to time:

- (i) a cover letter that indicates:
  - (a) a description of the rule and its nature and purpose; and
  - (b) a description and analysis of the possible effects of such rule on FundSERV, its participants, other market participants and the capital markets in general, including but not limited to competition, risks and the costs of compliance borne by any of the foregoing parties;
- (ii) the rule and a blacklined version of the rule indicating the proposed changes to an existing rule;
- (iii) the concept and business case; and
- (iv) the cost/benefit analysis.

**(b) Confirmation of Receipt**

Commission staff will within 3 business days send to FundSERV confirmation of receipt of documents submitted by FundSERV under subsection (a).

**(c) Notice of Rules to Participants**

FundSERV will provide notice to participants of any rules with an opportunity to comment and the notice will be posted on the FundSERV website for a period of not less than four (4) weeks.

**(d) Publication of a Rule by the Commission**

If a rule has an impact on market participants (other than FundSERV participants) or the capital markets in general, then Commission staff may require that a notice of rule change and, where applicable, a blacklined version of the rule, be published in the OSC Bulletin or the OSC website for a comment period of not less than four (4) weeks. The notice and accompanying rule will be published as soon as reasonably practicable.

**(e) Review by Commission Staff**

Commission staff will use their best efforts to conduct their initial review of the rule and provide comments to FundSERV within 30 days of FundSERV filing materials with the Commission. However, there will be no restriction on the amount of time necessary to complete the review of the rule.

**(f) FundSERV Responses to Commission Staff's Comments**

FundSERV will respond to any comments received to Commission staff in writing.

**(g) Approval by the Commission**

Commission staff will use their best efforts to prepare the rule for approval by the later of (i) 45 days receipt of the filing of the rule from FundSERV including the filing of all relevant documents in subsection (a) above, and (ii) 30 days after receipt of written responses from FundSERV to staff's comments or requests for additional information, and the summary of industry comments and FundSERV's response to the industry comments (and upon the request of Commission staff, copies of the original comments), or confirmation from FundSERV that there were no comments received. If at any time during the review period, Commission staff determine that they have further comments or require further information from FundSERV in order to prepare the materials for Commission approval, the review period will be extended by an additional period of 21calendar days commencing on the day that Commission staff receive responses to the comments or the information requested. Commission staff will promptly notify FundSERV of the Commission's approval.

**(h) Effective Date of a Rule**

A rule will be effective as of the date of approval by Commission in accordance with subsection (g) or on a date determined by FundSERV, if such date is later.

**4. Immediate Implementation of a Rule**

**(a) Criteria for Immediate Implementation**

FundSERV may make a rule effective immediately where FundSERV determines that there is an urgent need to implement the rule because of a substantial and imminent risk of significant harm to FundSERV, participants, other market participants, or the capital markets.

**(b) Prior Notification**

Where FundSERV determines that immediate implementation is appropriate, FundSERV will advise Commission staff in writing as soon as possible but in any event at least 5 business days prior to the implementation of the rule. Such written notice will include an analysis to support the need for immediate implementation.

**(c) Disagreement on Need for Immediate Implementation**

If Commission staff do not agree that immediate implementation is necessary, the process for resolving the disagreement will be as follows:

- (i) Commission staff will notify FundSERV, in writing, of the disagreement, or request more time to consider the immediate implementation, within 3 business days of being advised by FundSERV under subsection (b).
- (ii) Commission staff and FundSERV will discuss and resolve any concerns raised by Commission staff.
- (iii) If no notice is received by FundSERV by the 3rd business day after Commission staff received FundSERV's notification, FundSERV may assume that Commission staff does not disagree with their assessment.

**(d) *Review of Rule Implemented Immediately***

A rule that has been implemented immediately will be reviewed and approved by the Commission in accordance with the procedures set out in section 3 with necessary modifications. If the Commission subsequently disapproves the rule, FundSERV will immediately repeal the rule and inform its participants of the disapproval.

**5. *Miscellaneous Provisions***

**(a) *Waiving Provisions of the Protocol***

Commission staff may waive any part of this protocol upon request from FundSERV or as determined by Commission staff. Such a waiver must be granted in writing by Commission staff.

**(b) *Amendments***

This protocol and any provision hereof may be amended at any time with the approval of the Commission and FundSERV.

**APPENDIX "B"**

**FUNDSERV INC.**

**REPORTING OBLIGATIONS**

In addition to the notification, reporting and filing obligations set out in Schedule "A" to the Recognition Order, FundSERV will also comply with the reporting obligations set out below.

**1. Prior Notification**

1.1 FundSERV will provide to Commission staff reasonable prior notification of:

- (a) any proposed change to FundSERV's corporate governance structure other than significant changes to the governance structure or constating documents for which prior approval is required under item 3 of Schedule "A" to the Recognition Order;
- (b) entering into an agreement, memorandum of understanding or other similar arrangement with any governmental or regulatory body, self-regulatory organization, clearing agency, stock exchange, other marketplace or market, other than an agreement, memorandum of understanding or similar arrangement for normal commercial purposes; or
- (c) engaging in a new type of business activity or cease to engage in a business activity in which FundSERV is then engaged;

**2. Immediate Notification**

2.1 FundSERV will provide to Commission staff immediate notice of:

- (a) the appointment of any new director or officer, including a description of the individual's employment history; and
- (b) the resignation of a director or officer or the auditors of FundSERV.

2.2 FundSERV will immediately notify Commission staff if it:

- (a) becomes the subject of any order, directive or other similar action of a governmental or regulatory authority;
- (b) becomes aware that it is the subject of a criminal or regulatory investigation; or
- (c) becomes, or is aware that it may become, the subject of a material lawsuit.

**3. Annual Reporting**

3.1 FundSERV will provide to Commission staff annually:

- (a) a list of the directors and officers of FundSERV, and identify which directors are independent;
- (b) a list of the committees of the FundSERV board of directors, setting out the members, mandate and responsibilities of each of the committees;
- (c) a list of all participants in the clearing agency services; and
- (d) FundSERV's annual report.